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*Editors*

# Corporate Ethics and Corporate Governance

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# Introduction to Ethics<sup>1</sup>

*Robert C. Solomon*

## **Ethics: A Briefer Introduction**

Last Thursday, you went out for lunch with an acquaintance from class, a nice-enough fellow but not a candidate for lifelong friendship. As you were wolfing down your last bite of cheeseburger, you suddenly gulped and flushed: you realized that you had forgotten your wallet. You were flat broke. Embarrassed, you entreated your classmate to lend you five dollars, which you would, of course, pay back on Tuesday. Today is Wednesday; you forgot.

Now you are doubly embarrassed, for having had to borrow the money in the first place, for having then forgotten to pay it back when promised. You are tempted, momentarily, to ignore the entire awkward situation, just to assume – what may well be true – that your classmate has forgotten about the loan. (After all, it is only five dollars.) But maybe he hasn't forgotten, or, at least, he'll remember it when he sees you. For an irrational instant, you consider dropping the course, but then you realize that would be ridiculous – the five dollars just isn't that important. It is highly unlikely – it would be very embarrassing for him – that he would actually ask you for the money. Any way, you aren't close friends and don't generally talk to each other. So what's the difference?

But now, small hints of large doubts start interrupting your day. You've made up your mind. You are convinced that no harm will come to you. The fellow knows none of your friends and it is hardly likely that he will announce to the class or put a personal ad in the paper that you are a "deadbeat". And yet, it's ruining your day, and it may well ruin other days. "If only I could get rid of this guilty feeling", you say to yourself. But it is not just a feeling; it is a new and wholly unwelcome sense of who you are. A voice inside of you (sometimes it sounds like your own voice; occasionally it seems to be your mother's) keeps whispering, "deadbeat", "deadbeat" (and worse). Already distracted from your work, you start speculating, "What if we all were to forget about our debts?" Your first response is that you would probably be washing dishes at the Burger Shop, since no one would ever lend anyone money and your classmate would never have lent money

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<sup>1</sup> Published in: Solomon, R.: *Ethics: A Briefer Introduction*. Chapter 1: Introduction to Ethics. Wadsworth 2005. Reprinted by permission of the author.



to you. Your second response to yourself is that “everyone doesn’t forget”, but this argument doesn’t make you feel any better. It reminds you that in a world where most people pay their debts, you are one of the scoundrels who does not. You start rationalizing: “After all”, you say to yourself, “I need the money more than he does.” In a final moment of belligerence, you smash your fist on the table and say, in part to yourself and in part to the slightly surprised people sharing your library table, “The only person I have to worry about is me!” There is an embarrassed silence. Then you walk over to the bank of phones and dial: “Hello, Harris? You remember that five dollars you loaned me?”

This point of this little scenario is to capture the day-to-day nature of ethics. Even such a simple situation involves conflicting interests, profound moral principles and the nagging voice of conscience, culminating in a quiet but nevertheless telling conclusion concerning the sort of person you are. This case does not involve any of the more notoriously difficult social problems and life-or-death decisions so vehemently debated today, such as the abortion issue, the legitimacy of war, the plight of the homeless in a land of affluence or starving children in a world awash with surplus food. But, ultimately, the considerations that enter into our debates on these global issues reflect our habits and opinions in the most ordinary circumstances. Our politics express who we are and what we believe, and even our most abstract ideologies reveal (although often in a convoluted and even reactionary way) the principles and prejudices of everyday life.

## **What Is Ethics?**

Ethics is that part of philosophy which is concerned with living well, being a good person, doing the right thing, getting along with other people and wanting the right things in life. Ethics is essential to living in society, any society, with its various traditions, practices and institutions. Of course, those traditions, practices and institutions can and must themselves be assessed according to ethical standards, but they themselves determine many of the rules and expectations that define the ethical outlook of the people living within them. Ethics therefore has both a social and a personal dimension, but it is not at all easy, in theory or in practice, to separate these. Moral judgment is both the product of society and one of its constitutive features. What we call our “personal values” are for the most part learned together and shared by a great many people. Indeed, those values we consider most personal are typically not those that are most idiosyncratic but rather those that are most common, and most profound, respect for human (and animal) life, outrage at being the victim of a lie, compassion for those much worse off than yourself and an insistence on personal integrity in the face of adversity.

The word “ethics” refers both to a discipline – the study of our values and their justification – and to the subject matter of that discipline – the actual values and rules of conduct by which we live. The two meanings merge in the fact that we behave (and misbehave) according to a complex and continually changing set of

rules, customs, and expectations; consequently, we are forced to reflect on our conduct and attitudes, to justify and sometimes to revise them.

Why do we need to study ethics as a discipline? Isn't it enough that we *have* ethics, that we do (most of us, most of the time) act according to our values and rules? But part of our ethics is understanding ethics, that is, acting for *reasons* and being able to defend our actions if called upon to do so. It is not enough, after the age of eight or so, simply to do what you are told; it is just as important to know the reason why, and to be able to say no when you think an act is wrong. So, too, it is not enough to have strong political opinions on this or that controversial social issue. It is important to have reasons, to have a larger vision, to have a framework within which to house and defend your opinions. The study of ethics teaches us to appreciate the overall system of reasons within which having ethics makes sense. Understanding what we are doing and why is just as essential to ethics as the doing itself.

We learn ethics, typically, a piece at a time. Our education begins in childhood, first and foremost, with examples, continuous demonstrations of “normal” behavior. We watch our parents and our older siblings, before we know what they are doing, and we imitate them, no doubt before we know what we are doing. Our education continues with a number of instructions and prohibitions, such as “don't hit your little sister” and “you should share your toys with your friends”. The recognition of authority is essential, of course, beginning with “You do what your father says” and culminating in “Because it's the law, that's why”. But it is also learning reasons, such as “because if everyone did that, there wouldn't be any left” or “because it will make her unhappy”. Ultimately, we learn the specialized language of *morality* and its more abstract reasons for doing or refraining from certain actions, such as “because it is your *duty*” and “because it is *immoral*”. By this time we have begun to learn that ethics is not just a varied collection of “do's and don'ts” but a *system* of values and principles which tie together in a reasonable and coherent way in order to make our society and our lives as “civilized” and as happy as possible. The study of ethics is the final step in this process of education – the understanding of that system as such and the way that all our particular values and principles fit into it.

## Change, Choice and “Pluralism”

Our understanding of ethics is complicated enormously by the fact that, as a living system, our ethics is continually *changing*. Consider, for example, the tremendous changes that our society has experienced over just the past few decades in the realm of sexual morality; today, we accept behavior which would have been wanton immorality fifty years ago (for example, topless beachwear for *men*!). Similar changes have taken place in our concept of personal roles and career options. Only twenty years ago, many people considered it “unethical” for a wife to work except in cases of dire family need, but it was perfectly acceptable – in fact, even com-

mendable – for a husband to spend so much time working at his career that he virtually never saw his children or did anything but work. Today, we would not find such behavior praiseworthy but, rather, akin to a disease – some call it “workaholism”. Attitudes toward authority have also changed dramatically. Fifty years ago, the attitude of most young men, when drafted into the army (or invited to enlist), was unquestioning acceptance. Twenty-five years ago, those who refused to follow orders and resisted authority were praised by many people as moral heroes. What this means, and whether there are more basic values that support both obedience and disobedience, depending on the situation, are some of the most important questions of ethics.

We live in a society filled with change and disagreements, in which each generation is taught to reexamine the values and actions of the older generation, in which doing what you are told or simply conforming to tradition is not necessarily a mark of moral goodness but may be considered cowardice or lack of character. Our ethics, in other words, essentially involves *choice*. In fact, having and permitting individual freedom of choice is itself one of the most noteworthy values of our ethics. But choice is not arbitrary and to choose between alternative courses of action or opposed values requires intelligent deliberation and some sense of the reasons why we should choose one rather than another. Each of us must select a way of life, perhaps a career or a profession, perhaps a long search for selfhood or a life of creativity or adventure. We might “follow in our parents’ footsteps” or we might go off on a completely different path. But we must choose. Each of us must decide whether or not to get married, and when and to whom. We must decide whether or not to have children, how many, and how they will be raised, thus affecting the lives of others in the most direct and dramatic sense possible. Every day, each of us decides whether or not to engage in a dozen small misdeeds and an occasional misdemeanor, such as whether to drive high-speed Highway 10 to El Paso at a safe (but illegal) 80 miles per hour, or to take an extra box of paperclips from the office, since “no one will ever miss them”.

The importance of choice in ethics is often confused with the notion that we “choose our values”, that values are merely “subjective”, that everyone has his or her own “personal values”. This is misleading. Most of ethics involves decisions between already-established possibilities and already-available reasons, and those we do not choose. A student deciding between joining the Navy or going to law school does indeed have an important choice to make, but the alternatives and their values are provided by the society as a whole (There must already be a navy to join or a society with a role for lawyers). One does not choose the alternatives; one chooses among the alternatives. And once one has chosen, he or she is suddenly situated in a world of “objective” values – the iron-clad rules of the military or the ethics of the legal profession. In ethics we face choices, but the personal values we thereby endorse are virtually never one’s own values alone. The very nature of values is such that they must be shared; they exist over and above those who embrace them.

Nevertheless, there is a sense, defended recently by the French “existentialist” Jean-Paul Sartre, in which each of us “chooses” our values every time we make an ethical decision. By deciding not to take advantage of a loophole in the tax laws, for example, one personally affirms the priority of compliance over individual gain. By acting in one way rather than another, we support one value rather than another, one sense of who we are rather than another. Thus, Sartre also says that we “choose ourselves”, that ethics is largely a matter of individual choice and commitment rather than of obedience to already-established authorities.

We live in an ethically *pluralist* society. This means that there is no single code of ethics but several different sets of values and rules in a variety of contexts, communities and “subcultures”. Professional and business people in our society emphasize individual success and mobility; some cultural communities stress the importance of group identity and stable ethnic tradition. Some college and urban communities are notably more “liberal” in their tolerance for eccentricity and deviance than the more conservative suburban neighborhoods surrounding them. Even what would seem to be the most basic rules of morality seem to vary from culture to culture and context to context, neighborhood to neighborhood. Thus, we find our Supreme Court – the ultimate arbiter of laws if not morals – insisting on “community standards” as the test for what is permissible, in the case of pornography, for instance. Such disagreements cut to the very core of our ethical values. Many people in our society insist that the ultimate value is individual freedom. But freedom has its costs, among them the inconvenience and deprivation of others, and many people thus argue there are issues of morality and justice that are more important than individual freedom. Some people consider it absolutely wrong to take a human life even if the life in question is that of an unborn zygote or fetus; others do not believe that such a life counts a “human” and should be sacrificed if necessary to the well-being of the mother. None of these differences in ethics are easily reconciled; in fact, they may be irreconcilable. But that makes it all the more important that we understand the nature of these differences, and at least know how to try to reconcile our differences instead of intransigently shouting our views at one another, using the law to “legislate” morality or simply storming out of the room. Trying to be “reasonable” in this sense is much of what ethical discussion and debate are about, and pluralism provides much of the motive. If one isn’t clear about the nature and justification of one’s own values, he or she won’t be in a position to understand the nature and justification of other people’s values. And if one doesn’t understand other people’s values, neither will one understand how they conflict or might be brought into harmony with one’s own.

## Ethics and Ethos

The word “ethics” comes from the Greek word *ethos*, meaning “character” or “custom”, and the derivative phrase *ta ethika*, which the philosophers Plato and Aristotle used to describe their own studies of Greek values and ideals. Accordingly, ethics is first of all a concern for individual character, including what we

blandly call “being a good person”, but it is also a concern for the overall character of an entire society, which is still appropriately called its “ethos.” Ethics is participation in, and an understanding of, an ethos, the effort to understand the social rules which govern and limit our behavior, especially those fundamental rules, such as the prohibitions on killing and stealing and the commandments that one should “honor thy parents” and respect the rights of others, which we call *morality*.

The close connection between ethics and social customs (“mores”, which shares its etymological root with the word “morality”) inevitably raises the question of whether morality is *nothing but* the customs of our particular society, our ethics nothing but the rules of our particular ethos. On the one hand, it is clear that ethics and morality are very closely tied to the laws and the customs of a particular society. Kissing in public and making an enormous profit in a business transaction are considered immoral in some societies, not in others. But, on the other hand, we are firmly convinced that not *all* laws or customs endorsed by an entire society are equally acceptable. The rules of etiquette may be merely a matter of local custom or taste, but the prohibition against cannibalism, for example, seems to have much more universal power and justification than the simple reminder, “That just isn’t done around here”.

One way of circumscribing the principles of morality – as distinguished from rules of etiquette and standards of good taste, for example – is to insist that these are not the province of only a particular society or subculture within society but, rather, rules which we apply to all people everywhere and expect them to obey. We might be happy to accept, and even be charmed by, the fact that people in another culture eat food with wooden sticks instead of forks or enjoy music based on quarter tones without a discernible melody. But when we consider the “culture” of gangland America, for example, or the peculiar rules of certain cults and subcultures, our tolerance diminishes and we find ourselves quite willing to “impose” our values and standards. Ethics provides the basic rules of an ethos, but those rules are not limited to that ethos. Ethics needs a culture in which to be cultivated, but that does not mean that ethics consists of just the rules of that particular culture. Morality, according to many philosophers, is that set of rules which applies to all cultures, whatever their customs or traditions.

An ethos is that core of attitudes, beliefs, and feelings that gives coherence and vitality to a people (in ancient Greek, an *ethnos*, a word significantly similar to “ethos”). It may be spelled out explicitly in terms of laws, but much of an ethos resides in the hearts and minds of the people, in what they expect of one another and what they expect of themselves, in what they like and dislike, in what they value and disdain, hope and fear. It is an essential part of our ethos, for example, that individual success and “standing out in the crowd” are very important to us. There is no law or moral principle that commands that this should be so, but obviously our ethics very much depends upon these values of individualism and achievement. In some societies, by way of contrast, individual ambitions and eccentricities are unacceptable. “The nail that sticks out is the one that gets hammered down”, reads a traditional Japanese proverb. We should not assume that all ethè (the plural of “ethos”) are the same, even in their most basic values and visions.

## Morality

Ethics includes the whole range of acceptable social and personal practices, from the rules of “common courtesy” to the institutions that determine the kinds of work we do, the kinds of friends we have, and the ways we relate to both family and strangers. Morality, on the other hand, is something more specific, a subset of ethical rules which are of particular importance and transcend the boundaries of any particular ethos or situation. Thus, we believe, it is *always* immoral to be cruel to children, even if doing so is part of a family tradition for several generations. “Morality”, accordingly, is thought to be a weightier term than “ethics”. If someone refuses to play fair or to honor a verbal contract, we might say that he or she is untrustworthy or “unethical”, but we would not say “immoral”. If a person abuses children or poisons his in-laws, however, we would call such behavior “immoral”, thus indicating the seriousness of these violations. Morality consists of the most basic and inviolable rules of a society.

The distinction between ethics and morality – ethics as the whole of our sense of self and our place in society and morality as the core, universal, most inviolable rules in any society – is not always followed in either ordinary conversation or philosophical theorizing. Indeed, the curious history of these terms shows how much our very conception of ethics and morality has shifted over the centuries along with the more obvious shifts in the practices they evaluate and prescribe. The current definition of the word, “morality”, for example, displays a range of meanings that shows both the ancient sense in which the terms “morality” and “ethics” both embrace the whole of human behavior and the very narrow nineteenth century concern in which sexual behavior became an obsessive focus of ethical concern. The Random House Dictionary, for example, lists as definitions of “morality” (a) conformity to rules of right conduct, (b) Moral quality of character, (c) virtue in sexual matters, (d) a doctrine or system of morals, (e) moral instruction. We shall see how these various conceptions play off against one another in current as well as traditional debates in ethics. But for our purposes here, we shall start by sticking fairly closely to the first definition of morality as “conformity to rules of right conduct” – and as those rules themselves. But this is not sufficient. Many rules in ethics (“don’t be rude”) and even in etiquette (“don’t eat your burrito with a spoon”) seem to be “rules of right conduct”. What distinguishes moral rules is a number of rather distinctive features, which are emphasized (in different ways and with many mixed opinions) by philosophers and other moral theorists. Here are four of the most-often mentioned:

### Moral Rules Have Great Importance

Moral rules, however else they may be characterized, are of indisputable importance. They are like trump cards in certain games, overpowering all other considerations. In our opening example, the *obligation* to repay a loan outweighs purely

personal concerns, such as one's embarrassment or one's own need for money. Indeed, it is the mark of morality that the amount of money involved is not what is important. The obligation would override selfinterest whether the amount involved were ten cents or a thousand dollars. It is sometimes suggested that moral rules are those without which a society could not survive, or, at least, could not function in what it considers a "civilized" way. For example, how could there be promises or contracts at all – the basis of much of our lives – if the respect for promises and contracts were not more important than a person's personal advantage in breaking them? Furthermore, to call a person or an act "immoral" is to condemn that person or act in the strongest possible terms, just as to say that an issue is a "moral issue" is to say that it is of the utmost urgency.

One problem with characterizing moral issues in terms of their extreme importance, however, is that this reduces the insistence that any particular moral issue is important to a mere tautology, the trivial demand that it is important because it is important. Some matters concerning a person's private sexual behavior, for instance, are considered moral issues but, in the larger scheme of things, hardly seem very important. And some of the most global issues confronting us, international politics and wars which threaten the lives of millions, while indisputably important, are often not treated by State Department officials as moral questions at all. Therefore, while it is generally true that moral issues are important issues and that one way of emphasizing the importance of an issue is to designate it a moral issue, importance alone does not seem to be adequate to capture what we ordinarily mean by morality. There can be petty moral issues, and there can be extremely important non-moral issues.

## Morality Consists of Universal Rules

Morality is rule-governed in that it tells us what sorts of things to do and not to do, by way of general classes and types of acts, such as "one ought to repay debts" and "don't ever tell a lie". Morality involves obedience of such rules, but it also requires understanding, knowledge of the rules and the recognition that they are necessary and obligatory. Furthermore, moral rules are distinguished by the fact that they are *universal*: they apply to everyone everywhere. They are not just local customs or the rules of some particular practice (such as, staying behind the line of scrimmage is obligatory in football).

One problem with characterizing morality in terms of obedience to rules is that it seems to leave out a great deal of behavior that is, in an important sense, "mindless". Good habits are as important in ethics as they are in etiquette and sports, and the very nature of a habit is such that its actions are nondeliberative, unthinking. Of course, habitual behavior can *conform* to a moral principle, but this weakens the notion of obedience considerably. And is it true that all of what we consider moral can be captured in a genuine principle? The demand that we should "love our neighbors" has the form of a principle, but does it capture the spirit of love

that one should express affection *on principle*? Can the notion of rules capture all of the aspects of morality, for instance, the role of the right feelings in moral behavior? Or is obedience of certain rules just one aspect of morality and not morality as such? The question of universality, of course, is one of the central controversies in ethics. Again, moral principles may be universal in form (“everyone ought to...”) but the scope of the “everyone” remains in question. Does it mean everyone in the world, or everyone in this society, or everyone “like us”, or, the most trivial, everyone who is in the same relevant circumstances? At the minimum, moral principles can’t be designated for one and only one person. “John Jones ought to...” is not and cannot be a moral principle (even if, indeed, John Jones ought to).

### Moral Rules Are Rational, Disinterested and Objective

There are special *reasons* for acting morally, for example, “because it is my obligation”. These reasons require special concepts (e.g., “duty”, “obligation”, “on principle”) and a special kind of up-bringing in which these concepts are inculcated. This ability to think in terms of abstract principles (e.g., “never tell a lie”) and reasons (“because if everyone lied, no one could believe anyone”) is often called “rationality”. One of the key features of rationality, according to many philosophers, is its universality. Unlike most emotions and desires, for example, reason is the same in everyone. Everyone may have his or her own ideal of love or ‘pet peeve’, but we all necessarily share the conclusions of reason, e.g. “two plus two equals four”. Thus it is sometimes said that, if a reason is a good reason, it will be so “for every rational creature”, and morality has been defined by some philosophers as the rules and actions of “a completely rational person”. The hard question then, of course, is whether rationality is itself objective and universal, or whether what counts as “practical reason” in ethics might differ from culture to culture (It also differs from philosophical theory to philosophical theory).

It is also said that morality is rational, in part, because it is *disinterested*. A moral rule is disinterested both in that it applies without regard to one’s own personal interests or feelings or status in the case and in that it remains oblivious to the interests, feelings and status of the people to whom it applies (Think of the classic image of Justice as wearing a blindfold, thus being “blind” to individual interests and the identities of the people who stand before her). One has an obligation to repay a loan whether or not one needs the money, whether or not repaying the loan will advance one’s interests in other ways (for example, making it easier to obtain another loan in the future) and whether or not the person who made the loan needs the money back. Of course, one can sometimes use a moral principle to one’s own advantage, but the moral principle itself is formulated to no one’s advantage and with no particular person’s interests in mind. To so insist that morality is independent of “subjective” feelings and interests is to say that morality is *objective*. Thus rationality and disinterestedness imply objectivity. “Adultery is



wrong!” does not mean “I don’t like adultery” or “Our society disapproves of adultery”; a moral rule is objective insofar as its correctness is quite distinct from what particular people — or even whole societies — happen to think of it. “What’s right is right and what’s wrong is wrong.” (“Subjectivity”, by contrast, is often dismissed as the notion that morals are only “one’s own personal opinion” — nothing more)

Again, however, the scope of this feature of morality can be called into question. Is rationality, that is, thoughtfulness and deliberation, essential to all moral behavior, or is unthinking, habitual performance sometimes far more impressive? Should morality be disinterested? Perhaps in the case of justice or an actual judge in a courtroom, but should we praise parents for disinterestedly raising their children or friends for disinterestedly doing what they ought to do, for example, visiting a sick friend in the hospital? So, too, with objectivity. If objectivity rather than subjectivity means little more than a defensible, not merely personal opinion, then there may be no objection to it (though even then, with reference to such personal feelings as love and grief, there are hard questions to be raised). But if objectivity is taken to mean that there are moral facts in the world, quite independent of our feelings, interests and attitudes, then the notion of objectivity becomes quite controversial.

## Morality Is Concerned with Other People

Morality essentially involves consideration of interests other than one’s own and is thus well summarized in the various versions of the so-called Golden Rule. “Do unto others as you would have them do unto you” is found in almost every ethical system. In the Hebrew Talmud, for example, it is presented as the basic principle of ethics: “What is hurtful to yourself do not to your fellow man; that is the whole of the Torah [the Jewish Scriptures] and the remainder is but commentary”. The Confucian *Analects* tell us, “Do not unto others what you would not they should do unto you”. The Taoist *T’ai Shang Kan Ying Pien* says, “Regard your neighbor’s gain as your own gain, and regard your neighbor’s loss as your own loss”. The Buddha insisted, “Hurt not others with that which pains yourself”. And Mohammed commanded (as in the *Analects*), “Do not unto others what you would not they should do unto you”. The slight differences among these versions of the rule may make a considerable difference in morals. Consider the difference, for example, between the warning that what you do to others might be done to you in turn and the appeal to compassion, that you should think about other people’s feelings in the same way that you think of your own. It is worth noting that most of the versions refer to one’s own possible pains and interests. But, at the same time, every version makes reference to the interests of other people, and this is the essence of morality; it presupposes an awareness of the interests of others as well as of one’s own. (We might note that even the cynical version, “Do unto others before they do unto you”, presupposes awareness of other people’s interests and in-

tentions but construes these in a strictly antagonistic way). The opposition between morality and mere self-interest, however, does not imply that to be moral you must always go against your own self-interest. Indeed, one of the most common arguments for morality is that it ultimately serves all of our self-interest and, all things considered, it is to our advantage that everyone (including us) obeys the rules of morality and pays attention to the interests and well-being of others.

Again, however, the criterion comes into question when we begin asking what makes an action moral rather than, say, kind or considerate. To care for other people is undoubtedly a good thing, but one can pay attention to other people for many reasons other than the tugs of morality. One can love them, be friends with them, be related to them, have a job to look after them, work together in such a way that cooperation and coordination is essential. The idea resurfaces that morality cannot be merely other-directed concern but involves some special domain of issues and concerns or of rules and rationality. Thus we find ourselves in the somewhat peculiar position that while the study of ethics centers on the concept of morality it is precisely that concept which is in question. What is morality? Does morality consist of some special domain? Or could the distinction between moral and non-moral issues be a bogus distinction, an odd historical curiosity or a merely rhetorical device? Is morality so important, or is it nothing more than an overly precise name for a more general sense of the public good, caring about other people and being a good person.

Somewhere near the beginning of any book on ethics, it is virtually compulsory to introduce the most prominent single philosopher in modern ethics, who is, more than anyone else, responsible for this emphasis on “morality” in ethics, Immanuel Kant. Kant was a German who wrote at the end of the eighteenth century. In ethics, it is Kant who introduces the most distinctive philosophical version of the Golden Rule; it is also Kant, however, who defends the strictest characterization of morality in the history of ethics. His somewhat technical version of the Golden Rule is, “Act so that the maxim (principle) of your action can be willed as universal law”. Kant’s thesis is a formal version of the demand that morality is essentially universal and that moral principles are universalizable; moral rules always apply to everyone and never refer to just one person or that person’s own interests alone. But where most conceptions of morality tend to give equal emphasis to both one’s own interests and the interests of others (as in the standard formulations of the Golden Rule), Kant separates self-interest and morality completely; indeed, insofar as an act is based on “inclinations” of any kind (whether personal desires or sympathy for the other fellow), that act is not called “morally worthy”. Morality, he says, is a law unto itself, “categorical” and independent of all personal interests and inclinations. Accordingly, Kant analyzes morality in terms of what he calls the “categorical imperative”. An imperative, of course, is simply a command; morality for Kant consists of rules. “Categorical” is a strong way of insisting on the absolute nature of moral rules. According to Kant, morality is thoroughly objective, a product of reason (“practical reason”). A moral principle has nothing to do with personal interest or the particular circumstances of the case. It is thoroughly disin-

terested, in other words, and it is also what Kant calls “a priori”, or “prior to” any particular cases or moral judgments we might make. It is in Kant’s ethics, in other words, that the four basic features of morality are brought together into a singularly powerful conception of morality. Many philosophers and readers have challenged this conception as too narrow, as too impersonal, even as “heartless”, and many others have come to Kant’s defense and argued more flexible, less dogmatic interpretations of his ethics. But even in its most rigid expression, Kant’s model of morality is so systematic and persuasive that it is impossible to study ethics without coming to grips with it. Indeed, there are ethicists who would say that the study of ethics today is a study of variations and objections to the theory set out by Kant some two hundred years ago. Still others would say that the heart of contemporary ethics is the rejection of this same moral theory.

## **Ethics, Ethos and Morality: The Problem of Relativism**

To understand the ethos and the ethics of various peoples is one of the aims of the science of anthropology. Ethics, however, is something more than this. For example, as the great French anthropologist Claude Levi-Strauss commented in a 1970 interview:

“When I witness certain decisions or modes of behavior in my own society, I am filled with indignation and disgust, whereas if I observe similar behavior in a so-called primitive society, I make no attempt at a value judgment. I try to understand it.”

Philosophers often distinguish between *descriptive* statements and *prescriptive* statements; the former tell us what the facts are, but the latter tell us what *ought* to be. It is one thing to describe what people do and what they value; it is something more to enter into their lives and tell them what they ought to do and value. In anthropology, we can and should be content with description. In ethics, however, our descriptions are always mixed with prescriptions, for we are not merely trying to understand ourselves. We are also trying to live well and do what is right to do.

Ethics is not a descriptive science but an active participation in a set of values, a way of life. But as we have already noted the notion of “a way of life” leaves open the question whether some ways of life (human sacrifice, military aggression for the fun of it) might be morally wrong. Morality, as characterized in the preceding section, is universal and not just one set of values among others. Moral rules, accordingly, get applied not just to one’s own ethos, but to all others as well. When European explorers found out that the natives of the New World practiced human sacrifice, they did not simply note it as an anthropological curiosity; they were horrified (even as the Inquisition was systematically killing people in Europe in the name of Christianity). When Northerners visited the Southern states during the years preceding the Civil War, they did not see slavery as a quaint custom or a

local necessity; they viewed it as the grossest immorality and a pretext for war. When some rural German philosophers visited the sweatshops of London and Manchester at the beginning of the industrial revolution, they were indignant, and they started fomenting a revolution of a very different kind. Karl Marx was one of them, and, not surprisingly, he formulated his revolutionary manifesto in the universal vocabulary of morality and justice, not just in economic terms.

Moral rules are more than mores and customs because they claim to outline the conditions which *any* society must fulfill, applicable to everyone everywhere. The moral prohibition on incest, according to some influential anthropologists and biologists, is not only a universal moral rule but built right into our genes as well. (Partial evidence for this is the prevalence of incest taboos among most animal species, although such inferences from other species to human morality are always to be made with extreme caution). The moral rule that “thou shalt not steal” seems to be not just a custom common to many societies but the necessary condition for there being any secure sense of ownership at all. The moral rule that it is wrong to lie seems to be the precondition of anyone’s ever believing anyone else. Imagine visiting a city, for example, where most of the directions you receive are lies, as the natives mischievously send you off in this direction and that. After a short time, you will refuse to listen to any directions at all, knowing the odds against their being correct. A society can exist with *some* lying, of course, but it is impossible to imagine a society in which lies would be more than occasional deceptions, presupposing that most people most of the time tell the truth.

Moral rules are considered to be basic rules because they outline the conditions for the very existence of society. Certain moral rules may be of special importance in particular societies. For example, cheating and plagiarism are considered moral transgressions in a college community because they undermine the conditions for a truly competitive, creative community. Violating a contract and refusing to pay one’s bills are considered especially serious violations in business because such acts threaten the very existence of the business community. Some moral rules seem to be of special importance in virtually every society: sexual mores and family relationships, for example, have a profound importance in almost every culture, insofar as having babies and raising them is obviously essential to the continuation of the culture.

Although morals are basic to the existence of a society, there is clearly at least a shift if not a dramatic change in morals depending on changing social and economic conditions. For instance, the morality of having children changes dramatically in times of serious overpopulation or underpopulation. Whenever the population seems to be increasing to the breaking point, many people insist that it is “immoral” to have more than one or two children, even when a family can easily afford them. In societies eager to increase their population on the other hand, *not* having children is typically considered a moral failing. (In underpopulated ancient Rome, for example, pregnancy was so encouraged that there was not even a word for “contraception” [ironically, a term derived from Latin roots]). Indeed, there are overpopulated societies in which even murder is taken less seriously, and the death

of hundreds of people from disease and starvation is considered merely a normal part of daily life. Or, to take a more agreeable example: In a society in which there is much to be accomplished (for instance, in colonial America), work becomes a virtue – even an “ethic” unto itself. Just lying back and enjoying life, the “virtue” of some aristocratic and leisurely societies, is recast as “laziness”, a vice.

These variations in morals from society to society have naturally troubled moralists and ethical philosophers who would like to find a single, universal set of standards which lies at the basis of all societies. Some ethicists avoid this problem by restricting their attention to the moral rules and the logic of moral thinking just in their own society, without even attempting to pass judgment on societies other than their own. Other ethicists consider the variations on a single set of moral rules which are universal. Consider, for example, the various senses of “stealing”. Aristotle and much of medieval society considered the taking of profits in business transactions a mode of stealing, and Marxist societies regard the very institution of private property as a form of theft. (“Property is theft”, wrote a nineteenth-century French socialist named Proudhon, who was quoted by Marx). On Wall Street, it is just another day’s business to take an entire company away from its unwilling owners (an “unfriendly acquisition”), so long as the buyer is willing to pay for 51 percent of the stock and an expensive team of lawyers and strategists. What counts as ‘stealing’ is often determined by context. In baseball, running unexpectedly from one canvas sack to another counts as “stealing a base”, but this is a legitimate part of the game. (Stealing a base by actually picking up one of those sacks and running off the field with it, however, is not part of the game and thus illegitimate). In the face of very different views of what might be called “stealing”, it would not seem easy to isolate some underlying if very complicated universal principle, summarized simply and without qualification as “thou shalt not steal”, which applies to medieval life and Marxism as well as Wall Street and baseball. But one could argue, for instance, that all of these variations are but special instances of the general rule, “do not take that to which you are not entitled”. Of course, one would then, in any particular application of the rule, have to specify what warrants “entitlement”. Aristotle accepted the idea of private property and the desirability of wealth but rejected the legitimacy of exchange for profit. Marx rejected the institution of private ownership and so saw all accumulation of wealth as theft. Stealing a base is a legitimate play in baseball but disrupting the field by taking the sack is not. So although what counts as stealing may vary from context to context, the underlying moral prohibition remains the same. But then again, could it be that this underlying principle is trivial – saying only that “wrongful taking is wrong”?

There are ethicists, however, called relativists, who reject this idea that there are universal moral principles, with or without local variations and contextual qualifications. Relativists argue that morality is indeed *relative* to an ethos and limited to that ethos. “What is moral in India can get a man hanged in France”, wrote one eighteenth-century relativist, his conclusion being that morals are nothing but the local customs of a particular community. This conclusion might not

upset us, if it meant only that certain customs and mores – eating habits and attitudes toward pets, for example – were different in different societies. Nor would it be especially troublesome if it were only a way of reminding us that *particular* moral rules and actions differ from place to place – whether charging high interest rates counts as “stealing” or whether early abortion counts as “murder”. What is upsetting is the idea that cold-blooded murder or slavery might be moral, in feudal Japan or ancient Greece, for example, and that we have no right whatever to condemn them.

*Relativism* in its extreme form claims that there is much more than just superficial differences among societies. It insists that the most basic rules of morality are different too, that not only what counts as murder, for example, but even murder itself has different moral status in different societies. For example, in some cultures, religious sacrifices, such as Agamemnon’s slaughter of his daughter and the Aztec annual vivisectionist rituals, were considered legitimate forms of killing. Trying to bridge the cross-cultural gap, one might say that it is not a murder in such cases because there was *some reason* for the killing, namely, a religious reason. But this limp suggestion would eliminate as murder virtually all cases of killing except involuntary manslaughter (which is not murder) and the very rare cases of intentional murder without any (conscious) reason at all. Again, one might make the purely verbal point that “murder” by definition means “wrongful killing”, and thus *all* murder is (necessarily) wrong, but this just moves the question back one step to “killing”, and whether killing is always considered wrong. Relativism, consequently, continues to be one of the most pressing problems in ethics, and it will follow us like a shadow through many of the discussions in this book. A society’s ethos is partially defined and circumscribed by its morals, but does the ethos alone define and circumscribe morals? Is morality, like etiquette and entertainment, just the product of a particular society, or does it underlie the *ethè* of all societies as their basic foundation? Are we justified in extending our moral principles to people across the world? Or is this, too, just another example of “imperialism”, the unwanted imposition of one culture’s tastes and standards upon another which itself is considered, by many people, to be morally wrong?

## Egoism and Altruism

Just as some philosophers have been suspicious that what we call “morality” may be only the projection of our own ethics onto other people, many philosophers and a great many other people (e.g. most economists) have suspected (or presumed) that what moves people to act is virtually never morality or the interests of other people (except, perhaps, their closest kin) but rather *one’s own* interests, which may or may not coincide with the moral rules. Of course, such behavior in one’s own interest need not be crude or inconsiderate, and it need not even serve one’s own interests “in the short run”. Indeed, the mark of smart or “enlightened” self-interest or what we call *prudence* is precisely the wisdom to be considerate and

concerned with the well-being of others if only as a means to furthering one's own long term interests. Prudence is still self-interest, but it involves caution, social awareness and long-term thinking. It may be an enormous thrill to drive your car at top speeds down a winding country road, but you could easily be killed or, given the occasional pedestrian loitering in the middle of the road, kill someone. It may be what you want at the moment, but it is not prudent. It may seem to be in your self-interest to cheat on an exam, when that one extra grade will get you on the Dean's list. But you may be caught and expelled; you may be initiating a habit that will ruin or deprive your educational talents later on; you will deprive yourself of the opportunity to prove your worth on your own; you will probably lower yourself in your own eyes and in the eyes of any other students who see you. Cheating may be in your immediate self-interest but it is not at all prudent. Thus prudence, unlike crude, thoughtless self-interest, is often in conformity with the dictates of morality. But is morality motivated by nothing more than prudence, or is prudence – as enlightened self-interest – still something short of truly moral behavior?

One of the most enduring debates in ethics (dating back to Plato, at least) concerns this question of motivation in morals. Do we, in fact, always act for the sake of our self-interest? Or do we, at least sometimes, act for the sake of duty and duty alone, or for the sake of others without regard to our own self-interest? Traditionally, this dichotomy between acting out of one's own self-interest versus acting for the benefit of others has been marked by the terms "egoism" and "altruism". Egoism is acting out of self-interest. Altruism is acting for the benefit of others. Altruism may be based on some sense of attachment or compassion, but it need not be. One could be altruistic on principle, always taking other people's interests as more important than his own. Like many ethical categories, egoism and altruism are used to refer to the consequences as well as the motivation of behavior. Egoism is action that benefits oneself. Altruism is action that benefits others. (Many biologists have even begun using the words "egoism" and "altruism" to refer to the behavior of genes, viruses and one-celled lifeforms, where the question of motive cannot intelligibly arise). But the primary meaning of these terms is and must be tied to motivation, not consequences. One can, perhaps despite one's bad intentions, benefit others, but such behavior is not by any means altruistic. One often does, unfortunately, fail in one's efforts to help others, occasionally benefiting oneself in the process. And whether or not genes or genotypes exhibit patterns that can be described as self-perpetuating, "selfishness" is hardly the motive.

On the one hand, egoism is obviously antithetical to morality; it designates concern for one's own interests whatever the rules and whatever one's obligations. (One can, of course, be moral and fulfill one's obligations just as a means to satisfying one's interests). On the other hand, egoism, many ethicists have argued, is the sole basis for *any* human behavior, moral or otherwise. This raises a very difficult question; If this is true, how is it possible ever to act for the sake of morality (unless our obligations also satisfy our interests)? Are we moral (when we are moral) only because being so is in our interests? If I give money to a beggar and feel good that I have done so, have I in fact given him the money only in order to

feel good afterward? This raises the age-old question of “human nature”, and whether we are indeed “by nature” selfish creatures or perhaps rather social beings in whom concern for others and at least some minimal sense of compassion is equally natural. But it also raises another debate, which questions not our nature but rather the strategies with which we get along in life. Then the question is not what we “naturally” feel or do but rather what we *ought*, as rational creatures, to do. The first issue, again, is descriptive – having to do with what sort of beings we are, the second prescriptive – giving us advice on how to behave.

Philosophers accordingly distinguish between psychological egoism and ethical egoism. *Psychological egoism* is the psychological theory that everything that we do, we do for our own interests, whether or not the same act serves other people’s interests or moral obligations. *Ethical egoism* is the view that one ought to act in one’s own interests. Of course, if psychological egoism is true, one cannot help but act in one’s own interests. Nevertheless, the two positions are distinct. One might believe that all people are motivated by their own interests and nevertheless try to make sure that these interests coincide with the common good and morality (for example, by inflicting punishment to offset any personal advantage in wrongdoing). And one might believe that people are not “naturally” out for their own interests but that they *ought* to be so. Imagine a person who believes, for instance, that most of the damage done in the world is caused by “do-gooders” who “ought to mind their own business”. Egoism, by contrast, might seem like virtue.

Altruism might also be divided into two parts: psychological altruism, the theory that people “naturally” act for the benefit of others – and ethical altruism, the view that they *ought* to act for the benefit of others. Many theorists have debated whether *any* of our actions are altruistically motivated, but very few have ever asserted that *all* of them are. The debate, therefore, typically centers on psychological egoism and the question of whether all our actions are self-interested. Ethical altruism quite naturally runs into questions about the motivation of morality. If we are naturally prone to consider the interests of others and the well-being of society then the egoistic question, “Why should I be moral?” loses much of its force. So, too, if reason has its own motivational influence (above and beyond the motivating power of the inclinations, as Kant suggested), then the idea that we always act self-interestedly also loses its initial persuasiveness. It may well be that some of our desires – even our most basic desires – are to be ethical and to help other people when we can. If so, to call the satisfaction of such desires “self-interested” (much less “selfish”) is indeed peculiar if not perverse.

## A Note on Selfishness

The somewhat technical notion, egoism, is often conflated or confused with the more familiar word “selfishness”. But whereas egoism entails reference to self-interest, it does not exclude concern for others (just as altruism does not exclude satisfying one’s own interests). “Selfishness”, on the other hand, implies lack of



consideration of (or outright interference with) other people and their interests. It is, therefore, not just the pursuit of self-interest but the inconsiderate, vulgar pursuit of one's own interests.

According to a popular story, President Lincoln was passing a puddle in a carriage when he saw that several piglets were drowning as the mother pig squealed helplessly. He stopped the carriage and saved the piglets (Whether the mother pig thanked him was not recorded). Back on the road, Lincoln's companion asked him whether that act counted as a pure case of altruism; Lincoln replied, "Why, that was the very essence of selfishness. I should have had no peace of mind all day."

The word "egoism" may suggest some antagonism between one's own interests and the interests of others. Nevertheless, one can be an egoist and also be charming, morally correct, and even a philanthropist, as a number of very wealthy and ambitious people have demonstrated. The word "selfishness", however, is another matter. "Selfishness" has built into it the antagonism between one's own and others' interests, and to say that someone is selfish is to say that this person not only is an egoist but also that he or she subverts the interests of others. "Selfishness" has an undeniable connotation of condemnation and should not be confused with the more neutral term "egoism". To suggest that everyone's behavior is motivated by self-interest is at least a plausible hypothesis; to suggest that everyone's behavior is selfish is both offensive and implausible (though nevertheless there are terrible times when it appears to be true). Accordingly, Lincoln's reply to his friend seems like nonsense. Satisfying oneself is not the same as being selfish, and even if most human action is (at least in part) self-interested, it is not therefore selfish as well.

## **Why Be Moral? Self Interest, Motivation and Justification**

Many of the problems that arise in our thinking about morality are the product of an overly sharp dichotomy between the demands of morality and self-interest. Morality is said to be "disinterested", while self-interest is obviously "interested". Moral rules have some sort of universality and apply to everyone, but self-interest is distinctively particular, concerned with a single person, oneself (Matters became curiously complicated when self-interest is turned into pseudo-moral doctrine, as in "everyone *ought* to pursue his or her own self-interest". But this is usually argued just on the (dubious) grounds that, *if* everyone were to pursue his or her own self-interest, then the results would be best *for everyone* – and so it turns out not to be an ethics of self-interest after all). We have already noted that the sharp opposition between morality and self-interest leads to a problem of motivation, namely, *if* it is true that people do only what they want to do and act only according to their own interests, then why (for what reason, by virtue of what motive) could or should people ever act *against* their interests, as morality may sometimes require? In our opening example, why should one pay back a debt just because morality demands it? An apostle of self-interest might point to our opening story and insist that the reason for repaying the debt was not the sense of obligation (which would

be a distinctively moral motive) but, rather, the personal pain of guilt and the annoyance of those nagging thoughts. Or it may have been with an eye to future possible loans. In other words, despite any noble appearances, the act was self-interested. Indeed, the apostle might say, *all* actions, no matter how moral or heroic or apparently generous, are motivated by self-interest. We may continue to distinguish, the apostle might allow, between moral appearances and self-interest, but we should understand that all actions are ultimately self-interested.

This sharp opposition between morality and self-interest also has dangerous implications. In a society that preaches the virtues of self-reliance and “looking out for number one”, the allure of self-interest becomes more than a perverse theory of moral motivation; it becomes a *rationale* for selfish and immoral behavior as well. In our opening scenario, this view had its explosive but short-lived expression in the table-bashing declaration, “The only person I have to worry about is me!” But in the competitive world of business and professional careers, as well as the “all’s fair” worlds of professional sports, love and war, this rationale can lead to outright rejection of moral rules, and the world really can become, in the words of the seventeenth-century philosopher Thomas Hobbes, “a war of all against all” in which life becomes “nasty, brutish and short”. It is a world summarized, too, in a popular version of Darwinism, as a “jungle” in which the only rule is “survival of the fittest”.

It is a mistake, however, to present the opposition between morality and self-interest as an inevitable conflict. Most of the time, because of shared and mutual interests, because of considerations of reputation, because of the threat of punishment or because of painful “pangs of conscience”, our interests coincide with our moral obligations. And indeed, if they did not, we could rearrange society, with systematic rewards and more rigorous, efficient punishment, in such a way that individual interests would almost always coincide with social and moral principles. But this could be a Draconean measure, and it already assumes that people are basically self-interested and will cooperate and obey the rules only if they are, essentially, forced to do so. A much more amiable suggestion is that people are naturally social and sociable and are prone to behave in whatever ways are admirable or acceptable in their society. They tend to be selfish and act in their own self-interest (to the obvious detriment of others) only when they are taught or forced to do so, by an excessive emphasis on competition to the detriment of cooperation, by conditions of scarcity or adversity that make cooperation impossible. But even then, one should note, people in extreme emergency conditions often act with great courage and generosity. They do not become more antagonistic but more cooperative. The idea that people are naturally self-interested, antagonistic and accept moral constraints only when forced to do so seems to give us a false picture of human nature, and so too a false picture of morality.

We can imagine a world in which moral action and self-interest would always agree, if society were arranged so that people were rewarded for doing beneficial and socially productive deeds, if they were thoroughly socialized as members of the community and educated in civic participation and, where this failed, the pen-

alties were such that immoral or anti-social action would always be against one's better self-interests. This would still not eliminate the distinction between morality and self-interest, however, and one still might insist that the behavior in question, however much in *accordance* with morality, nonetheless fell short of moral behavior. On a very strict (Kantian) moral point of view, to be moral requires the intention to be moral "for its own sake", and this entails at least minimal resistance to one's inclinations. And, of course, it is not "moral" if one wants only to reap rewards or avoid punishments or censure. To tell the truth because one is afraid of being punished for lying does not strike us as morally worthy. Thus, the motivation of morality is not only a matter of getting people to behave morally; it is also an essential ingredient in morality. To borrow Kant's much-quoted example, a grocer who doesn't cheat his customers just because he is afraid of getting caught cannot be counted as a moral example. He is concerned only with staying in business.

The extent to which an action is self-interested gives us a ready understanding of its motivation, but a distinctively moral action seems to require something more than self-interest. Thus Kant tells us that an action has "moral worth" only insofar as it is motivated by duty alone. The motivation of morality thus becomes a key question in ethics, a matter of extreme practical as well as theoretical importance. The question of motivation leads quickly into a further, larger question of *justification*. If moral actions are not (entirely) self-interested, what reasons and arguments can we give for the moral thesis that people ought sometimes to act against their own self-interest? The simple question, "Why be moral?" summarizes both these issues. On the one hand, it can be construed as the query, "How is it in my interest to be moral?" On the other hand, it is the more general question of how "ought"-type rules can be rationally supported, even in the absence of self-interest.

## Rules and Virtues

In our introduction to ethics, we have so far followed an established Kantian tradition by placing a special emphasis on *morality*. Accordingly, we have been emphasizing the importance of moral *principles* in ethics, and, indeed, our ethical tradition is built around the importance of formally stated rules, from the Ten Commandments in the Old Testament to the policy of "government by laws, not men", put into practice by the framers of the United States Constitution. But this emphasis on principles is not the whole of ethics, and there are many systems of ethics which do not place such stress on principles at all. For example, there are societies where the central concern of ethics is obedience – to a ruler or a religious leader, for example – and general principles of the sort we have been discussing may not enter into their system of ethics. One could always formulate the principle, "Do whatever he or she says!" but this is a dubious example of a moral principle. The nature of ethics as well as its specific content is also a matter of *ethos*, and not all *ethè* are so bound up with what we call morality.

What is essential to ethics might not be universal rules and objective rational principles but rather an established way of doing things, a shared sense of value and significance. Consider a group of children at play, throwing a ball or chasing through the woods. Their game does not necessarily need rules. In fact, one might suggest, they tend to formulate rules for activities only when things start to get out of hand. For example, one of the children may decide to sit on the ball and not let the others have it. Consequently the others formulate a “no sitting on the ball” rule. What is essential for understanding almost all human activities is not so much the notion of a rule as such as it is the idea of a *practice*, a shared cooperative activity with mutually understood goals and ways of doing things. Most practices have rules, but rules are not what define the practice. Consider, for example, almost any game. Games are paradigmatic practices. The object of a game may be as simple as keeping a ball in motion or as complicated as the trading games that are daily played on Wall Street. Every game has its characteristic activities – batting, kicking, running, tackling, checkmating – and its essential equipment – a ball of a certain shape, distinctive pieces on a checkered board. Every game distinguishes behavior that is unacceptable and punishable, and every game has its rituals, its ways of doing things, some of which are specified in the rules and dictated by the very purpose of the game. Others just grow up with the game as part of its traditions. Most games have their champions, whom both players and spectators admire. So, too, a society will inevitably have its goals, perhaps the happiness and prosperity of all of its citizens, but perhaps alternatively sheer military might, prestige or religious orthodoxy, whether such goals are conducive to happiness and prosperity or not. A society will have its characteristic activities and rituals, only some of which are essential to survival as such, and it will have its heroes and idols, whom the citizens will emulate – a self-made millionaire in a primarily business society, a warriorchieftain in a primarily military society, a spiritual leader in a primarily religious society. It is sometimes suggested that many social activities work best without formal rules or laws. Thus, business people decry government regulation and insist that the business world works best when left to its own nonmoral governance by supply and demand. And artists often insist that their art consists more in defiance of convention than in obedience to a set of rules. In fact, strict obedience to a set of rules (e.g., in paint-by-numbers paintings) sometimes produces the very worst “art” imaginable. What is important is the practice and its traditions, and, of course, the talents and effort of the individuals participating.

In our preliminary characterization of morality, we said that many theorists would insist that morality consists of rules, principles, and laws; it is not merely right action but right action *on principle*. If we were to accept this as a characterization of ethics, we might have to conclude that many of our activities are devoid of ethical concern, that is, if they are not circumscribed and defined by some set of explicit moral principles. In business, for example, there are any number of implicit understandings about what is fair and what is not, and a great deal of business goes on by way of merely verbal agreements or just a hand-

shake, mutual trust and understanding. (This is what is so misleading about the popular characterization of business as unethical because it is based solely on “the profit motive”. In fact business is more like a complex game in which the sense of mutual participation and cooperation is presupposed just as much as the much-celebrated spirit of competition). Many societies are based on ritual, tradition and obedience to authority, and there is much to their ethics that is not necessarily a matter of principle.

We do not want to say that such activities are amoral. Instead, we are more likely to expand our sense of morals. Or, we might insist instead that morality is not all there is to ethics. The ancient Greeks, for instance, would not have understood our emphasis on rules and principles. They were far more concerned with the *character* of individuals and their distinctive *virtues*. Obeying the laws of society was more-or-less taken for granted, but a good person was not just someone who obeyed the rules. Such people also displayed personal traits and exceptional abilities, characteristics which involved much more than simply abstaining from evil. Indeed, a Homeric Greek with many warrior virtues might indulge in a great many evils and nevertheless remain an ethical hero. Greek ethics turned on individual virtue and heroism more than on obedience and principled behavior.

Largely because of the influence of the great German philosopher Immanuel Kant, however, the emphasis in ethics in the past two hundred years has been on the specific nature of morality as a set of universal principles. But, although we might expect to find rules of some kind in any articulate civilization, it would be a mistake to think of rules alone as the key to ethics. Ethics concerns character and the characteristics of particular individuals rather than on rules and obedience. For example, the virtues of compassion, generosity, courage and so on are an important part of morals, but they do not consist in following rules. Moral behavior in this sense is often spontaneous, habitual, “without thinking”, while morality in the Kantian sense places a premium on being deliberative, thoughtful and reflective. This emphasis on character also allows us to focus on what is special about a person, his or her particular virtues. There is no reason to expect that all admirable people will be the same.

This shift from morality as obedience of a specific set of rules to character has its problematic aspects. One of the more interesting complications of the introduction of the virtues into ethics is the complicated moral status of people who don't obey the rules but nevertheless emerge as heroes of a sort. One notably problematic example is the *rogue*. Some rogues – Robin Hood, for instance – might be morally defended as appealing to a “higher” morality than the laws of the land. But many of the heroes in American movies, for example, have no such thought in mind. They may simply be asserting their own freedom, or having a good time. They are chased by the police, and they do such things as wreck cars and rob banks. They even betray their friends, yet they retain our admiration because of the characters they are. On the more respectable side of the law, too, we find general admiration for the rogue. For example, one of our heroes today is the *entre-*

*preneur*, the type of maverick businessman who takes high risks in order to get a new idea or product on the market. The entrepreneur too is a rogue. One professor at the Harvard Business School recently wrote that to understand the entrepreneur, you have to understand the mind of a juvenile delinquent. Many of our most popular artists and musicians are admired despite what would seem to be their dubious morals. So the question, “what virtues are to count?” becomes central to the issue of virtue ethics. Are there specifically *moral* virtues, and if so, could it be that virtue ethics is nothing but morality-in-action, moral rules internalized and cultivated as habit? Then the distinction between two kinds of ethics collapses and morality retains its central place. Or is virtue something more than morality and quite different in kind? But first, we should look much closer at the institution of morality itself, its nature and justification.

## Appendix: The Great Moral Philosophers

Our ethics as well as our ethos is derived from a long tradition, stretching back in history to ancient times. Foremost among the books and authors that have influenced us, of course, are the Bible and its many scribes and speakers. But of nearly equal importance are the mores and opinions of the ancient peoples of Greece and Rome as well as dozens of other ethnic groups whose views on life have slowly evolved into our own. In philosophy, however, the history of ethics is punctuated, if not actually defined by a number of truly great moral philosophers who wrote about the mores and morals of their own societies and, at the same time, tried to say something universal about morality and living the good life. Even a survey of the history of ethics would include several dozen such authors, and a detailed study would take many years and include possibly hundreds or thousands of minor moralists, essayists, theologians, social reformers, political theorists, and newspaper editors. But for our purposes here, we will find that several names have repeatedly appeared in our discussion and will continue to do so for the remainder of the book. Accordingly, what follows is a brief introduction to ten of the most influential moral philosophers in Western history:

- Socrates and Plato
- Aristotle
- Saint Augustine
- Thomas Hobbes
- David Hume
- Immanuel Kant
- John Stuart Mill
- Friedrich Nietzsche
- Jean-Paul Sartre

## Socrates and Plato

Socrates lived from 470 until 399 B.C. His student Plato lived from 427 to 347 B.C. Most of what we know of Socrates's ethical teachings comes to us through Plato's writings, in which Socrates's conversations or "dialogues" with other Greek philosophers are preserved in vivid, dramatic form. In Plato's earliest dialogues, Socrates's story and his teachings are carefully preserved for us. Against the Sophists who taught such pessimistic theses as "all men are selfish" and "there is no such thing as justice", Socrates took a positive and optimistic view, exemplifying his own integrity and arguing against injustice. Of particular importance is Socrates's insistence on dialogue and debate, "the examined life", as he called it. Socrates spent his life arguing the importance of living virtuously. In his early seventies, he was accused of "corrupting the youth" with his teaching. He was tried and executed. After his death, Plato established the Academy in Athens for the purpose of continuing Socrates's work. In Plato's later dialogues, he clearly embellished Socrates's views and insisted that, over and above the changing things of this world, there was a pure world of "Forms", including the pure Forms of Justice and the Good.

## Aristotle

Aristotle was born in 384 B.C. in northern Greece. His father was the physician of King Philip of Macedonia, and Aristotle later became tutor to the king's son, Alexander (soon to become "the Great"). Aristotle studied with Plato for eighteen years, but he also became the world's most accomplished scientist. His theories of biology and physics ruled Western science for almost two thousand years. In ethics, he developed a theory that was very much in the spirit of biology. Everything, including all human activity, he argued, has a purpose, a function, a *telos*. The ultimate human purpose is *happiness*, but happiness is not just a life filled with pleasures and satisfactions. It must also be a rational life, a life in accordance with reason. And it must be an active and a virtuous life, "a life of rational activity in accordance with virtue".

## Saint Augustine

Augustine was born in Africa in A.D. 354. He was not religious as a young man but, in his thirties, while in Rome, he embraced Christianity and became one of the most influential voices in the development of Christian ethics and theology. Following Plato's and Socrates's vision of the "pure Form of the Good" – which he interpreted as God – Augustine argued that Christian ethics requires the separation of the secular and the divine. In opposition to Aristotle, Augustine insisted that the purpose of life is religious faith and salvation.

## Thomas Hobbes

Hobbes was born in England in 1588. He graduated from Oxford University and entered into a lifetime of study in mathematics, philosophy, and science. (One of his friends was Galileo). His philosophical writings were politically controversial and got him into trouble. He escaped to France, but his irreligious writings got him in even more trouble there, and he fled back to England, where he wrote his greatest book, *The Leviathan*. The book is a masterful political treatise in which Hobbes attacks the ancient idea of “the divine right of kings” and replaces it with the radical view that societies are based on a “social contract” between everyone in the society. At the basis of this theory, however, Hobbes also argues his famous thesis that all men are naturally selfish and that, in the “state of nature” – before men enter into the social contract – human life is “nasty, brutish and short”, “a war of all against all”.

## David Hume

Hume was born in Scotland in 1711. He was an atheist and a self-proclaimed “pagan” whose theory of human nature was an attempt to return to the ethics of the Greeks, Aristotle in particular, in which happiness and social “utility” were of the greatest importance. Accordingly, he attacked Christian virtues, such as humility, which he thought to be degrading. He emphasized the importance of having a virtuous *character*, which includes the “natural” feeling or sentiment of *sympathy* and forms the basis of all ethics. He was skeptical about the traditional emphasis on reason in ethics, suggesting that “reason is and ought to be the slave of the passions”. Because of his atheism and skepticism, Hume was never able to teach philosophy in the universities, and some of his books were condemned.

## Immanuel Kant

Kant was born in eastern Prussia in 1724. He was a pious Lutheran, and his ethical philosophy reflects his Christian sense of morality. The key to his thinking about ethics is that morality is essentially a matter of *practical reason*, and *universal law*, or what he calls the *categorical imperative*. Kant rejected both the idea that moral principles can be securely based on human feelings or “sentiments” and the idea that morals may differ from one society or one time to another. Despite his moral conservatism, however, he remained an ardent enthusiast of the French Revolution of 1789, even through its worst years. And in his great philosophical works, especially three monumental books called *Critiques* (*The Critique of Pure Reason*, *The Critique of Practical Reason*, and *The Critique of Judgment*), he set in motion his own powerful revolution in philosophy.



## John Stuart Mill

John Stuart Mill was born in 1806 in England. His father, James, was already a famous philosopher who, with Jeremy Bentham, founded the ethical movement known as *utilitarianism*. John Stuart Mill became the movement's most articulate and best-known defender. Utilitarianism is essentially the thesis that a "good" act is that which results in "the greatest good for the greatest number" of people. It is an ethics that, as the name implies, puts its emphasis on the usefulness or "utility" of actions in making people happy, or at least in not making them more miserable. It is an ethics that places far more emphasis on the good or bad *consequences* of an action than it does on the intentions according to which it is carried out. Thus, Mill and Kant are often cast as the central opponents in many contemporary arguments in ethics.

## Friedrich Nietzsche

Nietzsche was born in 1844 in a small town in Germany. He spent most of his life, however, in Italy and Switzerland, and he liked to call himself a "good European". He was trained in the classics and loved the life of the ancient Greeks, which he compared unflatteringly with nineteenth-century life. Accordingly, his ethical philosophy consists mainly of a virulent attack on Judeo-Christian morality and its religious supports. He proclaimed that "God is dead" (that is, people no longer believed in Him) and that, given that ominous fact, the morals of our society would soon collapse as well. What we call morality, Nietzsche argued, is in fact just a weapon of the weak that is used to bring everyone to the same level. Unlike most modern moralists, Nietzsche was an unabashed *elitist*, insisting that all people are *not* equal. Some people are superior, and rather than follow the rules of the "herd" they should "follow our virtues". His ethics, according to his imaginary spokesman Zarathustra, is "for a few", for those who find themselves unhealthily inhibited by the strictures of morality and who have much more to offer the world than mere good citizenship.

## Jean-Paul Sartre

Sartre was born in Paris in 1905. He is generally recognized as the definitive spokesperson for the philosophy known as *existentialism*, which he expounded in his mammoth wartime work *Being and Nothingness*, written while he was in a German prison camp. The central theme of his ethics is the concept of *freedom*. "We are condemned to be free", he writes in his usual dramatic manner. He rejects such idea as our "natural" purpose is happiness or that we are "naturally" selfish. There is no human nature, except for the fact of our freedom. We are what we *make* of ourselves, Sartre argues, and by the same reasoning, there are no moral laws or principles of reason which bind us all. Our morals are what we *decide* to do, and our principles are those which we *choose* to act upon. In accordance with this philosophy, Sartre was an ardent political reformer, committed to many causes. He died in 1980 at the age of 75.

# Business Ethics<sup>1</sup>

*Walther Ch. Zimmerli and Michael S. Assländer*

## Business Ethics as Applied Ethics

The problem business ethics – as any other applied ethics – is facing to put formal ethical considerations developed a priori into practical use in real-life situations. It becomes apparent that applied ethics in this sense must do more than just reflect on philosophical principles if it is to be of relevance in the dynamically developing real world. This means we must move away from the idea implied by the term “applied ethics” that we can simply take – from whichever source – pure ethics and apply it wherever we like. However, this makes it impossible to separate the ultimate justification of principles from practical implementation in order to solve real ethical problems, as propagated for example by transcendental pragmatics. In applied ethics there is a fundamental relationship between applying valid principles, and criticising and modifying them. In the prescriptive field this relationship exhibits structures similar to those in the field of understanding. Ethics which takes this into consideration can be called “hermeneutical ethics” (Zimmerli 1995). It can resolve the “dilemma of philosophical ethics” (Zimmerli 1990, pp. 205f.): that ethics as a theory for justifying moral norms presupposes that they are factually valid, yet must be able to distinguish between legitimate and illegitimate validations. Hermeneutical ethics resolves this dilemma thus: when applying ethical principles, it presupposes their factual validity; when however, testing their suitability in altered situations, it questions it.

Business and entrepreneurial action is determined by economic constraints. The economic decision-making process is dominated by the need to ensure stability and growth while aiming at making a profit, consolidating market position and constantly increasing shareholder value. This demand for economic rationality dominates other aspects of economic action. The ongoing public debate on the ethics of commercial strategies based purely on maximising profit and on the interests of shareholders has become increasingly relevant in recent years following

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numerous corporate collapses and scandals. Aspects being called into question include not just global ones such as the concentration of power in the hands of multinational global players, the legitimacy of European and American companies' business practices in the Third World and the way companies deal with their customers and competitors, but also internal aspects such as staff management, corporate decision-making structures and commercial objectives. As well as this, there is growing criticism of the economic and materialistic nature of our values and thinking. One reason for this is that economic theories are based mainly on the construction of models (see below); this seems to be an increasingly unsuitable method of describing "reality". Another is that the limitations of economic solutions are becoming ever more apparent.

This is where business ethics attempts to expand the concept of economic rationality by means of ethical consideration concerning economic action. Because it is applied ethics in the sense described above, it is hermeneutically structured and thus acts not only descriptively by outlining the basis of economic theories and questioning their relevance, but also prescriptively by formulating and justifying ethical criteria which economic action must meet.

## The Relationship Between Business Reality and Economic Rationality

Business ethics subjects economic reality to a prescriptive examination. But what is the reality of business? Like reality as a whole, we 'manufacture' it by means of our "ways of worldmaking" (Goodman 1978), and one of the preferred approaches in our economic civilisation is that of economic theory.

Economic theory is mainly based on the analysis of models. Economic models assume that it is possible to determine the effects of individual variables by altering them. Also, economic models are always presupposing rational economic action on the part of the subjects, i. e. that every action is directed towards maximising individual profit or minimising expected costs. The problem with this approach is that the characteristic assumptions of the models prohibit the theory from being applied precisely to reality. By starting from specially constructed premises such as the "*homo oeconomicus* principle", economic theory can only achieve a very limited degree of general applicability. By introducing the theoretical assumption that it is possible to alter one variable in the model without changing any of the others ("*ceteris paribus* clause") economics is rendering itself immune from falsification, because any deviation from reality can be explained by referring to this assumption (Zimmerli/Assländer 1995d).

The image of reality underlying economic rationality is determined by the benefit the individual achieves by means of his actions. With this action, which Max Weber describes as "goal-oriented rational action" (Weber 1922, p. 82), it is not the underlying motives or intentions which are evaluated, but exclusively the degree to which the goal is achieved, by looking at observable processes. Retro-

spectively (*ex post*), the empirically demonstrated success of a company is considered proof that the commercial decisions on which it was based were correct. This means the problem in assessing business decisions is that no evaluation criteria can be set beforehand (*ex ante*). *Ex ante*, it is only possible to make forecasts of the expected success. However, any decision which actually results in commercial success can only be proven right or wrong *ex post*, namely by the commercial success itself. *Ex ante*, all alternative actions would have to be evaluated equally, as in theory at least, they could have proved successful *ex post*.

The rationality of an action does, however, not only depend on its observable economic success, but also on the stringency of the decision given the knowledge, motives and intention of the decision maker.

This discrepancy between “economic reality” and the reality which the individual faces in the actual situation where the decision is made implies that if we take the concept of economic rationality as a measure for decisions, then it is in fact impossible to be fully informed. The concept of economic rationality unrealistically assumes that the individual is fully informed. However, full knowledge cannot be acquired, due to the individual’s limited capacity to absorb information and the transaction costs of procuring it (Zimmerli/Aspländer 1995b). Furthermore, economists who base their theories on market success are facing the problem that it is impossible to be fully informed of future events (Popper 1960). Thus, action always takes place in conditions of partial ignorance and uncertainty.

Even if all other parameters for the decision maker were assumed to remain constant or at least predictable over a specific period for short- and medium-term planning, the strategies of the other decision makers would remain fundamentally unknown. An essential factor in decisions made under conditions of partial ignorance and uncertainty is therefore that individual actors do not know what the others will do.

The individual must therefore guess what other market participants will do and base his action strategies on this. Because economic rationality implicitly expects all market participants to maximise their own profit, this motivation can be assumed for all competitors. This gives rise to at least two problems which are relevant in the context of business ethics:

- (1) Business ethics must answer the question of whether assuming that all competitors will act to maximise their profits is sufficient motivation for rational ethical action. Put differently, can egotistical behaviour based only on maximising one’s own profit lead to ethically correct results?
- (2) Business ethics must answer the question of the extent to which self-interest as a motivation to act can lead to unethical results, in other words, whether economically rational decisions can result in unethical action.

As regards (1), this question is fundamental in nature. It must be answered in order to establish whether economics and ethics can go together, or whether the two disciplines are essentially incompatible. There are three ways of looking at the matter of compatibility:

- (a) According to the idea of “market metaphysics” (Ulrich/Thielemann 1993, p. 64), the mechanisms of the market itself create equilibrium between selfish interests. For Adam Smith, this balance was the work of what he called the “invisible hand” (Smith 1759, p. 316 and Smith 1776, p. 370f.). According to this concept, the market itself introduces morality (i.e. fair distribution) to the economy.
- (b) Another view is represented by Karl Homann and Franz Blome-Drees. They looked at the position of morality in the economic system (Homann/Blome-Drees 1992, p. 20ff.) and drew a distinction between rules and moves of the game. Rules define modes of action which are permitted in business, and these require moral criteria. Moves are the strategies which players can use within the established rules; they are amoral in the literal sense of the word, in that no ethical reflection is required, since all economically useful strategies are within the set rules. Morality in the economic system is therefore positioned in the conditions within which each business subject can freely operate.
- (c) Finally, there are those who regard economic action exclusively as a means of realising other aims. In their view, moral decisions only affect the individual level. Economic action is therefore viewed as neither moral nor immoral. The decisive factor in the moral quality of the action is the individual goal of the actor. The question of adequacy conditions for economics and morality is thus returned to the level of the subject. Economic action is morally justified as long as it does not violate norms of individual ethics.

As regards (2), if ethics and economics are considered compatible, then business ethics must also answer the second question concerning “moral deficiencies” of economically rational action which are inherent in the system. In other words, are there situations where obeying the principle of economic rationality would necessarily lead to unwanted results?

Game theory provides clues to situations of this kind. Assuming economically rational action on the part of all those involved, real market situations can be described as dilemma structures. No participant in the market will give up the pursuit of maximising individual profit unless he can be sure that all the others are willing to do so too. This can be interpreted in two ways:

- (a) On the one hand orientation towards maximising profits leads to a dilemma which is desirable in the context of the market economy. Each market participant is forced to comply with the rules of the competition for fear of perishing if caught breaking them.
- (b) On the other hand this dilemma makes it difficult to enforce ethical standards. Ethical action, for example voluntarily accepting higher production costs by implementing environmental technology or offering better welfare benefits, is seen by competitors as a weakness to be exploited.

In game theory, this situation can be represented in the form of the prisoner's dilemma (Rapoport/Chammah 1965). Two prisoners are accused of having committed a crime together. They have no way of making contact with each other to come up with a common defense strategy. If both prisoners keep quiet, they can be sentenced to two years in jail for a less serious offence. If one of the prisoners incriminates the other, and the other does not talk, the King's Evidence rule applies: the witness escapes unpunished and the other is sentenced to fifteen years imprisonment. If both prisoners incriminate each other, they each receive a ten-year sentence.

Regardless of the strategy of the other prisoner, from an individual point of view the non-cooperative strategy appears best. If both prisoners act rationally, they each receive ten years in prison. In this case, rational strategies have worse results for both prisoners than they would have been able to achieve by cooperating.

This means that economically rational action does not necessarily lead to the best results for all those involved. This is where business ethics must develop methods and decision-making rules which can break out of economic dilemma structures. The dilemma's underlying rewards matrix must be changed using positive and negative incentives so that ethical behaviour is perceived as being worthy of reward and unethical action is avoided (Assländer 1998, p. 323ff.).

## Ethical Assessment Methods

In today's modern market economy, an ethical system must meet three conditions (Zimmerli/Wolf 1993, p. 316):

- (1) Ethics must be oriented towards problems, instead of principles. Formal (universal) and material (situational) principles are integrated in ethics so that differentiated decisions can be made according to the situation.
- (2) It is often forgotten that plurality of values requires an irreconcilable difference between value systems and therefore not consensus but disagreement. This means models must be developed for dealing with disagreement.
- (3) Orientation towards the consequences of technological and economic action must take priority. In other words, it becomes a matter of (deontological) conscience to be a (teleological) ethicist of responsibility.

Discussions on morality within the pluralistic value systems of market economies must be restricted to formal ethics. Material ethics are subject to individual preferences. By reducing dissensus on formal moral values, this problem-based concept allows for dissenting on values from a material point of view.

Ethical evaluation of each action must follow a four stage procedure from top to bottom (fig. 1). Anything that cannot be decided on the top level as "required" or "forbidden" is put in the category "undecided" and dealt with on the next level,

**Table 1.** Four-level model of ethical assessment according to Zimmerli/Wolf

	forbidden	further clarification	permitted
1) formal principles			
2) regional principles			
3) professional principles			
4) material values			

and so on. Amongst the formal principles (1<sup>st</sup> level) there are the ethical principles of modern reason (such as universalizability, equality, justice), while the regional principles (2<sup>nd</sup> level) include principles limited to particular times and places (such as worst case priority). The professional principles (3<sup>rd</sup> level) take account of the specialisation between various professions in society in the form of professional ethics (such as the principle of informed consent). It is only on the lowest level (4<sup>th</sup> level) that material values come into effect.

This model meets the requirements for the pluralism of values typical in market economies and shows the extent to which moral action requires a general problem-oriented ethical system.

### Moral Qualities of Economic Action

In addition to criticising system-inherent weaknesses of decision-making rules and suggesting the above mentioned procedural model, business ethics must also question the moral quality of economic action. In other words, it must examine the extent to which economically rational action is leading to commercially desirable results, yet transgresses basic moral norms. This requires an in depth analysis of individual economic and entrepreneurial decisions. For example, do the WTO rules for international commerce violate the principle of fairness? How is Germany's current employment policy to be viewed in moral terms? Which ethical norms apply when managing staff or dealing with external stakeholders in the company?

On the whole, it appears that economically oriented thinking has led to a paradigm shift in this respect. Moral action is no longer based on the obligation to obey a "moral law" (Kant 1788) or to promote "the greatest possible quantity of happiness for the greatest number" (Bentham 1789). Instead, one of the necessary conditions of moral action is that it does not result in an economic disadvantage. Moral imperatives or prohibitions only seem to be relevant in decision-making processes when they do not conflict with economic interests.

Many managers in particular fail to distinguish between economic and moral imperatives (Ulrich/Thielemann 1993; p. 54–91). Only a small minority of managers take up the challenge of exploiting commercial possibilities with the aim of promoting morality. However, if we look at the commercial decision-making process, we see that decisions within the company are not made and implemented by one manager alone. Decisions in large organisations are usually the result of more than one individual's intention to take action. This often results in a decision which suits none of them. Decisions are thus subject to an organisational selection process which is to a large extent determined by the interests of decision makers in the company rather than by rational considerations alone. This makes it difficult to clearly assign responsibility for economic action within organisations.

The arguments of economic thinking described above raise the suspicion that many managers think any economically rational action is justified as responsible action within certain general conditions. They believe that the market alone decides whether or not economic planning and action is morally acceptable. According to this attitude the market sanctions incorrect behaviour such as transgressions of group standards and irregular business relationships with their own customers. However, this attitude is questionable in at least two regards:

- (1) This way of looking at the market as a mechanism to determine what is right or wrong only allows evaluation *ex post*. Therefore, market acceptance cannot be used as a criterion for making decisions, because it cannot provide a measure for assessing correct behaviour *ex ante*.
- (2) This approach ignores the fact that this sanctioning mechanism can only apply to the very limited area of responsibility for economic action which concerns the direct and immediate consequences. It does, however, ignore accumulative and synergy effects, as well as long-term consequences, since these are not sanctioned by the market alone. Therefore, the concept of economic responsibility must be expanded.

## Responsibility for Economic Action

“Responsibility” is a three-term notion requiring at least three aspects: the subject of responsibility, the object or field of responsibility, and the instance of responsibility (Zimmerli 1987, p. 102ff). Additionally, a distinction must be made between retrospective responsibility such as liability in a purely legal sense, and prospective responsibility, which also refers to the subject's feeling responsible.

- (1) In the strictest sense, the subject of responsibility can usually only be a single individual (for “secondary moral actors” see “Addressees of Moral Norms”). Increasing frequently however, decisions are made by teams and implemented by organisations. The traditional identification of the subjects of responsibility and action must therefore be dispensed with (Zimmerli/Assländer 1995a).



- (2) The object or field of responsibility – that for which the subject is responsible – includes the action and its intended (and unintended) consequences and side effects. “Action” refers to doing something as well as intentionally avoiding to do something (Birnbacher 1995), including simple verbal acts. The constant increase in technical knowledge without a comparable increase in prior knowledge of the consequences of actions means that the power to act and the power to control are drifting apart. Above all, the transfer of steering and controlling functions to machines means that despite our increased technical knowledge, we are less aware than ever of the results of our actions.
- (3) The instance of responsibility is what the subject must answer to. As well as individuals and formal institutions such as courts, professional organisations and arbitrators, also informal institutions can be instances of responsibility. These can include public opinion, peer assessment and one’s own conscience. Because human activity and its consequences not only affect today’s world but also the lives of future generations, the concept of the instance of responsibility must be expanded to include people not yet born.

This gives rise to the following questions for business ethics: (1) Who are the subjects of responsibility for economic action? (2) Which effects of economic action are they responsible for? (3) How can suitable instances of responsibility be set up to assess the moral quality of economic action?

(ad 1) The subject of responsibility is normally a natural person. This is evident from the very concept of responsibility itself. However, individuals can take on responsibility on behalf of an institution, although the institution itself only bears indirect responsibility. This may explain why some ethicists in business ethics and elsewhere have come to believe that institutions and corporations can become subjects of responsibility in the strictest sense of the term (Werhane 1992). However, the concept of responsibility in the strict moral philosophical sense includes both prospective and retrospective components, i.e. it refers to the anticipatory feeling of responsibility at the time of the action, as well as being responsible and being called to answer for the consequences afterwards. The problem is that although an institution can be allocated a responsibility in terms of legal liability, a company cannot feel responsible. Strengthening individual awareness of responsibility and moral authority is therefore a matter for business ethics.

(ad 2) Estimating the extent of the consequences of economic actions is all the more difficult the more people are affected, the more irreversible the processes initiated and the later the expected pay-off on the investments. On the one hand this is due to some of the evaluation criteria, which make it more difficult to rationally estimate future benefits and disadvantages (a–d). On the other hand, the implementation of technical methods of analysis and control cause problems in anticipating the consequences of actions affected by these systems (e).

- (a) First, a “pure time preference” (Birnbacher 1988, p. 29) makes it difficult to rationally estimate the future consequences of actions. People making the decision pay less attention to future positive and negative consequences of actions than they do to present ones, precisely because they are in the future.
- (b) Second, decision makers have a “preference for current preferences” (Birnbacher 1988, p. 29): this means they rate future preferences which may be different and which they may not share lower than their current personal preferences.
- (c) Third, the “ego preference” (Birnbacher 1988, p. 29) means that we treat consequences which only affect others with much less importance than those that affect us directly.
- (d) Fourth, the “moral distance” (Birnbacher 1988, p. 29) means that we perceive consequences which affect those who are close to us as being more serious than results that affect those who are not.
- (e) Fifth, the transfer of steering and controlling functions to machines leads to the “paradox of information technology” (Zimmerli 1987, p. 104). Decisions to act are taken according to the standard values of technical analysis systems, which thus can no longer be controlled. The consequence is the loss of direct human monitoring of human actions.

Therefore, business ethics must develop adequate procedures of evaluating the consequences of economic actions.

(ad 3) Economic action must be justified to various instances of responsibility. However, when making a business decision, usually only the formal instances are taken into account. Legal conditions and professional codes of conduct form the framework within which economic action can be taken. Informal moral instances such as God, future generations or the common good are often not considered relevant when business decisions are made. Business ethics attempts to develop methods and solutions introducing responsibility also to informal instances as a factor of making business decisions. It is possible, for example, to use methods of discourse ethics to include those affected by economic action in the decision-making process (Zimmerli/Assländer 1995a). Demonstrating ways of implementing informal instances of this kind in corporate organisational structures is an additional concern for business ethics.

## Addressees of Moral Norms

When developing moral norms for acceptable economic action, we must ask ourselves who they are aimed at. Opinions on this fall into two opposite camps. On the one hand, there are approaches which attempt to look at the company as a whole, and to address moral imperatives at corporations themselves. On the other hand, there are those who believe that moral norms can only be addressed to indi-

viduals, as only individuals are able to reflect on them and take them into account in their decisions.

Patricia H. Werhane assumes that when corporations claim the right to freedom and autonomy, they also claim them as moral rights. This leads her to conclude that these moral rights necessarily bring with them moral obligations. Therefore, corporations are to be held morally responsible for their actions (Werhane 1992, p. 329). This responsibility concerns those aspects of economic action in which companies as productive organisations must take on the role of responsibility towards their customers and staff, as well as towards society, and includes not only legal liability, but also elements of prospective moral responsibility (Assländer 2001, p. 90).

Corporations are secondary moral actors: their secondary actions are composed of the primary actions of rational adults. Because rational, independent adults are capable of primary moral or immoral acts, corporations are capable of such acts on a 'secondary' level (Werhane 1992, p. 330). From this capability of carrying out "secondary" acts, it can be concluded that corporations enjoy secondary moral rights, but equally, have corresponding moral obligations.

It is unimportant whether these obligations apply to a corporation or an individual. The moral obligations of corporations extend to the individuals who constitute the corporation's intention to act. The following features of corporate rights are to be considered:

- (a) Because they are only valid as secondary rights, they cannot replace justified claims on primary rights of individuals.
- (b) Corporations cannot themselves administer their claims to rights: they must always rely on the individuals acting for them.
- (c) Finally, the rights of corporations are of a collective rather than aggregate nature, because they are assigned not to multiple individuals, but to the corporation itself.

If corporations claim certain rights, then they must also recognise those of other corporations or individuals, as otherwise they would violate the principle of equal treatment. From this Werhane concludes that a corporation cannot enjoy more freedom than it grants to its members (Werhane 1992, p. 334).

This position, where corporations have moral rights and obligations, is disputed by authors such as Oswald von Nell-Breuning. He believes there is an interaction between the individual and the collective, because whereas the individual depends on the collective for his or her freedom to act, the collective depends on the cooperation of all its members. Therefore, the individual is responsible for the collective wherever he or she exerts an influence on it (v. Nell-Breuning 1968, p.20).

Oswald von Nell-Breuning sees businesses ("Unternehmen") as undertakings ("etwas unternehmen"), working together to achieve a common goal (v. Nell-Breuning 1983, p. 65ff.). Those who co-operate in realising an undertaking of this kind therefore have the same moral rights and obligations. These rights and obligations apply to their dealings not only with each other, but with outsiders too.

Individuals must do business in order to secure the economic basis of the company. We can call this aim the *finis operis*, or purpose of the work (v. Nell-Breuning 1963, p. 32). In contrast to this there is the *finis operantis*, which is the intention of the individual worker (v. Nell-Breuning 1963, p. 33), for example, literally making a living. Where they conflict, the purpose of the work must give way to the intention of the worker. Even if the individual operates within a corporation and must act on its behalf, he or she is responsible for moral action and is free to act in his or her own interest. The crucial factor in individual responsibility is that corporate decisions cannot be asserted against the will of individuals. Each individual is free to leave the company and thus refuse to participate in decisions which they do not want to be responsible for.

## Analysis of Business Ethics (Systematic Classification)

Generally, approaches to business ethics can be classified using two criteria (Zimmerli/Assländer 1994). On the one hand, business ethics approaches can be classified according to the systems they refer to. On the other, they can be classified according to the actors they address (Table 2).

The systems theory approach breaks down business ethics into micro-, meso- and macro-levels (Lenk/Maring 1992a, p. 19; Homann/Blome-Drees 1992, p. 14):

- (1) On the macro-level, business ethics examines the state, the economic system and society as a whole. This is referred to in the literature as business ethics in the strict sense of the word.
- (2) On the meso-level, business ethics is dealing with moral problems of companies, corporations, organisations and their actions. For this the term “corporate ethics” has become established.
- (3) On the micro-level, business ethics attempts to answer questions on how individuals can act in a morally sound way within the business field.

This analysis is largely based on the classification of business ethics which has become established in English-speaking countries since the mid-1970s (DeGeorge 1992, p. 302).

The actor-based classification breaks business ethics down according to individual and institutional ethical paradigms. This method of classification focuses not on the systematic order of the subject of analysis, but on what the respective theory says about the subjects of action and responsibility.

The individual ethical paradigm starts with the individual as the subject of responsibility: because only the individual can develop moral competency, it is concluded that also within the business process, moral problems only arise in the actions of individuals. The institutional ethical paradigm takes the insight that business decisions are not implemented smoothly by individuals, but increasingly by institutions, and concludes from this a need to expand the concept of responsibility used by traditional ethics to corporations.

## Classification of Approaches to Business Ethics on the Macro-, Meso- and Micro-levels

(1) On the macro-level, business ethics examines the compatibility of fundamental economical concepts with prescriptive ethical statements. Subjects discussed include the following:

- socio-political aspects such as the basic well-being of individuals in industrial societies (v. Nell-Breuning 1975), civil liberties (v. Hayek 1960) and reflexiveness of economic processes (Fromm 1976),
- the consistency of economic theories like problems of the postulation of value-free judgement (Eucken 1939), or problems of economic rationality (Vossenkuhl 1992, Assländer 1999), and
- consequences of economic policy such as the “third world” (Zinn 1990), environmental policy (Thielemann 1990) and development aid (Gore 1992).

(a) Descriptive approaches to business ethics attempt a critical analysis of existing economic theories. They aim at detecting ethically deficient developments resulting from these theories, and to identify discrepancies between the characteristic assumptions of the economic theories and the social reality of the individuals affected. Descriptive business ethics also endeavours to analyse the interdependencies between various systems, such as economic and legal systems.

(b) Prescriptive approaches to business ethics attempt to change economic conceptions with the aim of facilitating moral action. This includes creating structures to allow all individuals affected by economic decisions to have a say in them. They propose replacing an incentive system which only rewards economically rational action with one that rewards action which is morally right. With regard to their consequences, economic systems should take greater account of social justice.

(2) On the meso-level, questions of corporate ethics are discussed, for example:

- aspects of corporate responsibility such as the side effects and consequences of companies' actions (Ladd 1992), allocation of responsibility in changing economic and technical circumstances (Zimmerli 1987), creation of awareness for responsibility (Lenk/Maring 1992b),
- ethical aspects of corporate management such as the discrepancy between individual moral concepts and requirements of the market (Gerum 1992), moral values in corporate management (Ulrich/Thielemann 1993) and socio-economic aspects of economic action (Etzioni 1993a), and
- the moral dimensions of corporate goals such as internalisation of external responsibility (Zimmerli 1994), defining corporate codes of conduct (Rath 1990; Schmidt 2002), and strategic advantages of moral action (Wieland 1993).

(a) Descriptive approaches to business ethics study value orientation in corporate management, analyse how incorrect ethical decisions arise, and identify ineffi-

ciencies in the corporate structure and culture which create difficulties in asserting moral standards. They also focus on problems in allocating responsibility in large organisations and in creating a “moral identity” in companies.

(b) Prescriptive approaches to business ethics promote changes in entrepreneurial action. Moral aspects should be given the same priority in the decision-making process as economic considerations. Companies must therefore help alter structures on the macro-level to prevent immoral action. In addition to this they must create internal structures to develop moral value orientation among members of the organisation and prevent cognitive dissonance between moral values and economic necessities.

(3) On the micro-level business ethics studies the behaviour of individuals in the company and of the individual as a subject of economic action. The aspects studied include:

- responsibility of the individual in the company, creation of a common understanding of responsibility (Schreyögg 1989), responsibility for one’s own intentions included in the decision-making process (Zimmerli 1987), and responsibility for preventing unwanted occurrences (Alpern 1983), and
- changing decision-making behaviour according to the role ethics in the company, in other words the feeling of duty to act in the interest of the company (French 1992), and cognitive dissonance between the business task and individual morality (Gentz 1993).

(a) On the micro-level, descriptive business ethics study the effect of roles on morality, moral aspects of individual action in the economic context, and the individual values underlying that action.

(b) Prescriptive business ethics attempts to help individuals in their decision making allowing them to be linked to ethical justification. The aim is to create moral awareness for the ethical aspect of economic action.

## Individual and Institutional Ethical Paradigms

(1) According to the individual ethical paradigm, the subject of morality in the economic decision-making process is always the individual. Because only the individual is able to experience a prospective feeling of responsibility, only the individual in the strictest sense can be the subject of responsibility for economic action. Some authors admit there can be a discrepancy between the subject of action and the subject of responsibility (Zimmerli 1987, p. 109), due to the increase in organisational action. However, here too they assume that responsibility is held by individuals, because they are (at least indirectly) involved in making the decision. Approaches to business ethics which follow the individual ethical paradigm deal with questions such as the following:

- responsibility of the individual: fields of study include the range and expansion of the concept of responsibility (Jonas 1979; Zimmerli 1987) and problems in anticipating responsibility (Birnbacher 1988),
- promoting individual moral authority using case studies (Hennessey/Gert 1992), and by specifying individual decision-making rules (Koslowski 1988b),
- analysing individual behaviour patterns, such as examining role ethics (Mead 1934) and analysing moral shortcomings in management (Hansen 1989).

(a) Descriptive approaches to the individual ethical paradigm describe morally wrong behaviour in the context of economic action, study the effects of individual moral behaviour on corporate and business practices, and analyse moral justification strategies. The values and intentions of decision makers are also subject of descriptive analyses.

(b) Prescriptive approaches to business ethics which follow the individual ethical paradigm attempt to effect a change in economic action. The individual must be aware of the ethical dimension of his intention during the decision-making process, even if he or she is only indirectly involved.

(2) Approaches which follow the institutional ethical paradigm do not regard ethical norms as being addressed to the individual only. If corporations present themselves as subjects of action, then they must take responsibility for the consequences of their actions. Based on the observation that individuals tend to decide in the interests of their respective company, even if this occasionally conflicts with their own moral views, the institutional ethical paradigm contends that corporations have an “intention to act” of their own. This, however, is only manifested in the decisions of the individuals who represent the company. As well as this, the institutional ethical paradigm includes approaches dealing with the framework for moral action in the company or within general economic conditions. Here, the following questions are of interest:

- How can we conceive of companies as moral agents? In detail, this means: can corporations be said to have an “intention” (French 1992)? Do corporations have moral rights and obligations (Werhane 1992)?
- Do corporations have responsibility: are corporations responsible for their business policy (Weiss 1994)? How can corporations deal with this responsibility (Lenk 1994)?

(a) Descriptive approaches to the institutional ethical paradigm study decision-making structures and behavioural patterns in corporations, providing insight into whether there is a corporate “intention” shared by all the decision makers.

(b) Prescriptive approaches to the institutional ethical paradigm are directed at the company itself. The aim is to redefine the “intention” of the company.

**Table 2.** Summary of the systematic classification of business ethics

	<b>Individual ethics</b>	<b>Institutional ethics</b>
Microscopic level	e.g.: Questioning the responsibility of the individual in the economic decision-making process	e.g.: Questioning the internalization of specific corporate intentions of acting
Mesoscopic level	e.g.: Questioning the changing organizational structures that allow individual morality	e.g.: Questioning the responsibility of corporations for consequences of acting
Macroscopic level	e.g.: Questioning the influence of economical processes on the self-conception of an individual	e.g.: Questioning the role of corporations in the politics of economy

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# Habits of the Heart in US-American and German Corporate Culture

*Bettina Palazzo*

*Our future economic success depends on how well we understand the deepest motivations of our trading partners. It takes more than language skills and etiquette lessons to plumb the complexity of desires and actions we can barely recognize in ourselves.*

Charles Hampden-Turner/Alfons Trompenaars

The accelerating globalization of economic transactions provokes the impression that human values and patterns of behavior will sooner or later converge into one worldwide culture. This assumption seems to be especially true for the business world with its ‘culturally invariant rules of the market’. In fact, however, this convergence of the various business cultures of the world takes place only on their very surface and does not reach the different fundamental value systems. They are the result of a mostly unconscious and complex process, having developed over centuries, and thus resisting short-term change.

Tocqueville called these shared cultural standardizations “habits of the heart”, i.e. the common patterns of thinking, feeling and acting within a certain group or society. Since they are habits of the heart we are oftentimes unaware of their influence. They are taken for granted and only become conscious when put into contrast to other cultures with different tacit background assumptions. Then they always have the potential for intercultural misunderstandings and conflicts, mutual value violations, frustration, and in the case of business may block communication, and thereby risk corporate efficiency.

I want to give some examples about how the national habits of the heart influence the way American and German corporations deal with values.<sup>1</sup>

Today many American companies have developed a very explicit way in their management of values and introduced so-called business ethics programs.

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<sup>1</sup> I am not dealing with the role the specific corporate cultures may play. Since people are first socialized within their national culture, its influence is usually more fundamental.

They have written Codes of Ethics to manifest the company's ethical value system, to provide rules and orientation for employees, and to signal their commitment to their outside stakeholders.

They implemented Ethics Committees of the Board of Directors to integrate ethics at the company's top-level, communicate the concern for ethics to the outside world, and back the ethics program with the necessary political impact needed for the resolution of touchy issues.

This committee is supported by the Ethics Office that handles and coordinates all aspects of ethics management on a day-to-day basis. It runs the company's Ethics Trainings and enforces and controls the whole process. It communicates the Ethics Code and answers employees questions.

To facilitate this advice task some companies even installed a toll-free Ethics Hotline. The head of this department – the Ethics Officer – serves as an ombudsman for employees, investigates alleged violations, and reports to the board.

To monitor the effectiveness and the success of these activities the Ethics Office runs an Ethics Audit. This instrument tries to survey whether the employees know the code, are able to deal with ethically sensitive situations and what aspects or parts of the company's ethics program might need adjustment.

The motivation to implement and run such extensive corporate programs has many sources and ranges from the genuine need and will to be a "good corporate citizen" to the simple and purely self-interested wish to avoid bad reputation, public pressure, and legal consequences in case of corporate misconduct.

Certainly one very important legal incentive for US companies are the Federal Sentencing Guidelines (Dalton et al.). This reform of criminal law, which came into effect in 1991, aims at the stricter prosecution of organizational offenses. In addition to raising the amount of fines for, e.g., corruption and environmental crime, the guidelines give judges the possibility to mitigate the suggested sentence by as much as 5% of the initial fine, if the offending corporations have shown "due diligence" in securing the law-abiding conduct of its employees. One possibility to meet this requirement is the existence of an effective business ethics program. This carrot-and-stick-principle encourages many companies to install business ethics programs.<sup>2</sup>

German companies on the other hand, although they increasingly see the need for creating a shared vision of the norms and values within their organizations, are very reluctant to publicly address normative questions and they tend to keep relying on a traditional but fading business ethos.

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<sup>2</sup> According the EOA 2000 member survey most Ethics Officer positions have been introduced after 1991. 53% of the 150 responding organizations state that their ethics program had been introduced in response to the Federal Sentencing Guidelines. During the period of 1994 to 2000 94% of the respondents have revised their code of conduct. These numbers show the motivating influence of the Sentencing Guidelines quite nicely.

Almost exclusively the business ethics instrument that is found in German companies are mission statements (Unternehmensleitlinien) (Ulrich et al., KPMG). And even in these documents the actual words “ethics” or “integrity” or “morality” almost never appear.<sup>3</sup> Furthermore, questions of business ethics are often dealt with more implicitly in the context of general and more holistic programs in organizational development or corporate culture. Business ethics programs in the American understanding are still a big exception in German companies.<sup>4</sup>

This is basically also the result of the survey Ulrich et al. conducted in 1996 with the 500 biggest German and the 200 biggest Swiss companies. When asked after their current situation in the implementation of business ethics measures their answers revealed a mixture of ignorance, skepticism and uneasiness, but also the feeling that business ethics is about to become a pressing issue. Over 50% of the respondents admitted that they had never heard of ethics officers, ethics hotlines, or ethics audits (Ulrich et al. 34). 21% of the German respondents reported that the very word “ethics” is being avoided in their company (Ulrich et al. 34). Some respondents even felt insulted by the suggestion that they should introduce formal business ethics programs and reacted with indignation (Ulrich et al. 44). Only 16 of the 67 (= 23,9%) responding German companies had Codes of Ethics.

Nevertheless, 42 % of the respondents said that they were planning business ethics measures. This gives the authors of the survey reason to believe that there is a slow but steady trend towards a growing acceptance and implementation of business ethics programs.<sup>5</sup> Of course, one reason for the still relatively slow development in Germany is the lack of a strong legal incentive such as the Federal Sentencing Guidelines in the United States. On the other hand, as my article will show, there are also a lot of “cultural barriers” to the implementation of business ethics in German companies. I do agree, however, with Ulrich et al., that this hesitant attitude is slowly but surely fading, since other pressures, like the increase in corporate crime or the value problems of globalization, increase the need for business ethics.

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<sup>3</sup> Cf. Lenk, H./Maring, M. (ed.): *Wirtschaft und Ethik*. Stuttgart 1992, pp. 353ff. The mission statements and codes of conduct collected in this publication avoid the „e-word”. Only the business principles of the German subsidiary of the American company IBM deal explicitly with ethics. The more recent survey conducted by KPMG re-confirmed this general tendency.

<sup>4</sup> Among these exceptions are, e.g., a few Bavarian construction firms that formed an association to avoid the problems of bribing so common within their industry. Cf. *Ethikmanagement der Bauwirtschaft e.V.* „Ethikmanagement-System für die Bauwirtschaft in Deutschland.“ In: Wieland, J./Ulrich, P.: *Praktische Unternehmensethik*. Bern 1998, pp. 239-254.

<sup>5</sup> Cf. Ulrich et al. 38. Of course this figure has to be taken with caution, since, respondents probably tend to answer this question positively because they feel this to be socially expected.

## “Public Moralizing”: Privacy vs. Publicity

One reason for the German uneasiness about business ethics programs can be seen in their resentment of public moralizing. We are obviously dealing with different cultural standardizations of the relationship of the public and the private sphere.

In general the separation between the public and private sphere in Germany is stricter than in the USA. Morality is mostly considered as belonging to the realm of one’s private life, whereas one’s professional life is considered to be part of the public sphere (Hampden-Turner/Tompenaars 224).

The demarcation line between public and private becomes evident already in our architecture: in German houses the entrance door usually leads into a hallway, whereas in most American houses you directly enter the living room.

The popularity of garden fences and the “closed door policy” (Samovar/Porter 268) in German offices are other examples of the need to shelter one’s privacy from the outside.

Correspondingly, Germans also shelter their ethical sentiments from the public sphere. Therefore, an invasion of this emotional harbor by an employer is rejected.

The private space of Americans is much smaller. There are only few things that are considered to be a strictly private matter. Consequently the prescription of corporate values is more acceptable for American employees. These value codes are not seen as an intrusion into their private life, but as the code of conduct valid during their work hours (Hampden-Turner/Tompenaars 224).

This different notion of privacy can be explained through history: Germans had to shield their private territory from an intruding state (Obrigkeit). The result of this separation was a split morality – one for the private sphere and one for the public sphere. The Nazi regime tried to reunite the two spheres by introducing a national ethic of comradeship. Of course, this totalitarian endeavor resulted in even greater resentment against any public invasion into private morality until today.<sup>6</sup>

That public moralizing is accepted in the USA and has its roots in dissenting protestantism that propagated a political right to opposition. If a ruler did not obey the divine law, his people had the right to dismiss him. Consequently, they also had the right and the duty to judge whether their leader’s behavior was morally correct. To be able to do so the public has to have access to relevant information on their ruler’s moral behavior. Correspondingly, it was also in the very interest of the ruler to publicly communicate his moral integrity. Therefore, the borders between the public and the private spheres are much more permeable than in Germany.

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<sup>6</sup> The relationship between the public and the private sphere is extremely complex, especially if we would want to consider its historical development. Therefore it has to be noted that I can only give a very simplified summary here. See Jürgen Habermas. *Strukturwandel der Öffentlichkeit. Untersuchung zu einer Kategorie der bürgerlichen Gesellschaft*. Frankfurt: Suhrkamp, 1990. Stephen Kalberg. „The Origin and Expansion of Kulturpessimismus: The Relationship between Public and Private Spheres in Early Twentieth Century Germany.“ *Sociological Theory*, 5 (1987): 150-164.

Protestantism also enhanced the public communication of morality within the American business culture: A business man's reputation as a Protestant assured his customers and suppliers that he was trustworthy and fair. Therefore, it was vital for the successful business man to demonstrate his moral decency in public (Weber 279-317).

Today's public control of corporate morality by the consumer movement, ethical investment funds and other interest groups continues this tradition. Also because of this tradition American corporations, compared to Germany companies, are more open to communicate and cooperate with these groups.

## **“Only Law Is Sovereign!”: Individualistic Universalism vs. Collectivistic Particularism**

*America is all one prairie, swept by a universal tornado.*

George Santayana

Many US corporations are using formal Codes of Ethics to communicate the moral standards valid for them.

This way of dealing with ethical issues within corporations strikes Germans as strange, since they feel that this does not have much to do with ethics at all, since it “only” aims at legal compliance. Ethical behavior goes further than legal behavior, and it is per definitionem impossible to legislate genuine ethical conduct.

In fact American business ethics often seem to be rather legalistic. Obviously Americans tend to understand ethics in terms of compliance to a certain set of universal rules (“to play by the rules”). The popularity of checklists, guidelines and principles makes this evident. Thus it comes as no surprise that ethics codes are much more common in the USA than in Europe.

This tendency can be explained by the individualistic nature of the American culture and society. In general individualistic societies are characterized by an universalistic approach towards ethics. That means that they believe that all humans are equal and deserve the same rights. Norms and values are valid for everybody and are expressed in universal duties the individual has to live up to. In an individualistic society like the USA it seems necessary to define fixed rules for everyone to comply with to keep this community of “unencumbered selves” integrated.

The American moral universalism also manifests itself in the strong belief in the existence of universally valid norms and values and their sometimes missionary efforts to convince others of their standards.

Besides being the characteristic moral orientation in individualistic societies, moral universalism in the USA has its roots in the American religious tradition of dissenting protestantism: according to this doctrine even the rulers had to adhere to the divine law and if they fail to do so, it is the holy duty of their subjects to end their rule.



Therefore, a set of rules put down in an ethics code has not only the function to co-ordinate and avoid conflicts but first and foremost pursues an egalitarian aspect. In contrast to informal systems, fixed rules are (at least ideally) valid for all employees (Vogel 38).

This can also be understood by looking at American history: Since many different cultures came together in the new world, the new community could not rely on shared traditions for ethical behavior and a common sense of justice. E.g. according to a survey of 1915 over 50 languages were spoken at the Ford factory in Highland Park (Fukuyama 301).

The preference of universal rules got enhanced by the dominance of the Tayloristic principles of organization in American companies that resulted in a tight web of formal rules controlling the employees (Fukuyama 301).

Compared to the USA, European societies are more community-oriented. Therefore, the preferred moral orientations tend to be more relational than in the USA. Moral principles and behavior depend more on the situation and the role somebody plays. Furthermore the Tayloristic approach was never as dominant as in American companies. The German system of vocational education (Lehrlingsausbildung) softened the effects of Taylorism and insured a higher level of employee competence (Fukuyama 274-289). This resulted in a more confident and trusting relationship between workers and managers. Consequently German companies rely more on informal mechanisms of social control. The ethical expectations and norms in a German company are usually transmitted informally and are not made explicit. It even seems to be somewhat rude or barbaric to openly tell employees what kind of ethical attitude and behavior is expected of them. This would communicate to the employees that their superiors do not think that they are capable of making an ethically responsible decision on their own.

The rise of corruption, white collar crime and corporate crime in German corporations<sup>7</sup> suggests that this relational value basis is changing and the effectiveness of the traditional, informal control mechanisms is fading.

Obviously the German business culture is presently in the middle of a value shift concerning business ethics. The above mentioned survey of Swiss and German entrepreneurs (Ulrich et al.) illustrates this double bind situation: Although many of the respondents said that they felt a growing need for business ethics, they often reject the idea of implementing formal business ethics programs. Instead they kept referring to a traditional entrepreneurial ethos and refused to explicitly examine the normative foundations of this ethos. In the case of corporate and white collar crime this oftentimes leads to a strong resistance to deal with questions of corporate integrity or even the denial of the whole problem.

The conventional business ethos in Germany is not only crumbling, it is just no longer capable to live up to the complexities and the dynamics of a modern globalized economy. When also in Germany the workforce is becoming more

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<sup>7</sup> Cf. KPMG Survey on White Collar Crime in Germany, Berlin 1997.

divers and heterogeneous corporations can no longer rely on traditional ethical norms and values.

The fading of the traditional business ethos is one phenomenon within the general process of modernization and individualization in our society. Therefore, in the near future also German companies will have to invest into some form of ethics management. Of course, they will have to proceed in a less explicit way than American corporations. E.g. when developing and implementing a code of ethics, German corporations should carefully avoid the impression that they are forcing it on their employees, but proceed with a high level of employee participation. Furthermore the universal declaration of material norms and values, common in American compliance-style codes of ethics should be avoided. Ethics programs in German companies have to be more relational.

There should be more room for the interactive, situational settling of ethical problems and more discretionary power for the employees and managers. This modification is also necessary because a too explicit and rigid prescription of rules of behavior tends to conflict with the German conception of employee privacy and runs the risk of being interpreted as a signal of distrust.

## Conclusion

*Cross cultural communication involves predictable conflicts of perspective, such conflicts constitute dilemmas, these dilemmas are resolvable and once resolved represent integrations of knowledge of far greater value and richness than was realisable for the initial conflicts.*

Charles Hampden-Turner

*There will be no 'there' any more. We will all be here.*

Slogan for MCI Telecommunications

Since in a globalized economy we can no longer rely on the stabilizing effect of shared values and norms, the professional and proactive management of values will gain importance.

For the success of this endeavor it is vital to be aware of the potential value conflicts between the various global business cultures.

To avoid the dangers and pitfalls of intercultural misunderstandings and mutual value violations corporations have to develop organizational programs and structures that enable a mutual process of cross-cultural learning.

A first step on this admittedly difficult path is the identification and awareness of the existing intercultural differences and their consequences. In this process business ethics programs can be a useful tool for the identification and proactive management of intercultural conflicts. Doing this, it is important to avoid cultural relativism as well as cultural imperialism. Instead mutual learning in this context

means to stay rooted in ones own cultural background, but at the same time transcend it and create the minimal value consensus that lies at the heart of all forms of fruitful economic cooperation.

In doing this the differing habits of the heart and the instability of cross-cultural business transactions can be seen as a chance for the innovative development of organizations and thus contribute to economic success.

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PART II:

## **Leading Self and Others**

# The Importance of Leadership in Shaping Business Values<sup>1</sup>

*Joanne B. Ciulla*

Few doubt that leaders play a role, either as founders or promoters of values in organizations. So the more important question is not “Whose values?” but “What values?” Just because a leader has values doesn’t mean that they are good ones. Furthermore, the question is not so much about what a leader values, but what a leader actually does to demonstrate his or her values. This paper is about how leaders translate values into action and actions into enduring organizational values. I first examine how we have come to think about the values of business leaders and success. I also reflect on what theories of leadership say about how leaders influence followers. Then I argue that the language of having values is often inadequate for understanding individual and organizational ethics. Lastly, I look at the leadership of P. Roy Vagelos of Merck & Company to illustrate the how the values of founders and current leaders shape the values of their own organizations, and can shape the values of the industries in which they operate.

## **Old Assumptions About the Values and Virtues of Business Leaders**

Some of our attitudes towards the values of business leaders can be traced to the Protestant work ethic, which included the belief that accumulation of wealth was a sign that one was among God’s chosen. One of the Calvinists’ favorite Biblical passages was “Seest thou a man diligent in his business? He shall stand before kings” (Proverbs xxii 29). This equation of business success and salvation seemed to stick even in the secular world. In the 18th century, Benjamin Franklin tempered the Protestant work ethic with enlightenment ideals. He believed that business leaders should strive for wealth so that they can use it in a humane way to help society. Franklin thought good character was necessary for success. In his autobiography he listed eleven virtues needed for success in business and in life:

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temperance, silence, order, resolution, sincerity, justice, moderation, cleanliness, tranquility, chastity, and humility. Virtues tell us what we should be like and what we have to do to be that way. Values are what we believe to be important or morally worthy. We usually assume that values motivate us to act, but this isn't always the case. Some are satisfied to have a value and not act on it. This is not possible with a virtue. A person may value courage, but never do anything brave or heroic, whereas one cannot possess the virtue of courage unless he or she has done something courageous.

America is somewhat distinct in its history of celebrating the values and character of business leaders. For example, in the 19th century, William Makepeace Thayer specialized in biographies of chief executive officers. His books focused on how the values leaders formed early in life contributed to their success. Thayer summed up the moral path to success this way: "Man deviseth his own way, but the Lord directeth his steps." (Huber 1971, p. 53) As the number of business journalists grew in America, some dedicated themselves to lionizing business leaders. The Scottish immigrant Bertie Charles (B.C.) Forbes elevated the moral adulation of business leaders into an enduring art form, imitated by business publications throughout the world. When he started Forbes magazine in 1916, Forbes described it as "a publication that would strive to inject more humanity, more joy, and more satisfaction into business and into life in general." (Forbes, October 1947, p. 10) His goal was to convey Franklin's message that work, virtue, and wealth lead to happiness and social benefit.

The 18th and 19th century advocates of the work ethic preached that strong moral character was the key to wealth. By early 20th century the emphasis on moral character shifted to an emphasis on personality. In Dale Carnegie's 1936 classic *How to Win Friends and Influence People*, psychology, not morality, was the key to success in business. This was true in leadership theory as well. Scholars were more interested in studying the personality traits of leaders than their values. This is in part because through most of the 20th century many prominent leadership scholars were psychologists.

The mythologies of business leaders remain popular, even though many of them are not great philanthropists or particularly morally virtuous or advocates of enlightened self-interest. (Economist, 30 May 1998) Today business leaders are more likely to be celebrated in the first person than in the third. Consider, for example, the popularity of autobiographies by Al Dunlap, Donald Trump, and Bill Gates, all of whom enjoy touting their own virtues and values to the public.

Recent books such as *Business as a Calling*, by Michael Novak, draw the traditional Protestant connection between success in business and God's favor. (Novak 1996) Novak, who is a Catholic, argues that successful business people are more religious than other professionals. He cites two studies to back up his view. The first looked at church attendance by elites from the news media, business, politics, labor unions, the military, and religion. It found that groups with the highest proportion of weekly church attendance after religious professionals were the military at 49% and then business at 35%. The second study, of Conference Board survey

of senior executives at Fortune 500 companies, reported that 65% of the respondents said they worshipped at churches or synagogues regularly. (Across the Board 1998, pp. 11-12) Novak infers that church going affects business values. However, we need more evidence than church attendance to connect religious values with the values a leader brings to work. After all, for some going to Church is nothing more than going to Church.

## Leadership Theories and Values

The legacy of the Protestant work ethic and its attitudes toward business present a paradox. Are business leaders successful because of their virtues? or are they virtuous because they are successful? In the literature of leadership studies both seem to be true, depending on how one defines leadership.

Leadership scholars have spent way too much time worrying about the definition of leadership. Some believe that if they could agree on a common definition of leadership, they would be better able to understand it. Joseph Rost gathered together 221 definitions of leadership. After reviewing all of his definitions, one discovers that the definition problem was not really about definitions per se. All 221 definitions say basically the same thing – leadership is about one person getting other people to do something. Where the definitions differ was in how leaders got other followers to act and how leaders came up with the something that was to be done. For example, one definition from the 1920s said, „[Leadership is] the ability to impress the will of the leader on those led and induce obedience, respect, loyalty, and cooperation.” (Moore 1927, p. 124) Another definition from the 1990s said, “Leadership is an influence relationship between leaders and followers who intend real changes that reflect their mutual purposes.” (Rost 1991, p.102) We all can think of leaders who fit both of these descriptions. Some use their power to force people to do what they want, others work with their followers to do what everyone agrees is best for them. The difference between the definitions rests on a normative question: “How should leaders treat followers?”

The scholars who worry about constructing the ultimate definition of leadership are asking the wrong question, but inadvertently trying to answer the right one. The ultimate question about leadership is not “What is the definition of leadership?” The whole point of studying leadership is, “What is good leadership?” The use of word *good* here has two senses, morally good and technically good or effective. If a good leader means *good* in both senses, then the two should form a logical conjunction. In other words, in order for the statement “She is a good leader” to be true, it must be true that she is effective *and* she is ethical.

The question, “What constitutes a good leader?” lies at the heart of many public debates about leadership today. We want our leaders to be good in both ways. Nonetheless, we are often more likely to say leaders are good if they are effective, but not moral, than if they are moral, but not effective. Leaders face a paradox. They have to stay in business or get reelected in order to be leaders. If they are not



minimally effective at doing these things, their morality as leaders is usually irrelevant, because they are no longer leaders. In leadership, effectiveness sometimes must take priority over ethics. What we hope for are leaders who know when ethics should and when ethics shouldn't take a back seat to effectiveness. History tends to dismiss as irrelevant the morally good leaders who are unsuccessful. President Jimmy Carter was a man of great personal integrity, but during his presidency, he was ineffective and generally considered a poor leader. The conflict between ethics and effectiveness and the definition problem are apparent in what I have called, "the Hitler problem." (Ciulla 1995) The answer to the question "Was Hitler a good leader?" is yes, if a leader is defined as someone who is effective or gets the job they set out to do done. The answer is no, if the leader gets the job done, but the job itself is immoral, and it is done in an immoral way. In other words leadership is about more than being effective at getting followers to do things. The quality of leadership also depends on the means and the ends of a leader's actions. The same is true for Robin Hood. While in myth some admire him, he still steals from the rich to give to the poor. His purpose is morally worthy, but the way that he does it is not. Most of us would prefer leaders who do the right thing, the right way for the right reasons.

The way that we assess the impact of a leader's values on an organization also depends on one's theory of leadership. Many still carry with them the "Great Man" theory – leaders are born and not made. Personality traits, not values catapult leaders to greatness. This theory has been articulated in different ways. Thomas Carlyle wrote about the traits of heroes such as Napoleon. Niccolo Machiavelli described the strategic cunning of his "Prince". Friedrich Nietzsche extolled the will to power of his "superman". While the innate qualities of leaders are primary factors in these theories, it is not always clear what makes people want to follow great men. Charismatic leadership is a close relative to the Great Man Theory. Charismatic leaders have powerful personalities. However the distinguishing feature of charismatic leadership is the emotional relationship that charismatic leaders establish with followers. Charismatic leaders range from a John F. Kennedy, who inspired a generation to try and make the world better, to the cult leader Jim Jones, who lead his followers into suicide. The values of charismatic leaders shape the organization, but in some cases these values do not live on when the charismatic leader is gone.

Other theories of leadership focus on the situation or context of leadership. They emphasize the nature of the task that needs to be done, the external environment, which includes historical, economic, and cultural factors, and the characteristics of followers. Lee Iacocca was the right leader for Chrysler when it went bankrupt, but we don't know if he would be the right leader at some other phase of the firm's history. Ross Perot was good businessman, but many doubted his ability to be effective as a political leader. Situational theories don't explicitly say anything about values, but one might surmise that in some situations a person with particularly strong moral values must emerge as a leader. For example, Nelson Mandela and Václav Havel seemed to have been the right men at the right time.

They both offered the powerful kind of moral leadership required for peaceful revolutions in South Africa and the Czech Republic.

A third group of scholars combine trait theories with situational models and focus on the interaction between leaders and followers. The leader's role is to guide the organization along paths that are rewarding to everyone involved. Here values are sure to play an important role, but again it matters what the values are and what they mean to others in the organization. The Ohio studies and the Michigan studies both measured leadership effectiveness in terms of how leaders treated subordinates and how they got the job done. The Ohio Studies looked at leadership effectiveness in terms of "consideration" or the degree to which leaders act in friendly and supportive manner, and "initiating structure" or the way that leaders structure their own role and the role of subordinates in order to obtain group goals. (Fleishman 1953) The Michigan Studies measured leaders on the basis of task orientation and relationship orientation<sup>2</sup> Implicit in these theories and studies is an ethical question. Are leaders more effective when they are kind to people, or are leaders more effective when they use certain techniques for structuring and ordering tasks? Is leadership about moral relationships or techniques? – the answer is both about both. (Yukl 1989, p. 96)

Transforming Leadership and Servant Leadership are normative theories of leadership. Both emphasize the relationship of leaders and followers to each other and the importance values in the process of leadership. James MacGregor Burns' theory of transforming leadership rests on a set of moral assumptions about the relationship between leaders and followers.<sup>3</sup> Servant leadership has not gotten as much attention as transformational leadership in the literature, but in recent years interest in it by the business community has grown. Servant leaders lead because they want to serve others. (Greenleaf 1977, p. 23) In both transforming leadership and servant leadership, leaders not only have values, but they help followers develop their own values, which will hopefully overlap or be compatible with those of the organization.

## The Problem Only Having Values

Social scientists like to talk about values because they are descriptors. When a poll asks voters if they prefer better schools or lower taxes, we assume that if the majority pick better schools, it means most respondents value education. Ask people about their values and they will tell you what they think is important. Different types of moral statements and concepts *do* different things. For example the

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<sup>2</sup> Results from the earlier and later Michigan Studies are discussed in: Leikert, R.: *New Patterns of Management*. New York 1961 and *The Human Organization: Its Management and Value*. New York 1967.

<sup>3</sup> Burns uses the terms transforming and transformational in his book. However, he prefers to refer to his theory as transforming leadership.

statement “you ought not to kill” prescribes, “Do not kill” commands, “Killing is wrong” evaluates, and “Killing is wrong because I value life” explains, and “Killing is against my values, which include the value of human life” describes. Values are static concepts. You have to make a lot of assumptions to make a value do something. You have to assume that because people value something they act accordingly, but we know this isn’t the case. While values change all the time, having a value does not mean that one has or will do something about it.

Since values themselves do not have agency, the main way that a leader influences the organization is through his or her words and actions. One way to understand a leader’s values is through their vision. The CEO who says his or her vision is to double market share by the year 2000 has a goal, not a vision. All businesses want to make profits. Visions must have an implicit or explicit moral component to them. (Nanus 1992) Often the moral component has to do with improving the quality of life, particularly in the case of making a product safer, environmentally friendly, or more affordable to those who need it. A leader’s vision should tell us where we want to go, why it’s good to go there, and the right way for us to get there.

The only way to understand if a business leader’s values have an impact is to look at how his or her values connect with actions. Hypocrisy is the most extreme form of values not meeting up with actions. Hypocrites express strong moral values that they do not hold and then act against them. For example, a company that advertises its commitment to green products while continuing to sell products that don’t meet its own espoused green standards is hypocritical. (Bird 1996, p. 4) What is most odd about some hypocrites is that they are not always complete liars. Some know they should live up to the values they talk about, but simply do not or will not.

Another problem with values and actions is what Frederick B. Bird calls “moral silence”. Moral silence is the opposite of hypocrisy. Morally silent leaders act and speak as if they do not hold certain moral values, when they actually do. The company president who cuts 1000 jobs from the payroll may publicly state that he cut jobs to fill what he considers his most important obligation to protect shareholder value. When in fact he is guilt ridden because he really believes that his greatest moral obligation is to his employees. Leaders sometimes lack the ability or the moral courage to act on their values. Similarly, there are some who have values, but are either too busy, distracted, or lazy to act on those values. Consider the case of a female corporate executive who has strong convictions about giving women opportunities for career advancement, but does not go out of her way or take advantage of opportunities to ensure that women in her company have these opportunities.

Often leaders don’t realize that the values they hold are in practice contradictory or inconsistent. Once a colleague and I conducted an ethics seminar for the presidents of a large conglomerate. The CEO of the corporation was an enthusiastic participant. During the seminar he expressed his feelings about the importance of honesty and integrity in business. However, as the participants discussed our case studies, it became clear that there were a number of situations in which pro-

protecting the company's integrity meant losing business or money. The CEO actively agreed with these conclusions. However, the others in the seminar pointed out to him that quarterly sales determined the compensation for each business unit. The CEO set profit targets for each business unit and used a formula to determine compensation. When it came to performance, he valued the numbers more than anything else. What the CEO failed to realize was that he was espousing the value of integrity, but in effect saying that employees would be punished if they did not act with integrity (with firing) and punished if they did act with integrity (with reduced compensation). Some thought that if the CEO really valued integrity, he should make some adjustment to the incentive system to take into account business lost for ethical reasons. One brave man wondered out loud if the CEO didn't really value profits over integrity.

Often companies write codes of ethics or mission statements but don't think through what the values in the statement mean in terms of how they manage their businesses. In 1983 the Harvard Business School wrote a glowing case study of how CEO Jim Beré developed the Borg-Warner code of ethics. (Goodpaster 1983) Borg-Warner is a conglomerate of automotive, financial services, and security service businesses. Its code began with the statement, "We believe in the dignity of the individual", and "We believe in the commonwealth of Borg Warner and its people." An elegant framed copy of the code was hung offices and factories of Borg-Warner's various businesses. Their ethics code also said, "we must heed the voice of our natural concern for others" and "grant others the same respect, cooperation, and decency we seek for ourselves." (Murphy 1998, p. 27)

Warner Gear, a division of Borg Warner, manufactured gears for cars and boats. In 1984 it made a text book turn around in labor relations and productivity. After years of losing money and engaging in endless labor disputes, the union and management finally agreed to cooperate. They formed effective quality circles that saved the company millions of dollars in waste and inefficiency. Company profits soared in 1985. (Ciulla/Goodpaster 1985, p. 11) However, in July of that year, with no warning to the managers or employees who implemented the turnaround, Borg Warner announced it was shipping part of Warner Gear to Kenfig, Wales to save on labor costs. This meant that the factory would lose 300 jobs. While the business decision may have been warranted, the way that it was implemented did not show decency and respect for those who had worked so hard to make the firm successful. All the energy, good will, and commitment of the employees didn't matter, and neither did the grand values that hung on the wall.

Lastly, there are cases where a business leader acts on values that he has never made any concerted effort to express in words to employees. In 1995, a textile factory in Massachusetts named Malden Mills, burnt down. The next day, the owner, Aaron Feuerstein, announced that he would give out Christmas bonuses and pay his employees full salaries until the factory was repaired. In the midst of massive corporate downsizings of that time this story of kindness captured the public imagination. Feuerstein was a quiet man running a family business. The business itself was known for treating workers fairly, but Feuerstein

had never been one to publicly articulate his own values. Given the publicity of his actions after the fire, he was asked by the press to talk about his values. He then explained that his business values came from his Jewish faith and the teachings of the Talmud. Yet for most employees, where he got his values didn't matter as much as what he did with them.

The point of these examples is to show that a leader's values do indeed shape the values of the firm when they are paired with policies and actions that breath life into them. The way in which founders influence the values of the company is by setting out their mission, what they want to do, and how they want to do it. But most importantly, their actions write the story of the organization's values. The story can be a morally good one or an evil one. Either way, the role of leaders who come after the founder is to tell and add to the story of the company and its values. This includes ethical lessons learned from its mistakes as well as its moral triumphs.

Howard Garner believes that great leaders are also great story-tellers. He says "leadership is a process in the minds of individuals who live in a culture. Some stories tend to become more predominant in this process, such as stories that provide an adequate and timely sense of identity for individuals."(Gardner 1995, p. 22) The story of the fire at Malden Mills will become part of the company's mythology. It not only conveys a message of moral commitment to employees, but it sets a moral standard for those who will take Feuerstein's place.

Leaders' values matter when they are repeatedly reflected in their actions. However, a leader's values and his or her will to act on them are also shaped by the history and the culture of the organization itself. As I pointed out earlier, we sometimes mythologize business leaders because they are successful or imagine that their lone values are responsible for doing some heroic action. However, as we saw earlier, there can be a gap between having values and acting on them. This gap is often narrowed or widened by the values already present in the story of the organization.

One of the more dramatic illustrations of business leadership and values is the case of P. Roy Vagelos, CEO of Merck & Co., Inc.(Useem 1998, Chapter 1). Prior to becoming CEO, Vagelos was director of Merck Sharp & Dohme's research laboratories. In 1979 a researcher named William Campbell had a hunch that an antiparasite drug he was working on called Ivermectin might work on the parasite that caused river blindness, a disease that threatens the eyesight and lives of 85 million people in 35 developing countries. He asked Vagelos if he could have the resources to pursue his research. Despite the fact that the market for this drug was essentially the poorest people in the world, Vagelos gave Campbell the go ahead. While the decision was Vagelos', it was also reinforced by the Merck's axiom "health precedes wealth".

Campbell's hunch about Ivermectin proved to be right and he developed a drug called "Mectizan", which was approved for use by the government in 1987. By this time Vagelos had become the CEO of Merck. Now that the drug was approved he sought public underwriting to produce Mectizan. Vagelos hired Henry

Kissenger to help open doors for Merck. They approached several sources including the U.S. Agency for International Development and the World Health Organization, but couldn't raise money for the drug. Merck was left with a drug that was only useful to people who couldn't buy it. Vagelos recalled, "We faced the possibility that we had a miraculous drug that would sit on a shelf." (Useem 1998, p. 23) After reviewing the company's options, Vagelos and his directors announced that they would give Mectizan away for free, forever, on October 21, 1987. A decade later the drug give-away cost Merck over \$200 million. By 1996 Mectizan had reached 19 million people. In Nigeria alone it saved 6 million people from blindness.

Few business leaders ever have the opportunity to do what Vagelos did. His values guided his decisions in this case, but so did the values of the founder. George C. Merck, son of the company's American founder said that from the very beginning Merck's founders asserted that medicine was for people not profits. However, he quickly added that they also believed that if their medicine is good for people, profits will follow. (Useem 1998, p. 29)

Like many corporate mission statements Merck's says its mission "is to provide society with superior products and services". The statement goes on to assert, "we are in the business of preserving and improving human life". "All of our actions must be measured by our success at achieving this goal." It concludes with, "we expect profits from work that satisfies customer needs and that benefits humanity." (Useem 1998, p. 29) The values in Merck's mission statement are as grand as the ones in Borg Warner's. However, the corporate leaders prior to Vagelos acted on and hence reinforced these values long before Vagelos donated Mectizan. After W.W.II tuberculosis thrived in Japan. Most Japanese couldn't afford to buy Merck's powerful drug, Streptomycin, to fight it. Merck gave away a large supply of the drug to the Japanese public. The Japanese did not forget. In 1983 the Japanese government allowed Merck to purchase 50.02 percent of Banyu Pharmaceutical. At the time this was the largest foreign investment in a Japanese company. Merck is currently the largest American pharmaceutical company in Japan. The story makes Merck's mission statement come alive. It is the kind of story that employees learn and internalize when they come to work there.

In this case, Vagelos' moral leadership extended beyond his organization into the industry. As Michael Useem points out, at that time, Merck was the benchmark by which the moral behavior of other pharmaceutical companies were judged. Sometimes the moral actions of one CEO or company set the bar higher for others. Useem observes that the message hit home at Glaxo. In comparing Glaxo to Merck, a business writer once called Glaxo "a hollow enterprise lacking purpose and lacking soul" (Useem 1998, p. 31). Merck's values seemed to inspire Glaxo's new CEO Richard Sykes. In 1993 Glaxo invested in developing a drug to combat a form of tuberculosis connected to aids and found mostly among the poor. In 1996 Glaxo donated a potent new product for malaria. Similarly, Dupont is now giving away nylon to filter guinea worms out of drinking water in poor countries and American Cyanamid is donating a larvacide to control them.

A cynic might regard Merck's donation of Streptomycin and Mectizan as nothing more than public relations stunts. But what is most interesting about the actions of Merck's leaders is that while they believed that 'by doing good they would do well', at the time that they acted it was unclear exactly when and how the company would benefit. Neither the Japanese after the war nor the poor people of the world who are threatened by river blindness looked likely to return the favor in the near future. While this wasn't an altruistic act, it was not a purely self-interested one either. Since it was unclear if, when, and how Merck would benefit, it is reasonable to assume that Merck's leaders and the values upon which they acted were authentic. They intentionally acted on their values. Any future benefits required a leap of faith on their part.

Business leaders' values matter to the organization only if they act on them. In business ethics and in life we always hope that doing the right thing, while costly and sometimes painful in the short run, will pay off in the long run.

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# The Servant as Leader<sup>1</sup>

Robert Greenleaf

Servant and leader – can these two roles be fused in one real person, in all levels of status or calling? If so, can that person live and be productive in the real world of the present? My sense of the present leads me to say yes to both questions. This chapter is an attempt to explain why and to suggest how.

The idea of *The Servant as Leader* came out of reading Hermann Hesse's *Journey to the East*. In this story we see a band of men on a mythical journey, probably also Hesse's own journey. The central figure of the story is Leo who accompanies the party as the *servant* who does their menial chores, but who also sustains them with his spirit and his song. He is a person of extraordinary presence. All goes well until Leo disappears. Then the group falls into disarray and the journey is abandoned. They cannot make it without the servant Leo. The narrator, one of the party, after some years of wandering finds Leo and is taken into the Order that had sponsored the journey. There he discovers that Leo, whom he had known first as *servant*, was in fact the titular head of the Order, its guiding spirit, a great and noble *leader*.

One can muse on what Hesse was trying to say when he wrote this story. We know that most of his fiction was autobiographical, that he led a tortured life, and that *Journey to the East* suggests a turn toward the serenity he achieved in his old age. There has been much speculation by critics on Hesse's life and work, some of it centering on this story which they find the most puzzling. But to me, this story clearly says that *the great leader is seen as servant first*, and that simple fact is the key to his greatness. Leo was actually the leader all of the time, but he was servant first because that was what he was, *deep down inside*. Leadership was bestowed upon a man who was by nature a servant. It was something given, or assumed, that could be taken away. His servant nature was the real man, not bestowed, not assumed, and not to be taken away. He was servant first.

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I mention Hesse and *Journey to the East* for two reasons. First, I want to acknowledge the source of the idea of *The Servant as Leader*. Then I want to use this reference as an introduction to a brief discussion of prophecy.

Fifteen years ago when I first read about Leo, if I had been listening to contemporary prophecy as intently as I do now, the first draft of this piece might have been written then. As it was, the idea lay dormant for eleven years until, four years ago, I concluded that we in this country were in a leadership crisis and that I should do what I could about it. I became painfully aware of how dull my sense of contemporary prophecy had been. And I have reflected much on why we do not hear and heed the prophetic voices in our midst (not a new question in our times, nor more critical than heretofore).

I now embrace the theory of prophecy which holds that prophetic voices of great clarity, and with a quality of insight equal to that of any age, are speaking cogently all of the time. Men and women of a stature equal to the greatest of the past are with us now addressing the problems of the day and pointing to a better way and to a personage better able to live fully and serenely in these times.

The variable that marks some periods as barren and some as rich in prophetic vision is in the interest, the level of seeking, the responsiveness of the hearers. The variable is not in the presence or absence or the relative quality and force of the prophetic voices. Prophets grow in stature as people respond to their message. If their early attempts are ignored or spurned, their talent may wither away.

It is *seekers*, then, who make prophets, and the initiative of any one of us in searching for and responding to the voice of contemporary prophets may mark the turning point in their growth and service. But since we are the product of our own history, we see current prophecy within the context of past wisdom. We listen to as wide a range of contemporary thought as we can attend to. Then we *choose* those we elect to heed as prophets – *both old and new* – and meld their advice with our own leadings. This we test in real-life experiences to establish our own position.

Some who have difficulty with this theory assert that their faith rest on one or more of the prophets of old having giving the “word” for all time and that the contemporary ones do not speak to their condition as the older ones do. But if one really believes that the “word” has been given for all time, how can one be a seeker? How can one hear the contemporary voice when one has decided not to live in the present and has turned that voice off?

Neither this hypothesis nor its opposite can be proved. But I submit that the one given here is the more hopeful choice, one that offers a significant role in prophecy to every individual. One cannot interact with and build strength in a dead prophet, but one can do it with a living one. “Faith”, Dean Inge has said, “is the choice of the nobler hypothesis.”

One does not, of course, ignore the great voices of the past. One does not awaken each morning with the compulsion to reinvent the wheel. But if one is *servant*, either leader or follower, one is always searching, listening, expecting

that a better wheel for these times is in the making. It may emerge any day. Any one of us may find it out from personal experience. I am hopeful.

I am hopeful for these times, despite the tension and conflict, because more natural servants are trying to see clearly the world as it is and are listening carefully to prophetic voices that are speaking *now*. They are challenging the pervasive injustice with greater force and they are taking sharper issue with the wide disparity between the quality of society they know is reasonable and possible with available resources, and, on the other hand, the actual performance of the whole range of institutions that exist to serve society.

A fresh critical look is being taken at the issues of power and authority, and people are beginning to learn, however haltingly, to relate to one another in less coercive and more creatively supporting ways. A new moral principle is emerging which holds that the only authority deserving one's allegiance is that which is freely and knowingly granted by the led to the leader in response to, and in proportion to, the clearly evident servant stature of the leader. Those who choose to follow this principle will not casually accept the authority of existing institutions. *Rather, they will freely respond only to individuals who are chosen as leaders because they are proven and trusted as servants.* To the extent that this principle prevails in the future, the only truly viable institutions will be those that are predominantly servant-led.

I am mindful of the long road ahead before these trends, which I see so clearly, become a major society-shaping force. We are not there yet. But I see encouraging movement on the horizon.

What direction will the movement take? Much depends on whether those who stir the ferment will come to grips with the age-old problem of how to live in a human society. I say this because so many, having made their awesome decision for autonomy and independence from tradition, and having taken their firm stand against injustice and hypocrisy, find it hard to convert themselves into *affirmative builders* of a better society. How many of them will seek their personal fulfillment by making the hard choices, and by undertaking the rigorous preparation that building a better society requires? It all depends on what kind of leaders emerge and how they – we – respond to them.

My thesis, that more servants should emerge as leaders, or should follow only servantleaders, is not a popular one. It is much more comfortable to go with a less demanding point of view about what is expected of one now. There are several undemanding, plausibly argued alternatives to choose. One, since society seems corrupt, is to seek to avoid the center of it by retreating to an idyllic existence that minimizes involvement with the “system” (with the “system” that makes such withdrawal possible). Then there is the assumption that since the effort to reform existing institutions has not brought instant perfection, the remedy is to destroy them completely so that fresh new perfect ones can grow. Not much thought seems to be given to the problem of where the new seed will come from or who the gardener to tend them will be. The concept of the servant-leader stands in sharp contrast to this kind of thinking.

Yet it is understandable that the easier alternatives would be chosen, especially by young people. By extending education for so many so far into the adult normal participation in society is effectively denied when young people are ready for it. With education that is preponderantly abstract and analytical it is no wonder that there is a preoccupation with criticism and that not much thought is given to “What can *I* do about it?”

Criticism has its place, but as a total preoccupation it is sterile. In a time of crisis, like the leadership crisis we are now in, if too many potential builders are taken in by a complete absorption with dissecting the wrong and by a zeal for instant perfection, then the movement so many of us want to see will be set back. The danger, perhaps, is to hear the analyst too much and the artist too little.

Albert Camus stands apart from other great artists of his time, in my view, and deserves the title of *prophet*, because of his unrelenting demand that each of us confront the exacting terms of our own existence, and, like Sisyphus, *accept our rock and find our happiness in dealing with it*. Camus sums up the relevance, of his position to our concern for the servant as leader in the last paragraph of his last published lecture, entitled *Create Dangerously*:

One may long, as I do, for a gentler flame, a respite, a pause for musing. But perhaps there is no other peace for the artist than what he finds in the heat of combat. “Every wall is a door”, Emerson correctly said. Let us not look for the door, and the way out, anywhere but in the wall against which we are living. Instead, let us seek the respite where it is – in the very thick of battle. For in my opinion, and this is where I shall close, it is there. Great ideas, it has been said, come into the world as gently as doves. Perhaps, then, if we listen attentively, we shall hear, amid the uproar of empires and nations, a faint flutter of wings, the gentle stirring of life and hope. Some will say that this hope lies in a nation, others, in a man. One believe rather that it is awakened, revived, nourished by millions of solitary individuals whose deeds and works every day negate frontiers and the crudest implications of history. As a result, there shines forth fleetingly the ever-threatened truth that each and every man, on the foundations of his own sufferings and joys, builds for them all.

One is asked, then, to accept the human condition, its sufferings and its joys, and to work with its imperfections as the foundation upon which the individual will build wholeness through adventurous creative achievement. For the person with creative potential there is no wholeness except in using it. And, as Camus explained, the going is rough and the respite is brief. It is significant that he would title his last university lecture *Create Dangerously*. And, as I ponder the fusing of servant and leader, it seems a dangerous creation: dangerous for the natural servant to become a leader, dangerous for the leader to be servant first, and danger-

ous for a follower to insist on being led by a servant. There are safer and easier alternatives available to all three. But why take them?

As I respond to the challenge of dealing with this question in the ensuing discourse I am faced with two problems.

First, I did not get the notion of the servant as leader from conscious logic. Rather it came to me as an intuitive insight as I contemplated Leo. And I do not see what is relevant from my own searching and experience in terms of a logical progression from premise to conclusion. Rather I see it as fragments of data to be fed into my internal computer from which intuitive insights come. Serving and leading are still mostly intuition-based concepts in my thinking.

The second problem, and related to the first, is that, just as there may be a real contradiction in the servant as leader, so my perceptual world is full of contradictions. Some examples: I believe in order, and I want creation out of chaos. My good society will have strong individualism amidst community. It will have elitism along with populism. I listen to the old and to the young and find myself baffled and heartened by both. Reason and intuition, each in its own way, both comfort and dismay me. There are many more. Yet, with all of this, I believe that I live with as much serenity as do my contemporaries who ventures into controversy as freely as I do but whose natural bent is to tie up the essentials of life in neat bundles of logic and consistency. But I am deeply grateful to the people who are logical and consistent because some of them, out of their natures, render invaluable services for which I am not capable.

My resolution of these two problems is to offer the relevant gleanings of my experience in the form of a series of unconnected little essays, some developed more fully than others, with the suggestion that they be read and pondered on separately within the context of this opening section.

## Who Is the Servant-Leader?

The servant-leader is servant first – as Leo was portrayed. It begins with the natural feeling that one wants to serve, to serve *first*. Then conscious choice brings one to aspire to lead. That person is sharply different from one who is *leader* first, perhaps because of the need to assuage an unusual power drive or to acquire material possessions. For such it will be a later choice to serve – after leadership is established. The leader-first and the servant-first are two extreme types. Between them there are shadings and blends that are part of the infinite variety of human nature.

The difference manifests itself in the care taken by the servant-first to make sure that other people's highest priority needs are being served. The best test, and difficult to administer, is: Do those served grow as persons? Do they, *while being served*, become healthier, wiser, freer, more autonomous, more likely themselves to become servants? *and*, what is the effect on the least privileged in society; will they benefit, or, at least, not be further deprived?

As one sets out to serve, how can one know that this will be the result? This is part of the human dilemma; one cannot know for sure. One must, after some study and experience, hypothesize – but leave the hypothesis under a shadow of doubt. Then one acts on the hypothesis and examines the result. One continues to study and learn and periodically one re-examines the hypothesis itself.

Finally, one chooses again. Perhaps one chooses the same hypothesis again and again. But it is always a fresh open choice. And it is always a hypothesis under a shadow of doubt. “Faith is the choice of the nobler hypothesis.” Not the *noblest*; one never knows what that is. But the *nobler*, the best one can see when the choice is made. Since the test of results of one’s actions is usually long delayed, the faith that sustains the choice of the nobler hypothesis is psychological self-insight. This is the most dependable part of the true servant.

The natural servant, the person who is *servant* first, is more likely to persevere and refine a particular hypothesis on what serves another’s highest priority needs than is the person who is *leader* first and who later serves out of promptings of conscience or in conformity with normative expectations.

My hope for the future rests in part on my belief that among the legions of deprived and unsophisticated people are many true servants who will lead, and that most of them can learn to discriminate among those who presume to serve them and identify the true servants whom they will follow.

## Everything Begins with the Initiative of an Individual

The forces for good and evil in the world are propelled by the thoughts, attitudes, and actions of individual beings. What happens to our values, and therefore to the quality of our civilization in the future, will be shaped by the conceptions of individuals that are born of inspiration. Perhaps only a few will receive this inspiration (insight) and the rest will learn from them. The very essence of leadership, going out ahead to show the way, derives from more than usual openness to inspiration. Why would anybody accept the leadership of another except that the other sees more clearly where it is best to go? Perhaps this is the current problem: too many who presume to lead do not see more clearly and, in defense of their inadequacy, they all the more strongly argue that the “system” must be preserved – a fatal error in this day of candor.

But the leader needs more than inspiration. A leader ventures to say: “I will go; come with me!” A leader initiates, provides the ideas and the structure, and takes the risk of failure along with the chance of success. A leader says: “I will go; follow me!” while knowing that the path is uncertain, even dangerous. One then trusts those who go with one’s leadership.

Paul Goodman, speaking through a character in *Making Do*, has said, “If there is no community for you, young man, young man, make it yourself.”

## What Are You Trying to Do?

“What are you trying to do?” is one of the easiest to ask and most difficult to answer of questions. A mark of leaders, an attribute that puts them in a position to show the way for others, is that they are better than most at pointing the direction. As long as one is leading, one always has a goal. It may be a goal arrived at by group consensus, or the leader, acting on inspiration, may simply have said, “Let’s go this way.” But the leader always knows what it is and can articulate it for any who are unsure. By clearly stating and restating the goal the leader gives certainty and purpose to others who may have difficulty in achieving it for themselves.

The word *goal* is used here in the special sense of the overarching purpose, the big dream, the visionary concept, the ultimate consummation which one approaches but never really achieves. It is something presently out of reach; it is something to strive for, to move toward, or become. It is so stated that it excites the imagination and challenges people to work for something they do not yet know how to do, something they can be proud of as they move toward it.

Every achievement starts with a goal – but not just any goal and not just anybody stating it. The one who states the goal must elicit trust, especially if it is a high risk or visionary goal, because those who follow are asked to accept the risk along with the leader. Leaders do not elicit trust unless one has confidence in their values and competence (including judgment) and unless they have a sustaining spirit (enthusiasm) that will support the tenacious pursuit of a goal.

Not much happens without a dream. And for something great to happen, there must be a great dream. Behind every great achievement is a dreamer of great dreams. Much more than a dreamer is required to bring it to reality; but the dream must be there first.

# The Structure of Moral Leadership<sup>1</sup>

*James MacGregor Burns*

Leadership is a process of morality to the degree that leaders engage with followers on the basis of shared motives and values and goals – on the basis, that is, of the followers’ “true” needs as well as those of leaders: psychological, economic, safety, spiritual, sexual, aesthetic, or physical. Friends, relatives, teachers, officials, politicians, ministers, and others will supply a variety of initiatives, but only the followers themselves can ultimately define their own true needs. And they can do so only when they have been exposed to the competing diagnoses, claims, and values of would-be leaders, only when the followers can make an informed choice among competing “prescriptions”, only when – in the political arena at least – followers have had full opportunity to perceive, comprehend, evaluate, and finally experience alternatives offered by those professing to be their “true” representatives. Ultimately the moral legitimacy of transformational leadership, and to a lesser degree transactional leadership, is grounded in *conscious choice among real alternatives*. Hence leadership assumes competition and conflict, and brute power denies it.

Conflict has become the stepchild of political thought. Philosophical concern with conflict reaches back to Hobbes and even Heraclitus, and men who spurred revolutions in Western thought – Machiavelli and Hegel, Marx and Freud – recognized the vital role of conflict in the relations among persons or in the ambivalences within them. The seventeenth-century foes of absolute monarchy, the eighteenth-century Scottish moralists, the nineteenth-century Social Darwinists –these and other schools of thought dealt directly with questions of power and conflict, and indirectly at least with the nature of leadership. The theories of Pareto, Durkheim, Weber, and others, while not centrally concerned with problems of social conflict, “contain many concepts, assumptions, and hypotheses which greatly influenced later writers who did attempt to deal with conflict in general”. Georg Simmel and others carried theories of conflict into the twentieth century.

It was, curiously, in this same century – an epoch of the bloodiest world wars, mightiest revolutions, and most savage civil wars – that social science, at least in the West, became *most entranced with doctrines of harmony, adjustment, and sta-*

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<sup>1</sup> Published in: *Leadership* by James MacGregor Burns, pp. 36-43. Reprinted by permission of HarperCollins Publishers Inc.



*bility*. Perhaps this was the result of relative affluence, or of the need to unify people to conduct total war or consolidate revolutions, or of the co-option of scholars to advise on mitigating hostility among interest groups such as labor and management or racial groups such as blacks and whites. Whatever the cause, the “static bias” afflicted scholarly research with a tendency to look on conflict as an aberration, if not a perversion, of the agreeable and harmonious interactions that were seen as actually making up organized society. More recently Western scholarship has shown a quickened interest in the role of conflict in establishing boundaries, channeling hostility, counteracting social ossification, invigorating class and group interests, encouraging innovation, and defining and empowering leadership.

The static bias among scholars doubtless encouraged and reflected the pronouncements of political authority. Communist leaders apotheosized conflict as the engine of the process of overthrowing bourgeois regimes and then banned both the profession and the utilization of conflict in the new “classless” societies. Western leaders, especially in the United States, make a virtual fetish of “national unity”, “party harmony”, and foreign policy bipartisanship even while they indulge in – and virtually live off – contested elections and divisive policy issues. Jefferson proclaimed at his first Inaugural, “We are all Federalists, we are all Republicans.” Few American presidents have aroused and inflamed popular attitudes as divisively as Franklin D. Roosevelt with his assaults on conservatives in both parties, his New Deal innovations, and his efforts to pack the Supreme Court and purge the Democratic party, yet few American presidents have devoted so many addresses to sermonlike calls for transcending differences and behaving as one nation and one people. The potential for conflict permeates the relations of humankind, and that potential is a force for health and growth as well as for destruction and barbarism. No group can be wholly harmonious, as Simmel said, for such a group would be empty of process and structure. The smooth interaction of people is continually threatened by disparate rates of change, technological innovation, mass deprivation, competition for scarce resources, and other ineluctable social forces and by ambivalences, tensions, and conflicts within individuals’ personalities. One can imagine a society – in ancient Egypt, perhaps, or in an isolated rural area today – in which the division of labor, the barriers against external influence, the structure of the family, the organization of the value system, the acceptance of authority, and the decision-making by leaders all interact smoothly and amiably with one another. But the vision of such a society would be useful only as an imaginary construct at one end of a continuum from cohesion to conflict. Indeed, the closer, the more intimate the relations within a group, the more hostility as well as harmony may be generated. The smaller the cooperative group – even if united by language and thrown closely together by living arrangements – “the easier it is for them to be mutually irritated and to flare up in anger”, Bronislaw Malinowski said. Some conflict over valued goals and objects is almost inevitable. Even small, isolated societies cannot indefinitely dike off the impact of internal changes such as alteration of the birth rate or the disruption caused by various forms of innovation.

The question, then, is not the inevitability of conflict but the function of leadership in expressing, shaping, and curbing it. Leadership as conceptualized here is grounded in the seedbed of conflict. Conflict is intrinsically compelling: it galvanizes, prods, motivates people. Every person, group, and society has latent tension and hostility, forming a variety of psychological and political patterns across social situations. Leadership acts as an inciting and triggering force in the conversion of conflicting demands, values, and goals into significant behavior. Since leaders have an interest of their own, whether opportunistic or ideological or both, in expressing and exploiting followers' wants, needs, and aspirations, they act as catalytic agents in arousing followers' consciousness. They discern signs of dissatisfaction, deprivation, and strain; they take the initiative in making connections with their followers; they plumb the character and intensity of their potential for mobilization; they articulate grievances and wants; and they act for followers in their dealings with other clusters of followers.

Conflicts vary in origin – in and between nations, races, regions, religions, economic enterprises, labor unions, communities, kinship groups, families, and individuals themselves. Conflicts show various degrees and qualities of persistence, direction, intensity, volatility, latency, scope. The last alone may be pivotal; the outcome of every conflict, E.E. Schattschneider wrote, “is determined by the *scope* of its contagion. The number of people involved in any conflict determines what happens; every change in the number of participants...affects the results...The moral of this is: If a fight starts, watch the crowd, because the crowd plays the decisive role.” But it is leadership that draws the crowd into the incident, that changes the number of participants, that closely affects the manner of the spread of the conflict, that constitutes the main “processes” of relating the wider public to the conflict.

The root causes of conflict are as varied as their origins. No one has described these causes as cogently as James Madison:

The latent causes of faction are thus sown in the nature of man; and we see them every where brought into different degrees of activity, according to the different circumstances of civil society. A zeal for different opinions concerning religion, concerning government and many other points, as well of speculation as of practice; an attachment to different leaders ambitiously contending for pre-eminence and power; or to persons of other descriptions whose fortunes have been interesting to the human passions, have in turn divided mankind into parties, inflamed them with mutual animosity, and rendered them much more disposed to vex and oppress each other, than to co-operate for their common good. So strong is this propensity of mankind to fall into mutual animosities, that where no substantial occasion presents itself, the most frivolous and fanciful distinctions have been sufficient to kindle their unfriendly passions, and excite their most violent conflicts. But the most common and durable source of factions, has been the various and unequal distribution of property.

Not only “attachment to different leaders” but all these forces for conflict are expressed and channeled through many different types of leaders “ambitiously contending for pre-eminence and power.”

Leaders, whatever their professions of harmony, do not shun conflict; they confront it, exploit it, ultimately embody it. Standing at the points of contact among latent conflict groups, they can take various roles, sometimes acting directly for their followers, sometimes bargaining with others, sometimes overriding certain motives of followers and summoning others into play. The smaller and more homogeneous the group for which they act, the more probable that they will have to deal with the leaders of other groups with opposing needs and values. The larger, more heterogeneous their collection of followers, the more probable that they will have to embrace competing interests and goals within their constituency. At the same time, their marginality supplies them with a double leverage, since in their status as leaders they are expected by their followers and by other leaders to deviate, to innovate, and to mediate between the claims of their groups and those of others.

But leaders shape as well as express and mediate conflict. They do this largely by influencing the intensity and scope of conflict. Within limits they can soften or sharpen the claims and demands of their followers, as they calculate their own political resources in dealing with competing leaders within their own constituencies and outside. They can amplify the voice and pressure of their followers, to the benefit of their bargaining power perhaps, but at the possible price of freedom to maneuver – less freedom to protect themselves against their followers – as they play in games of broader stakes. Similarly, they can narrow or broaden the scope of conflict as they seek to limit or multiply the number of entrants into a specific political arena.

Franklin Roosevelt demonstrated the fine art of controlling entry in the presidential nomination race in 1940. There was widespread uncertainty as to whether he would run for a third term. He himself was following the development of public opinion at the same time that he was influencing it. Leaders in his own party were divided; onetime stalwarts like James A. Farley and Cordell Hull opposed a third term. It was supposed that FDR would discourage Democrats from entering the nomination race. On the contrary, he welcomed them. Secondary figures like Joseph Kennedy, coming to the Oval Office to sound out Roosevelt on his intentions and on their own chances, found themselves flattered and rated as serious and deserving possibilities. The effect was to broaden the field of possible adversaries and hence divide and weaken the opposition. FDR had little trouble winning the nomination.

The essential strategy of leadership in mobilizing power is to recognize the arrays of motives and goals in potential followers, to appeal to those motives by words and action, and to strengthen those motives and goals in order to increase the power of leadership, thereby changing the environment within which both followers and leaders act. Conflict – disagreement over goals within an array of followers, fear of outsiders, competition for scarce resources – immensely invigo-

rates the mobilization of consensus and dissensus. But the fundamental process is a more elusive one; it is, in large part, *to make conscious what lies unconscious among followers*.

The purposeful awakening of persons into a state of political consciousness is a familiar problem for philosophers and psychologists and one that has stimulated thought in other disciplines. For the student of leadership the concept of political consciousness is as primitive as it is fertile. That “conflict produces consciousness” was fundamental in the doctrine of Hegel, Marx, and other nineteenth-century theorists, but they differed over the cardinal question: consciousness of *what*? They recognized the essential human needs but differed as to the nature of those needs. Feuerbach, an intellectual leader of the young Marx, conceived humanity as imbued with real, tangible, solid needs arising from Nature. Marx compared human consciousness with that of animals, which had no consciousness of the world as something objective and real apart from the animal’s own existence and needs. But *human* labor, rather than leading to direct satisfaction of need, generates human consciousness and self-consciousness. Thus the early Marx had some understanding of the variety and inexhaustibility of human needs.

It was a marvelous insight, but Marx came to be identified with the doctrine that *true* consciousness, to be achieved through unremitting conflict, was always of *class*. Felt, palpable human needs, however, did not seem to be translated into a rising class consciousness in the capitalist environment of the mid-nineteenth century. Marx and Engels railed at the “false consciousness” of religion and nationalism and the other diversions and superficialities that seemed to engage men who were caught in the iron grip of material deprivation. The progress toward class consciousness was slow, irregular, uneven. The almost automatic movement toward revolution, emerging out of the “spontaneous classorganization of the proletariat”, simply did not come about in the great bourgeois societies; ultimately revolution would need to be spurred by militant leadership and iron party discipline.

In the fiery intellectual and political conflict of the nineteenth century both Marxists and their adversaries assumed too much about the central springs of human behavior without knowing enough about motivation or the complex relations between motives and behavior. Few perceived that if people did not behave the way they were supposed to, the fault might lie in the suppositions rather than in the people. One of the suppositions was that ultimately humans would respond rationally and “realistically” to “objective” social conditions. But what was real and rational? If Marx had turned Hegel’s dialectic of ideas on its head, Freud turned Marx’s Consciousness upside down. Freud was drawn to the function of the unconscious rather than the conscious or the preconscious; for him the unconscious was the “true psychic reality”, betrayed by dreams, fantasies, accidents, and curious slips of the tongue. Consciousness and related concepts of alienation and identity have continued to be variously defined and heatedly debated. During the ferment of the 1960s that reached across the Western world, young people were

urged to “expand consciousness” and “consciousnessraising” became something of a fad and a profession.

If the first task of leadership is to bring to consciousness the followers’ sense of their own needs, values, and purposes, the question remains: consciousness of what? Which of these motives and goals are to be tapped? Leaders, for example, can make followers more conscious of aspects of their *identity* (sexual, communal, ethnic, class, national, ideological). Georges Sorel argued that only through leadership and conflict, including “terrifying violence”, could the working class become conscious of its true identity – and hence of its power. But to what extent was Sorel imposing his own values and goals on workers who might have very different, even idiosyncratic, ones? We return to the dilemma: to what degree do leaders, through their command of personal influence, substitute their own motives and goals for those of the followers? Should they whip up chauvinism, feelings of ethnic superiority, regional prejudice, economic rivalry? What must they accept among followers as being durable and valid rather than false and transient? And we return to the surmise here: leaders with relevant motives and goals of their own respond to followers’ needs and wants and goals in such a way as to meet those motivations and to bring changes consonant with those of both leaders and followers, and with the values of both.

## The Elevating Power of Leadership

Mobilized and shaped by gifted leadership, sharpened and strengthened by conflict, values can be the source of vital change. The question is: at what level of need or stage of morality do leaders operate to elevate their followers? At levels of safety and security, followers tend to conform to group expectations and to support and justify the social order. At a certain stage Kohlberg finds a “law and order” orientation toward authority, fixed rules, and maintenance of the social order for its own sake. At a higher stage Simpson found a significant relation between tendencies toward self-esteem and positive law values (belief that the authority for judgments rests in the laws and norms humans have developed collectively). This is the level of “social contract morality”.

At the highest stage of moral development persons are guided by near-universal ethical principles of justice such as equality of human rights and respect for individual dignity. This stage sets the opportunity for rare and creative leadership. Politicians who operate at the lower and middle levels of need and moral development are easily understood, but what kind of leadership reaches into the need and value structures, mobilizing and directing support for such values as justice and empathy?

First, it is the kind of leadership that *operates at need and value levels higher than those of the potential follower* (but not so much higher as to lose contact). This kind of leadership need be neither doctrinaire nor indoctrinative (in the ordinary sense of preaching). In its most effective form it appeals to the higher, more

general and comprehensive values that express followers' more fundamental and enduring needs. The appeal may be more potent when a polity faces danger from outside, as from an invasion, or from inside, as in social breakdown, civil war, or natural catastrophe. "If inefficiencies and corruption of governmental and social leadership go beyond 'normal', if demands are constantly frustrated by incapacities, which can be readily laid at some human door, if all of this is compounded by a rising consciousness of discrimination and sense of justice", according to a four-nation study, "then people can experience great and often very sudden transformation of values, or those values that were subdued can become the basis for vigorous action". No single force, such as economic conditions, predetermines change, this study concluded; other factors – notably the quality of leadership – intervene, so the role of values in social change varies from culture to culture. Among the nations studied (India, Poland, the United States, Yugoslavia) similarities were found in leaders' espousal of innovative change, economic development, and the norms of selflessness (commitment to the general welfare) and honesty.

Second, it is the kind of leadership that *can exploit conflict and tension within persons' value structures*. Contradictions can be expected among competing substantive values, such as liberty and equality, or between those values and moral values like honesty, or between terminal values and instrumental values. "All contemporary theories in social psychology would probably agree that a necessary prerequisite to cognitive change is the presence of some state of imbalance within the system", Rokeach says.

Leaders may simply help a follower see these types of contradictions, or they might actively arouse a sense of dissatisfaction by making the followers aware of contradictions in or inconsistencies between values and behavior. The more contradictions challenge selfconceptions, according to Rokeach, the more dissatisfaction will be aroused. And such dissatisfactions are the source of changes that the leader can influence. There is an implication in Rokeach that the contradictions in themselves cause change, simply on the basis of self-cognition. Typically, however, an outside influence is required in the form of a leader, preferably "one step above". Rokeach bases much of his analysis on experimental situations in which the subjects are exposed to close direction and restraint – certainly a context of manipulation if not of leadership. Autonomous cognition usually is not enough to enable persons to break out of their imprisoning value structures. Experimenters may assume a leadership role.

Given the right conditions of value conflict, leaders hold enhanced influence at the higher levels of the need and value hierarchies. They can appeal to the more widely and deeply held values, such as justice, liberty, and brotherhood. They can expose followers to the broader values that contradict narrower ones or inconsistent behavior. They can redefine aspirations and gratifications to help followers see their stake in new, program-oriented social movements. Most important, they can gratify lower needs so that higher motivations will arise to elevate the conscience of men and women. To be sure, leadership may be frustrated and weakened at the higher levels as well as the lower. Potential support may thin out when

immediate parochial needs and values threaten to weaken higher, more general ones. Substantive values, such as liberty or equality, may compete with one another, and, however logically compelling the leader's value priorities may look, they may not co-exist so harmoniously in the political arena. Perhaps the most disruptive force in competitive politics is conflict between *modal values* such as fair play and due process and *end-values* such as equality. Roosevelt's court-packing plan, with its use of dubious means to attain high ends, is a case in point. Some of those believing in equal opportunity today may also believe in certain modes of conduct – endless debate, for example, or elaborate procedures for judicial review – that make the attainment of equal opportunity far less certain.

The potential for influence through leadership is usually immense. The essence of leadership in any polity is the recognition of real need, the uncovering and exploiting of contradictions among values and between values and practice, the realigning of values, the reorganization of institutions where necessary, and the governance of change. Essentially the leader's task is consciousness-raising.

By the same token, Weber's ethic of ultimate ends emphasizes the demands of an overriding, millenarian kind of value system at the expense of the far more typical situation (at least in pluralistic societies) in which choices must be made among a number of compelling end-values, modal values, and instrumental values. And the ethic of responsibility could rather be seen as the day-to-day measured application of the "ethic of ultimate ends" to complex circumstance.

For the study of leadership, the dichotomy is not between Weber's two ethics but between the leader's commitment to a number of overriding, general welfare-oriented values on the one hand and his encouragement of, and entanglement in, a host of lesser values and "responsibilities" on the other. The four-nation study notes the "most important motivational distinction among leaders desiring change – the distinction between those who see progress primarily in terms of political opportunity and those who nurse a feeling of social injustice arising out of the gap between the economically deprived and the privileged", even though no consistent relationship seemed to explain it. The great bulk of leadership activity consists of the day-to-day interaction of leaders and followers characterized by the processes described above. But the ultimate test of moral leadership is its capacity to transcend the claims of the multiplicity of everyday wants and needs and expectations, to respond to the higher levels of moral development, and to relate leadership behavior – its roles, choices, style, commitments – to a set of reasoned, relatively explicit, conscious values.

# Why Work?<sup>1</sup>

Joanne B. Ciulla

What's so good about work? Throughout history some have praised it, others have cursed it, but few escaped it or had the luxury of deciding whether they should work or not. At some time or another we all wish that we didn't have to work. We fantasize about catching up on chores or hobbies, spending more time with family, friends or a loved one, reading great books, and traveling. Lotteries seduce with the vision of freedom from work and material need, yet a surprisingly large number of lottery winners and other independently wealthy individuals continue to work. It is easy to imagine not working for a short time; the task of imagining a whole life without work is more difficult. For some people the question "Why work?" is ridiculous because they don't have a choice in the matter. "We work because we have to make a living." That is why people have paid jobs, but it doesn't explain why they do other kinds of work. Nonetheless, the economic interpretation of work is so strong in our culture and a growing number of other cultures, that we tend to equate work with "being on the job".

## Is the Idle Mind the Devil's Workshop?

One long held belief is that if people didn't work, they get into mischief. That "the idle mind is the devil's workshop". This is sometimes the case for those who are unemployed and have no other source of income. A 33-year old mother from a poor West Side neighborhood in Chicago, puts the problem of living with people who don't have jobs this way, "When you live in an area of your neighborhood where you have people that don't work... you have to worry if somebody's breakin into your house or not. So, you know, it's best to try to move in a decent area, to live in a community with people that works." (Wilson 1996, p. 11) But what if these people had income, but didn't work, Would they still get into trouble?

In his book *When Work Disappears*, William Julius Wilson observes when work is scarce people not only suffer from poverty, they "lose their feeling of connectedness to work in the formal economy; they no longer expect work to be a regular and regulating force in their lives" (Wilson 1996, p. 52). Wilson says work in the infor-

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mal economy and illegal economy differs from work in the formal economy because it is usually less regular and does not place a premium on discipline and regularity. He believes that when jobless people live in low-employment neighborhoods, they lose their perception of self-efficacy or their belief that they can take steps to achieve goals required in a certain situation. (Wilson 1996, p. 75) So according to Wilson, having a job means more than just meeting material needs. It also satisfies various psychological and social needs such as discipline, connectedness, regularity, and self-efficacy. But is work the only way to fill these needs? Why can't the unemployed fill these needs from leisure?

A sociographic study from the 1930's sheds some light on this question. Researchers observed a small industrial community in Austria called Marienthal at a time when the entire community was out of work. The sociologists noted that before the economic depression, people in the community were active in leisure as well as work. They participated in political organizations, frequented the public library, and enjoyed organizing various social events. After the town factory closed and everyone was out of work, the citizens became apathetic. The researchers note that the workers of Marienthal,

... cut off from their work and the outside world, lost the material and moral incentives to make use of their time. Now that they are no longer under any pressure, they undertake nothing new and drift gradually out of ordered existence into one that is undisciplined and empty. Looking back over any period of this free time, they are unable to recall anything worth mentioning. (Jahoda et al 1971)

Unemployment seemed to suck the energy out of people and the community. Marienthal' citizens not only lost their work, but they lost their ability to enjoy leisure. Clearly, the people in Marienthal were different from those in Wilson's study. They had work and lost it. Whereas, most of the people Wilson studied either cannot get work or have never really had steady jobs. Marienthal's citizens lost work and its social benefits such as self-efficacy, connectedness, and regularity. Many of the people in Wilson's study never had work and its social benefits. Perhaps the reason that the unemployed do not have leisure is because they have no work. They have no *free* time because they have no *constrained time*. A Union newspaper summed up the problem this way: "The trouble with unemployment is that you never get a day off." (Corrigan 1989, p. 192)

Aristotle offered another insight into why the unemployed don't have leisure. According to him you could not have leisure without peace, the proper virtues, and education. "Courage and endurance are required for business and philosophy for leisure, temperance and justice for both, and more especially in times of peace and leisure, for war compels men to be just and temperate, whereas the enjoyment of good fortune and the leisure which comes with peace makes them insolent." (Aristotle, pp. 2117) Aristotle used the case of Sparta to illustrate this point. Sparta's culture was centered around war and preparation for war. Serfs called helots did the Spartan's work. Sparta thrived as long as it was at war, but col-

lapsed in times of peace. Aristotle said Sparta was not governed in a way that was conducive to a life of leisure. Men were given a military education, which taught them discipline, and that carried over into peace time, but women had no such education and lacked discipline or self-control. As a result of this, in times of peace the women fell into luxury, vice, and chaos far worse than any enemy the Spartans had faced in war. (Aristotle, pp. 2014-2016) Furthermore the Spartans could never really have leisure because their serfs could rebel at any time. He concluded without a safe society and citizens who were taught the right virtues, people could not have leisure. This idea partly explains the Marienthal case. Its citizens were educated by the virtues of the Protestant work ethic. According to their social values, paid employment was the most important activity in life, leisure or amusement a mere accompaniment. Without work they were not capable of leisure. Without paid work the workers of Marienthal were failures. But perhaps most importantly, without work they had no security.

For Aristotle our real work in life is the work of being human. Freedom from fear, material needs, and commitments allows us the liberty to develop ourselves through leisure. War and education, (not work), provide people with moral virtues such as temperance and discipline needed for leisure. Aristotle believed that education for leisure would teach people how to engage in learning and activities that are good in themselves, because it is these activities that make humans unique from animals. He suggests that students study subjects such as reading, writing, drawing, physical training and music. (Aristotle, pp. 2121-2128) This idea of education is the basis of the liberal arts, which are the arts needed to live in a free society. The Roman Cicero also believed in the liberal arts. He said education should separate the truths needed for life's necessary cares from knowledge that is pursued for its own sake. The liberal arts ideal is knowledge that we pursue for its own sake. It is ironic that most students today pursue a liberal arts education so they can get a job, when ideally it was meant to teach them how to use their leisure, not how to work.

After looking at Aristotle's criteria for leisure, one can see why it is callous and cynical to think that the unemployed lead lives of leisure. Leisure is more than free time, it is freedom from need and the necessity of work, and an opportunity to do specific things. (Oxford Dictionary 1991, p. 815-6) People who have lost their jobs or cannot get jobs are not free *from* work. If anything, they are not free *to* work, since they have little choice in the matter. Leisure also requires safety and security, which do not characterize the urban areas of unemployment described by Wilson. Lastly, Aristotle tells us, leisure requires education, which imparts knowledge and moral virtues such as justice and self-discipline. Leisure also gave the ancient Athenian time to participate in civic affairs, which would certainly enhance a person's feeling of self-efficacy. In theory at least, if you set up a society for Aristotelian leisure, it might provide people with the same psychological and social needs as a society set up for work. In an Aristotelian utopia there would be no idle minds, hence no workshop for the devil.

What is most interesting and distinct about being human are the things that we choose to do with ourselves *after* we meet our basic needs. If those in poor neighborhoods with high unemployment were magically given an income that met their basic needs, safe streets, and solid liberal arts educations, they would be just as likely to go out and get good jobs, than lead lives of leisure. For example the way lottery winners respond when the necessity to work is removed depends on their material wants and desires, their ambition and whether they liked their jobs. But what about those who don't need to work and choose not to work? Do we really believe that without a job they will become morally decadent?

## Do We Need Work?

Elizabeth Perle McKenna had never realized how much of her identity and self-worth was tied up in her high-powered job as a publishing executive. "The first week without a paycheck I became worthless instantly. I was a three-legged stool and without a job to do every day, I toppled over." (McKenna 1997, p. 14) In her book, *When Work Doesn't Work Anymore* McKenna explains that she quit her job because she realized that she wanted a more flexible life. Her job no longer fit with her values and aspirations. Yet once she left her job, she discovered the difficulty of constructing an identity outside of the one on her business card and a life without work. It's not easy to feel sorry for McKenna. Her husband makes a good living, she is well educated, and she is not "unemployed". McKenna had the luxury of deciding whether to work or not. Nevertheless, cases like hers demonstrate why choosing not to work has its costs. Without work, we face infinite options about what we should do and what we should be. Also, people who can work but choose not to, have to explain themselves to those who suspect the only reason they gave up good jobs and choose not to work is because they are lazy or some way deficient.

Aside from providing income, it's easy to see why having a job is so desirable in our culture. Work works for us. It offers instant discipline, identity, and worth. It structures our time and imposes a rhythm on our lives. It gets us organized into various kinds of communities and social groups. And perhaps most importantly, work tells us what to do every day. Even with education, income, peace, and security, the free choice not to work is difficult in a culture where paid work is so central to life. Many of us would find it a challenge to fill every day with activities that give the feelings of satisfaction and well-being we get from work.

The satisfaction and well being that some people get from having a job is undeniable. Work provides for our material needs, but is work itself a human need? Many scholars have said no. For example, Jean-Jacques Rousseau noted that indolence is the natural condition of humans and the need to be productive is an artificial one produced by society. (Rousseau 1973, p. 104) Georg Wilhelm Friedrich Hegel said that the "habit of industrious" is a product of work itself and that the practical education we get through working creates the need to have something to do and the habit

of being busy. (Hegel 1952, p. 129) We *feel* the need to work because of our training and moral conditioning, not because of any inborn disposition. If this is the case, then there is nothing “natural” about work. It is an artificial need manufactured by our history and culture.

The idea that humans *need* to work is so embedded in modern Western economic and moral assumptions that it is difficult to understand cultures where people don’t share this need. Karl Marx once cited a newspaper story in which a West Indian Planter is indignant about the fact that the free Negroes of Jamaica, the Quashees, refused to work beyond their own consumption and look upon “laziness itself (‘indulgence’ and ‘idleness’) as the real luxury article” (Marx 1973, pp. 325-6). An anthropologist made a similar observation in 1961. He noted that the Yamana Indians in South America “are not capable of continuous daily hard labour, much to the chagrin of the European farmers and employers for whom they often work. Their work is more a matter of fits and starts...” (Sahlins 1928, p. 28). Modern companies have faced similar problems in developing countries where they cannot get employees to work overtime, because workers prefer leisure over the extra cash. Lately a growing number of overworked Americans have expressed a preference for free time over money, preferring to get time off rather than overtime pay for extra work.

In his study of hunter-gatherer societies, anthropologist Marshall Sahlins found that hunter-gatherers worked far less than people in other cultures. For example, the Arnhem Land aborigines in Australia spend about 4 or 5 hours a day getting and preparing food. Moreover they do not work continuously and usually stop working when they have enough for the time being. When not working, they spend their free time in rest and sleep, not in Aristotelian leisure. He concludes, with a tinge of disapproval, that the reason why primitive societies fail to “build culture” or develop “is not strictly from want to time. It is from idle hands” (Sahlins 1928, p. 20). We usually think of development for hunter-gatherers or whole countries as something that makes life easier, but the increase in the material quality of life usually entails an increase in the quantity of work. Sahlins observes that maybe aborigines don’t want to build culture. As one bushman asked him, “Why should we plant when there are so many mongomongo nuts in the world?” (Sahlins 1928, p. 27)

## To Work or Not to Work?

Most people who live in industrialized, democratic societies have more choices than their ancestors about where they live, what they do for a living, how they live, and who (what kind of person) they want to be. No one questions the necessity of work, but to explore the meaning of work we have to question its merit. Besides keeping ourselves alive and reproducing, why is work better than play? What is the value of a job? How should we live? Different people in different cultures will answer these questions in different ways. Yet, when it comes to work,

it's doubtful that human nature varies much. Some like to work and some don't. In any culture at any time, there are and have been industrious and lazy people. Only the standards of judgment are relative to the place and time.

The ancient storyteller Aesop sums up some of the basic questions about work and life in his fables. We still find meanings in his tales about animals who remind us of people we know, and appreciate his moral lessons on how to live. Aesop's musings on work are all the more interesting because he was a slave from Asia Minor who later bought his freedom. (Brewer 1989) His fables were written around 620 BC, but some of his stories exist in various forms on Egyptian papyrus that date back to 1000-800 BC. In the well-known fable, "The Grasshopper and the Ant", Aesop locks horns with the question, To work or not to work? Aesop also explores the complexity of this question in other stories about cicadas, ants, and bees. These insects crawl, buzz and hop their way through history. Each insect represents a set of dispositions, values, and ways to think about life and work. Consider, for example, the "Grasshopper and the Ant".

The ants were employing a fine winter's day in drying grain collected in the summer time. A grasshopper, perishing with famine, passed by and earnestly begged for a little food. The ants inquired of him, "Why did you not treasure up food during the summer?" He replied, "I had not leisure enough. I passed the days in singing". They then said in derision: "If you were foolish enough to sing all the summer, you must dance supperless to bed in winter." (Aesop's Fables 1924, p. 16)

This is a cautionary fable. It does not say that a life of work is better than a life of singing, but rather that if you want to sing, you should be willing to pay the price. The issue here is fairness and self-sufficiency – if you don't work, you don't eat and you shouldn't expect others to feed you. Aesop's story gives us a choice. We can lead the brief happy life of the grasshopper, or the long prudent life of the ant. Yet it's not wholly clear what the wise person should choose. The ant teaches a clearer lesson in the Bible. Proverbs' 6:6-8 says, "Go to the ant, thou sluggard; consider her ways and be wise: Which having no guide, overseer or ruler, Provideth her meat in the summer, and gathereth her food in the harvest." In *Thessalonians* 3:6-12, St. Paul says, do not burden others by eating their bread, "If any would not work, neither should he eat."

Unlike the good Protestant who would come along later, Aesop is somewhat ambivalent about industriousness. Greed, miserliness and covetousness sometimes accompany hard work. In "The Ant", he tells us that the ant was once a farmer who kept a jealous eye on his neighbor and stole some of his produce. Zeus, angry, changed the man into an ant and Aesop says, "Although his form has changed, his character has not, for he still goes around the fields gathering up the wheat and barley of others and storing it up for himself." (Daley 1961, p. 163) Aesop worried that industriousness, when motivated by envy can lead to theft and/or avarice and miserliness. As we'll see later, the early Christians shared this concern.

## Cicadas and Bees

Aesop is kinder to the grasshopper's relative, the cicada. He says that once there were men who, when music was invented, were so happy that they just kept singing and forgot food and drink until they died. From these men come the cicadas, who don't require food and sing their lives away. (Daley 1961, p. 251) The muses smile upon the cicadas because their singing brings joy. While Aesop doesn't exactly endorse the life of the cicada, he does express a somewhat romantic admiration. The cicada's brief life is spent in pursuit of beauty. Not everyone is as kind to the grasshopper, who became a shorthand icon for the noisy and useless. In Ecclesiastics (12:5) we read "the almond tree shall flourish and the grasshopper shall be a burden."

The aesthetic virtues of the cicadas and the moral virtues of the ant come together in Aesop's called the "Ant and the Bee". In it the bee and the ant have a dispute over who is more prudent and industrious. They appeal to Apollo for a judgment. The god applauds the ant's care, foresight and independence from the labors of others, but he says, "it is you alone that you benefit; no other creature shares any part of your hoarded riches. Whereas, the bee produces, by his meritorious and ingenious exertions, that which becomes a blessing to the world." (Northcote 1833, p. 11) Again we see chinks in the moral armor of hard work. It's good to provide for oneself. It is even better to contribute a pleasing and useful product for society. Poetry and literature portray bees as more cheerful workers than ants. After all, bees work in flowers and make tasty honey. Remember the famous Issac Watts rhyme: "How doth the little busy bee, Improve each shining hour, And gather honey all the day, From every opening flower." (Watts 1854, p. 320)

Successful business people don't want the public to think they are ants. We admire hard work much more if people do it for some purpose that lies beyond pure self-interest. During the period of hostile takeovers in the mid-80's, investors such as T. Boone Pickens and the late Sir James Goldsmith strenuously tried to portray themselves as bees. In a PBS debate Sir James claimed that hostile takeovers "cleanse" society of inefficient businesses. Pickens asserted that he helped the economy by getting rid of wasteful managers and doing a better job of running companies. Both men argued in the tradition of the Dutch doctor turned poet, John Mandeville, not Aesop. Mandeville crossed the ant with the bee and came up with an explanation for an economic system based on self-interest not thrift. His poem "The Fable of the Bees", presented the paradox of how personal vices and vicious motives could lead to the public good. The poem was considered so immoral that the Grand Jury of Middlesex, England declared it a nuisance in 1723. (Keynes 1936, p. 359) Mandeville believed that the desire for money, power and fame are the only reasons why people work. There is no moral value to work, only the instrumental value of what it buys and produces.

His poem begins,

A spacious Hive well stocked with Bees  
That lived in luxury and ease  
Millions endeavoring to supply,  
Each other's lust and Vanity,  
Whilst other millions were employ'd,  
To see their Handy-works destroy'd. (Mandeville 1724)

The social order of the hive, like a modern market system, depends on competition and self-interest to provide for the needs of society. In this system, some win and some lose. Nonetheless, Mandeville goes on to say "every part was full of Vice, Yet the whole Mass a Paradise" and "Envy itself and vanity, Were ministers of industry." (Mandeville 1724, p. 109) The idea that serving personal interests can lead to public benefit is central to capitalism. (cf. Hirschman 1976) Mandeville argued that thrift is not a virtue for the rich, because if they ceased to spend their money, the poor would be unemployed. (The economist John Maynard Keynes approvingly cited Mandeville's poem in the 1930's when he argued that thrift was not a virtue in times of chronic unemployment). (Keynes 1936, p. 358) Mandeville's bees worked like ants, consumed like grasshoppers, *and* brought about the greatest good.

Today, the environmental movement, among others, encourages us to replace Mandeville's bees with the species found in the sacred Buddhist scriptures. Here the bee is become a paradigm of ecological responsibility. The scriptures tell us "The wise and moral man, Shines like a fire on a hill top, Making money like a bee, Who does not hurt the flower." (Scripts of Theravada Buddhists)

## Life Strategies

Aesop's ant, grasshopper, and bee give us three ways of approaching life. Frugal, acquisitive, and hard working, the ant-like worker values security above all else. He spends all of his time working at a moderately interesting job, makes cautious career choices, has little involvement in non-work activities, takes few vacations, and takes fewer chances. Like the ant, this sort of person saves for retirement, mortgaging certain enjoyments for 65 years of his or her life, in hopes of making up for it in the last 20.

In Thomas J. Stanley and William D. Danko's study of American millionaires one interviewee expressed the ant's position, "My long range goal was, of course to accumulate enough wealth so I can get out of business and enjoy life." (Stanley/Danko 1997, p. 45) This plan can fail for a variety of reasons. A life-long habit like frugality is hard to break. Stanley and Williams found that the most of the self-made millionaires they studied were thrifty and did not change their spending habits much after they had made their fortunes. One interviewee described to them his wife's reaction when he gave her \$8 million dollars worth of stock. She said, "I appreciate this, I really do." Then she went on clipping out

twenty-five-cent food coupons out of the newspaper. Her husband explained, “She just does today like she always has done, even when all we owned was a kitchen table.” (Stanley/Danko 1997, p. 37)

For some people, the art of enjoying life is difficult to learn at a late age. There are those who retire with generous pensions, but still carry on their ant-like habits, whether it’s saving string or refusing to buy a new car or some other commodity that will make them more comfortable. Others suffer ill health, and a sad few die the day after they receive their gold watch. While the ant may not take pleasure in spending money and owning things, he may delight in the daily challenges of living frugally. Many people work so they can enjoy buying more, the ant may work to enjoy spending less. Hence the retired ant may spend a whole morning driving from store to store, looking for the best price on a can of tuna fish (especially if he or she grew up during the Great Depression).

The ant lives for the future, but doesn’t always know what to do when he reaches it. The merit of the ant’s life plan is that his frugality saves him from want and prepares him for emergencies, but money also ensures freedom. One of the millionaires interviewed by Stanley and Williams called his stashed away money “go to hell money”. He could work at will, knowing that he could walk away any time he wanted. Work feels very different when you can take it or leave it.

One way to overcome the shortcomings of the ant strategy is to work hard, make a fortune, and retire at 40, which is what many young people today hope to do. That way they can still enjoy life while they are young. Often this kind of ant is really a grasshopper in disguise or an *anthopper*. Such characters worked long hours and focused solely on making money – and a few made it. This strategy faces four possible pitfalls. First, unlike Aesop’s ant, the anthopper is impatient and has a difficult time with delayed gratification. Anthoppers want to make *fast* money. Second they often cannot quit working because instead of hoarding money, the anthopper creates a style of life that requires more and more cash. The third problem is that anthoppers, by putting all their time and money into work, risk harming their relationships with friends, spouses, and children. The anthopper’s spouse or partner may not wait around to enjoy his or her early retirement. Finally, anthoppers can become so addicted to money-making pursuits that they don’t stop working even when they reach their financial goals. They never have enough money or they become addicted to the work itself and the excitement of making money.

Both the ant and the anthopper work in anticipation of “the good life” in the future. They often fail to enjoy life in the present. How do the ant and the anthopper experience work? Clearly work has instrumental value to them, but do they seek meaning in their work? Do they find pleasure in it? Some people spend all their lives working and sacrificing for some the prize of happiness and freedom from work that they believe exists at retirement. When they get to retirement, they realize that the real happiness was in the striving. They don’t know what to do with freedom from work. For others who have just worked to make a living, work becomes such a habit that they have a hard time living without it. When Eric Hoffer retired from the waterfront he said he still kept dreaming of loading and unloading



ships and sometimes woke up in the morning aching all over from a nights work. He wrote, "One might maintain that a pension is pay for the work we keep doing in our dreams after we retire." (Hoffer 1982, p. 109)

In contrast to the ant, the grasshopper lives for the present and sacrifices the future. His playing goes nowhere and leaves nothing behind. There is pleasure in a life of play, but is there meaning? The bee works like an ant, but enjoys his pursuits like a grasshopper. It takes pleasure and finds meaning in producing a good and useful product that is appreciated by others. The bee symbolizes a life of useful and rewarding work. (Needless to say, the symbolic bee bears no resemblance to the life of real bees). While the ant represents a life of work and security, the grasshopper depicts a frivolous life of play and uncertainty. But what is wrong with a life of play?

## **Working at Play, Playing at Work?**

In his book *The Grasshopper: Games Life and Utopia*, Bernard Suits creates a dialogue between a philosopher grasshopper and his disciples about work and play. He raises a fundamental question about life. If we did not need to work to provide for the things that we need, what would we do with ourselves? The grasshopper defines play as any intrinsically valuable activity. Ants see work as an instrumental activity. Play is an end-in-itself. The grasshopper then argues, in the spirit of Aristotle, that the ideal of existence is doing "only those things whose only justification is that they justify everything else" (Suits 1978, p. 166). In *The Grasshopper*, Suits speculates that if we lived in a utopia where no one had to work, we would eventually invent games that resembled work. The carpenter would invent house building games, the scientist, discovery games, even though there was no need to build houses and all discoveries had been made. Suits believes that in his utopia work activities would become play because people would freely choose to do them, for their own sake and not for some outside goal. Here people would be playing at their work instead of working at their play. People who love their jobs or work in organizations that try to make work fun say work *feels* like play, but they are not playing at their work. According to Suits argument, you can only play at your work if two conditions are met. First, you don't have to work, and second, you can work any where, any time, and any way you want.

In Suits' Aristotelian utopia the ant's life does not make sense. It isn't necessary to save for the winter. However, the bee's life is plausible in this utopia. Like the ant, Aesop's bee works hard but unlike the ant, he still enjoys making honey for either the process itself or the pleasure its product brings. Today people grow their own vegetables and bake their own bread, even though they can buy them in a store. The home baked bread and home grown vegetable, despite claims to the contrary, may not be superior in quality to the ones that people buy, but the very process of making and growing makes eating them more enjoyable. Some types of

productive activities give satisfaction even though they are not necessary or especially because they are not necessary. The bee's work has the *promise* of meaning even if it is not necessary to survive.

Sometimes people try to make play sound like productive work. We legitimize play in a work oriented society by *working* out, playing squash to unwind, tennis to stay fit, golf to woo clients, boxing for security, jogging for cardio-vascular health, etc. We talk about efficient use of body energy, we train, we read books and watch videos on how to play. Intense competitiveness in games and sports shifts the focus of playing to winning, which makes play instrumental and more like work. Even animals aren't exempt from non-productive play. Note how the narrator of a Discovery Channel show on lions solemnly explains to the viewer that the frolicking lion cubs may *think* they are playing but they are *really* practicing skills that will make them good hunters.

This takes us very far from Plato's idea of play. He said that play evolved from the desire of children and small animals to leap. Think for a moment of the delight children and puppies get simply from jumping up and down. Play is often illogical and/or inefficient. Games are intentionally inefficient. The things that people do when they play them have no meaning outside the game. For example, if your job required you to put little white balls into 18 holes, you certainly wouldn't do it by hitting it with a thin stick over lakes, hills, and sand traps. The point of golf is to make it as difficult as possible to get the ball into 18 holes. Getting the ball into the hole is important to the player, but *having* the golf balls in the holes serves no purpose whatsoever outside of the game.

Play, like the cicada's singing, is done for no reason but pleasure. While the Aesop's grasshopper starves because he is irresponsible, the cicada is the "starving artist". It starves for love of music. The two fables convey different messages. Dying because of one's love of art seems to have a point, whereas, dying because one prefers to play games does not (unless you are an Olympian or amateur athlete). For most of us the more relevant questions are not about play. They are, "Does life have a point if you live like an ant, working and accumulating things until you are aged and feeble and closer to death?" and "Given freedom to choose, what should be doing with the time given to us in life?"

## How We Choose Our Jobs

Four values shape how we make choices about work. (cf. Hayworth 1977, ch. 4) They are meaningful work, or work that is interesting, and/or important to you or to others in society; leisure or free time to do the things you want; money, and security. These values carry different weights at different times in life. Ideally it would be best to have a fascinating job, plenty of vacation time, a salary that allows you to buy anything you want, and guaranteed lifetime employment. Since few of us have jobs that provide all of these things, we make tradeoffs and these tradeoffs signify

what we value most. Consider the following thought experiment. Imagine that you are single and have just graduated from college. You have four job offers. The first is a well-paying position in an accounting firm, the second is with the environmental group Greenpeace, the third is a civil service job, and the fourth is a place as a waiter at an Aspen ski resort hotel that only operates in winter. Which one would you choose?

The answer derives from another question: What are you willing to give up? People driven by the values of meaningful work and leisure are often more willing to give up security and money. If meaningful work is most important, you might choose Greenpeace. This job entails long hours without much pay or financial security in a environment that is sometimes dangerous. The resort job may not give you much meaning, money or security, but it will give you plenty opportunities to do what you love best, namely ski. Meaningful work and leisure have a lot in common. People who subscribe to these values like the idea of doing something that they want to do. They value certain activities either for what they are or what they mean.

Some people prefer leisure to meaningful work because they do not want to or cannot engage in the activity they love as paid work. They turn to other activities (hobbies, music, sports, and even crime) and other institutions (family, friends, church and community organizations) for the psychological rewards that they can't get from work. (Work in America 1973, p. 10) For example, not everyone who loves to cook would enjoy working as a chef. In fact, working as a chef in a restaurant day in and day out may diminish the pleasure that one gets from cooking. Meaningful work and leisure consist of activities that aren't just instrumental, but are rewarding or pleasurable in their own their own right.

If you value money and security above other things, then work is primarily an instrumental activity, a means to those ends. For example, the accounting job may not be exciting and few people ever make it to partner, but as a new graduate, you will make good money to pay off college loans, buy a condo, nice clothes, and a sports car. Those who value material goods above and beyond what they need to live comfortably, trade leisure for overtime or second job to buy extra cars, etc. Their pleasure in buying and owning things overrides their desire for free time. (Money is also important to those who value security; however, they value saving it over spending it). If you want security, the government job may fit the bill. Even though it may not be fast-paced and exciting, and you'll make less money than you would if you were in industry, the benefits are excellent, you get all the standard holidays, and it's relatively stable employment.

At different points in one's life, different values dominate. The new graduate may choose the resort job, because he or she likes to spend the summer months surfing or traveling, but this might not be an option if the person has a family to support. Single parents sometimes have to choose between a challenging and time consuming career and one that allows more time to spend with their children. Here free time is more important than money or their job. People who are in mid-life face harder choices. New opportunities force them to decide what is really impor-

tant. For example, they might be given the choice between a challenging new job with a risky start-up company or their current mundane but well paying job and the comfortable life that it has created. For some people, the choice is easy, because they know that twenty years in their current lucrative and prestigious job did not make them happy or their work no longer gives them satisfaction because the job or the organization has changed. Others will stick it out at the old job because they cannot give up their financial or psychological security. Our choices aren't always this stark or this simple, but we usually have to settle for more or less of each of these values when we choose a job.

## Odd Choices?

There are many variations on how the values of meaningful work, leisure, security, and money play out in our lives. When people make unique choices about how they work, live, and spend, we often read about them in the newspaper or hear about them on the news. Consider the case Thomas Cannon. Cannon graduated from college with a degree in art education, but opted for the secure job and steady salary of a postal worker. He and his family lived very modestly on his salary – “We had food, we had clothes, we had all of the basic necessities.” (Ryan 1997, p. 16) For Cannon meaning didn't come from his job, or from building up a nest egg. Work was instrumental for caring for his family and for what it could buy for others. By the age of 72, Cannon had given away over \$96,000 to people in need.

People like Cannon are exceptional and admirable, but also a bit peculiar. We don't expect people who make so little to give so much away. Similarly, we don't expect people who have power, prestige and money to throw it all away. For example, James J. O'Donnell, the chief executive of HSBC James Chapelin London and HSBC Markets, Inc. in New York, made news when he announced that he was leaving his job to join the priesthood. The 36-year-old O'Donnell had a B.A. from Princeton in comparative religion. He had held a string of highly successful high-powered jobs in the financial world. O'Donnell declined to discuss his decision with the press, maybe because he didn't feel the need to explain himself or because he didn't think people would understand. (New York Times, Nov. 20 1997)

Some people leave their jobs because the work no longer gives them or fails to give them what they want from it or they have a burning desire to do something else. Just before the Christmas of 1996 Jeff Stambovsky placed an ad in a magazine the caters to Wall Street traders. It read, “Jeff Stambovsky Left the Business. If He Doesn't Sell Enough Records, He's Coming Back.” (Eaton 1998) Stambovsky, the 43-year old managing director of Schroder & Company quit his job to become a jazz musician and children's record producer.

Some anthropoppers do make it. They build up enough of a nest egg to take the plunge into their dream job. Christophe J. Richter vacated her job as a bond sales-

woman to start a message therapy studio. Judd S. Levy left Merrill Lynch to manage an inn in Vermont. He said that many people told him that they wished they could do that. Levy said, "The truth is that many of them could have." (Eaton 1998) But they don't. Many of us have an image of work that we'd really like to do, but few dare to give up the security, prestige, and buying power of our current jobs to do it. Taking the plunge into meaningful work is risky, the musician may not sell records, the massage business may flop, and the innkeeper may discover that staying at a Vermont Inn is more fun than running it.

Since women have had to overcome barriers to get prestigious, high paying jobs, they are sometimes ambivalent about leaving such jobs to pursue other interests. They don't want to ruin the chances for other women to make it to the top. They don't want to appear as if they can't handle the job, and they do not want to reinforce the idea that women shouldn't be put on the fast track because they will leave when they have children. Yet, stories abound of women who have left high-powered jobs to spend more time with their children. Brenda Barnes made headlines when she quit her job as chief executive of Pepsi North America to be with her three children. On the one hand these stories send the message that there is more important work in life than one's paid employment. On the other hand, they suggest that home is where mothers belong in the first place. In America, 63 percent of married women, who have children under six, work. (Ableson 1997) As a result of this, some women, especially the ones who love their jobs, feel guilty about working. For some, going to work is like sneaking off to have an illicit affair. Witness a television commercial for cell phones. The scene opens with a mother telling her two little daughters that she can't play with them because she has a meeting with clients. The wide-eyed youngest pouts and says "I wish that I could be a client." But for many women work is simply a necessity, caring for children a tricky balancing act, and they do not welcome "mommy books" and television commercials that tell them they should feel guilty. (Gross 1998, p. 9)

Affluent, well-educated married women have the greatest choice about work. That is why their defections from prestigious, high paying jobs are interesting. They are not pushed by economic necessity and they are not shut out of interesting jobs due to lack of education. Feminists fought to give women the option of working outside the home and the opportunity to advance to powerful, high paying jobs. Women didn't just want to work, they wanted a *real* choice between staying at home and working. Because of the value and prestige that certain jobs give people, we often forget that the choice can go either way. There have been many interpretations of highly publicized defections of women from good jobs, from the sexist "women can't hack it", to "women's natural mothering instincts call them home", to "the workplace isn't friendly to women's needs". But maybe the most radical explanation is that some women, like McKenna and the successful women she interviewed in her book, have discovered the "great job" that they worked so hard to get, wasn't what it was trumped up to be. Work was cutting into life outside of work. Life outside of work has more to offer than life at work. Poor women have always worked outside the home and have had few illusions about

what it is and what it means. However, because women are still relatively new to the ladder of success and high-powered positions, it might be easier for them to see when work is an emperor who isn't wearing any clothes. In recent years a growing number of men have also come to this conclusion.

What is so great about work? Some jobs are interesting and fulfilling and some are not. Some jobs are worth investing large amounts of time and energy and others zap us of our energy and time to enjoy other things in life. But what about work itself? In our culture work is virtuous and time without work, potentially dangerous. Work gives people identity, of self-worth, and the sense that they can shape and influence the world around them. Perhaps the most fundamental satisfaction that work offers is the satisfaction of earning a living, the satisfaction of getting what we need to stay alive.

But why does so much of our personal well-being and identity rest on our jobs, when there are so many other types of work and activities that we do in life? How did paid work get such a good reputation in our culture and increasingly in other cultures?

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PART III:

## **Organizational Ethics**



# **Organizational Integrity – Understanding the Dimensions of Ethical and Unethical Behavior in Corporations**

*Guido Palazzo*

## **Beyond Character – From Managerial to Organizational Integrity**

Organizational integrity refers to the ethical integrity of the individual actors, the ethical quality of their interaction as well as that of the dominating norms, activities, decision making procedures and results within a given organization. This article discusses these manifold aspects of organizational integrity and outlines the main driving forces and dimensions of ethical and unethical behavior in corporations. Reflections on ethics in general start with the assumption that it has to do with human actors who do or omit something. It has to do with their motives and the product of their interrelated activities. Thus, the individual might be regarded as the main point of reference for analyzing organizational integrity. However, the ongoing formalization and institutionalization of the ethical dimension of management is based on a simple observation: Organizational integrity goes beyond managerial integrity and is more than the presence of individuals with good characters within the organization. Having “good” managers is certainly a precondition for organizational integrity, but it does not prevent organizations from obtaining bad ethical results. It is possible to take the bad apples out of the barrel but the risk of deviant organizational behavior will not be reduced to zero. The good apples might develop a bad taste and sometimes it might be a problem of the barrel itself.

Philip Zimbardo’s prison experiments from the 1970s clearly demonstrate that good people might do evil things if they are put in an evil context (Zimbardo, 2004). When Zimbardo asked average students to roleplay prisoners and guards, they started to behave and to feel like prisoners and guards. Already back in the 1960s Hannah Arendt showed that Adolf Eichmann who was responsible for organizing the logistics behind the German concentration camps was not a brutal monster. Thoughtlessness, distance from reality and lack of moral imagination drove him in the wrong direction (Arendt, 1994/1963). Badaracco and Webb (1995) showed that young managers often feel pressured to act unethically. This does not necessarily come from their superiors but more from the organization as

such. Greenberg (1993) examined the immoral behavior paradox which is based on moral reasoning: The perception of being treated unfairly is used as a means of justifying striking back or rebalancing giving and taking. Some employees might steal from their employers in the name of justice. Furthermore, in modern societies, individual actions and decisions are embedded in complex networks of cooperation where harmless individual acts might in combination lead to disastrous results without or even against the intentions of the individual actors (Dörner, 1992).

These manifold parameters of ethical decision-making in organizations are reflected in a model that has been developed by Trevino. With her person-situation interactionist model, she argues that ethical decisions have to be analyzed along individual and contextual/situational lines (Trevino, 1996). While mainly building on Trevino's model, I will slightly restructure it and add aspects that in my view have been omitted or underestimated in her early model. Following Trevino, I describe the individual stage of cognitive moral development as the starting point of ethical decision making. "The individual's cognitive moral development stage determines how an individual thinks about ethical dilemmas, his or her process of deciding what is right and wrong in a situation" (Trevino, 1996: 602). However, knowing what the right decision in a given ethical decision-making situation would be does not necessarily mean that individual actors really do what they perceive to be right action. Corporate integrity does not solely depend on its numerous actors' correct ethical decision-making at all hierarchical levels. It furthermore depends on the *design of the context* in which those actors are embedded while making decisions and the individual actors' the *perception of that context*. In the next paragraphs I will first outline Kohlberg's theory of cognitive moral development and then describe the major contextual issues that moderate individual moral decision making and shape the ethical quality of organizations.

## The Individual Level of Moral Development

Kohlberg (1981) argued that moral reasoning is the result of a development process from childhood to adulthood. The older we get, the more elaborated and sophisticated our ability of moral reasoning becomes. How do we start to learn to make moral judgements? We start on the so called *preconventional* level, discovering that wrong behavior might be punished and right behavior might be rewarded. On this level, moral decisions are a constant fight between the desire to satisfy immediate interests and the fear of being punished or the hope of being rewarded for suppressing those interests. The next level of moral development has been labeled *conventional*. Human actors learn to internalize others' expectations. Humans learn that they can choose to play certain roles (e.g. good son/daughter) that are linked to certain standardized forms of behavior. They learn in a subsequent step that beyond their immediate community they are embedded in a larger societal context that disposes of a framework of law and order. Following these prescriptions, people internalize their roles as citizens. Behavior is controlled by

the outside world much like at the preconventional level. However, the difference is that on the preconventional level we make calculations while on the conventional level we execute learnt and often unconscious role behavior. It is only on the third level of *postconventional* morality that human actors start to think autonomously and to follow self-imposed universal principles that transcend the narrow context of their respective communities, societies and interests. The external authorities are replaced by internal authorities. While most adults have been classified by Kohlberg as being on the conventional level of moral reasoning, it is important to understand that individuals on any level of moral development are still able to practice the inferior forms of moral reasoning. An individual on the postconventional level is still open to group pressure or fear of punishment. Being on a postconventional level simply means that the actor has the ability to transcend the inferior levels of moral reasoning. It does not mean that she/he necessarily does transcend it in his decision-making. As argued by Trevino, the Kohlberg scheme delivers a valuable basis for understanding “how managers think about ethical dilemmas in their work” (Trevino, 1996: 608). The Kohlberg scheme does not help to discover how managers or employees in general really decide and act in ethical dilemmas, since these decisions are moderated by contextual and further individual factors (Trevino, 1996). Furthermore, the Kohlberg scheme does not help to find and understand these contextual and individual factors and how they interplay with the individual level of moral reasoning. However, if organizational integrity may be considered as the result of that interplay, a profound understanding of such an interaction is important for the management of ethics within organizations. In the following paragraphs, I will discuss two types of moderators of ethical behavior, contextual design and contextual perception.

## Perceptions of the Context

### Moral Imagination and Managerial Language

Sometimes illegal and unethical behavior can be explained by the bad character traits of the actors involved and the low level of their moral development. However, in some cases, it might simply be a lack of moral imagination that leads to deviant behavior. In such cases, people simply do not see the moral dimension of their actions or decision-making and thus can not take it into consideration. Sometimes, neither the damaged dignity of a laid off manager nor the misery of a working child do pass the filter of managerial world perception. Ethics in that case is nothing but noise within the system even if the affected managers might have good characters or might be engaged in philanthropic causes in their spare time. How can this lack of moral imagination be explained? Analyzing the language used by managers within corporations might help to understand this seemingly schizophrenic behavior, because the world perception and sense-making filters of an individual actor are revealed in the language he or she uses.

Organizations have been analyzed as networks of shared meaning with meaning being transmitted through the “use of a common language and everyday social interaction” (Walsh & Ungson, 1991: 60, see also Smircich & Subbart, 1995). As a result, organizations develop cognitive maps as filters of their world perception (Ring & Rands, 1989) which can be analyzed by examining the language used by the actors in the corporation (Ferraro, Pfeffer & Sutton, 2005). This seems to be the key assumption behind Weick’s seemingly paradox question: “How can I know what I think until I see what I say” (Weick, 1995). Apparently, corporations play their own language games. Language game theory (Wittgenstein, 1999) is based upon Wittgenstein’s assumption that “words derive their meaning not from the actions or objects that they denote, but from the historical context of discourse, or language game, in which they are used” (Astley & Zammunto, 1992: 444). Language games deliver a platform for the optimized processing of routine communication and routine problem-solving within a specific context. However, such a language game does not transcend the routine for which it has been established.

Corporations operate in ambivalent contexts in which values collide, contradictory interpretations exist, and problems, roles and responsibilities are not clear (Weick, 1995). In such contexts, corporations with a “greater variety of beliefs” can develop better interpretations of conflicts and thus come to better solutions (Weick, 1995: 87). Following the Ferraro et al. (2005: 16) thesis that “how we talk about behavior influences that behavior” one can argue that the richness of corporate language games strongly influences corporate reactions to moral demands or value conflicts in stakeholder networks. This claim is in line with Ghoshal and Moran’s (1996) example that the application of transaction cost theory in managerial practice with its distrust in human nature might become a self-fulfilling prophecy. Organizations “make sense of things by seeing a world on which they already imposed what they believe” (Weick, 1995: 15). What are the lenses through which corporations see and interpret the world? Ashforth and Gibbs (1999) found three routinized language games: Corporations mainly follow an economic, legal or scientific logic in their communication.

If a manager who is trained to perceive the world through these three lenses is confronted with an ethical problem, she/he will either not see it or try to press it through one of these filters. A coffee roasting company’s spokesperson was recently asked about his corporation’s position in the discussion on starving coffee farmers. Coffee farmers often die because the money they receive from the coffee roasters is less than they need for buying new seeds. This does not even include the cost of feeding their families. The spokesperson’s answer was “we leave the solution of the problem to the market”. In economic terms that answer makes sense: When coffee farmers die, the number of coffee farmers is reduced, the quantity of coffee on the market is reduced, the price goes up and the surviving coffee farmers earn more money. But obviously, from an ethical point of view something is wrong with that calculation. A moral question was asked and an economic answer given. Many corporations show a comparable reaction when confronted with moral critique: Wal Mart is under pressure because they build one of

their large shops on the site of one of the most important Mexican pyramids. Their argument: We create jobs and our products are cheaper. As Oestreich observed, where managers see “the end of an old inefficient industry” external critics might see “families uprooted and lives destroyed” (Oestreich, 2002: 215). The same one-dimensional world perception has been described as resulting from the application of a scientific language game: Heyvaert (1999: 140) argues that the environmental risk assessment of corporations “takes into account only technical scientific considerations, not people’s values and perceptions”.

Mintzberg (2004) has recently criticized that the narrow world perception of today’s manager is partly based on severe flaws in management education: Managers learn that decision-making is basically the art of analyzing phenomena by using mathematical methods – and the result is quite obvious: “Give a little boy a hammer and everything looks like a nail. MBA programs have given their graduates so many hammers that many organizations now look like smashed-up beds of nails” (Mintzberg, 2004). Business schools train the wrong people (too analytical) at the wrong time (too unexperienced) in the wrong way (with a focus on mathematical analysis) with the wrong consequences (fixation on maximizing shareholder value) (Mowday, 2004, AME). Law students and engineers probably go through a comparably one-dimensional educational programme. The resulting mental programmes are reinforced in the corporate context (Weick, 1995) and eventually managers unlearn to see the ethical dimension of their activities.

## Psychological Contract Violation

Beyond the simple lack of moral imagination, there is a second major driver for the unethical behavior of average people: Under certain conditions, actors might have the conviction that it is their moral right to act against certain rules of conduct. When starting to work for an organization, employees have beliefs about the reciprocal obligations between them and the organization. If they have the impression that these mutual obligations have been violated by the corporation, their job satisfaction decreases and the perceived obligations towards the organization decrease. Frustration might then lead to immoral and illegal behavior such as employee theft or sabotage (Morrison & Robinson, 1997). These reactions to contract violations are also reactions to a perception that they are being mistreated. Employees observe the balance between giving and taking according to two justice criteria (Morrison & Robinson, 1997): They examine the fairness of outcomes (e.g. “It is unfair to fire me and not Mr. Miller”) and the fairness of procedures (e.g. “It is unfair to fire me via SMS”). As Greenberg showed in several experiments, “employees are inclined to steal company property when they feel underpaid for the work they do” (Greenberg, 2002: 985). Perceived unfairness is “compensated for” by (often immoral) counteractions. However, Greenberg’s research clearly shows that the probability that these dubious reactions to perceived unfairness will occur is higher on lower levels of moral development. “Employees at the

preconventional level will engage in more theft from their employers than employees at the conventional level” (Greenberg, 2002: 988). Furthermore the situational and organizational factors within the workplace context further moderate the effect (Peterson, 2002).

## Characteristics of the Context

### Leadership

Leadership has been argued to be a key driver for corporate ethics (Carlson & Perrewe, 1995; Paine, 1996; Weaver et al, 1999; Parry & Proctor-Thomson, 2002). Trevino et al. (2003) claimed that a corporation’s ethical tone is set by the top management, while Ramus (2001) argued that supervisory support is essential for CSR engagement and Parker suggested that it is a key aspect of a corporation’s engagement in self-regulation (Parker, 2002: 99). Employees imitate their superiors. Therefore, it is not the communicated values but the values which can be observed by their behavior that primarily shape the ethical climate of the organization. As Ciulla argued, “leadership is not a person or a position. It is a complex moral relationship between people, based on trust, obligation, commitment, emotion, and a shared vision of the good. [...] Ethics lie at the heart of all human relationships and hence at the heart of the relationship between leaders and followers” (Ciulla, 2004: XV).

Three main forms of leadership – transformational (also called charismatic), instrumental, and transactional (Antonakis & House, 2002) have been differentiated. Building on Mayer, Davis and Schoorman’s (1995) model of organizational trust, I assume that good leadership can manifest in all three forms of leadership, contributing additional aspects of ethical performance: integrity, benevolence, and ability. Integrity refers to whether a leader fulfills transactional obligations (Antonakis & Atwater, 2002), with consistency in promise keeping, acknowledgement of pluralistic positions, fair negotiation, and in the exercise of free choices (Bass & Steidlmeier, 1999). Benevolence corresponds to a leader’s transformational abilities that are based explicitly on values, fostering an ‘awareness of moral and ethical implications to transcend self-interest for that of the greater good’ among followers (Antonakis & House, 2002: 7). Ability refers to instrumental leadership, with a leader excelling in strategic/task-oriented functions of a leader, with specific ability to manage ethical or CSR challenges in given situations. While ethical or unethical transactional leadership deals with the minimum and taken-for-granted base of ethics, namely transactional fairness, it can even be described as “ethically neutral” (Trevino et al., 2000: 130). In contrast, transformational/charismatic leadership reaches for followers’ core of self-understanding and identity – their values – it can be regarded as the most influential form of leadership in terms of ethics. Transformational leadership might transform followers in good and bad directions, as Howell and Avolio have argued:

**Table 1.** Individual qualities of ethical and unethical transformational leaders (Howell & Avolio, 1992: 45)

<b>Unethical charismatic leader</b>	<b>Ethical charismatic leader</b>
Uses power only for personal gain or impact	Uses power to serve others
Promotes own personal vision	Aligns vision with followers' needs and aspirations
Censures critical or opposing views	Considers and learns from criticism
Demands own decisions be accepted without question	Stimulates followers to think independently and to question the leader's view
One-way communication	Open, two-way communication
Insensitive to followers' needs	Coaches, develops, and supports followers; shares recognition with others
Relies on convenient external moral standards to satisfy self-interests	Relies on internal moral standards to satisfy organizational and societal interests

Leaders and their values form the ethical climate of an organization and thus indirectly contribute to the ethical or unethical performance of the organization beyond their own good and bad deeds.

### Organizational Climate

The ethical climate of an organization has been defined as the set of “shared perceptions of what is ethically correct behavior and how ethical issues should be handled in the organization” (Peterson, 2002: 50). Enron has for instance been described as an organization with an ethical climate that provoked and promoted unethical behavior. “Making deals” regardless of the methods being used was regarded as the main criterion for success and breaking the rules and pushing the limits in a widely unregulated market and a new economy atmosphere throughout the late 1990s became key values within the organization (Sims & Brinkmann, 2003). Shared understandings of what is right and wrong, allowed and forbidden, desirable or undesirable set the normative context in which members of an organization interact. Through interaction, these convictions are reinforced or transformed. They tend to homogenize behavior within the organization and transmit a certain reputation to the outside world about the expectable behavior of organizational members (Dickson et al. 2001). The ethical climate of an organization is stabilized over time by corporate stories that illustrate how the organization applies

its values and norms. A good illustration of such a story is that of a former Arthur Andersen CEO. This is one of the stories that contributed to the serious and solid reputation of the former Arthur Andersen. It is about an internal memo which the CEO Spacek sent his employees: “It is exceedingly embarrassing to find men with their feet on desks or chairs, leaning back in chairs, reading newspapers, or two or three in an office laughing and apparently gossiping or otherwise not appearing to be occupied. Everyone should make it a habit to be busy all the time. When walking in the halls, walk briskly. Under no circumstances should anyone read a paper in the office. As a matter of fact, newspapers should not even be on the desks” (Ley Toffler, 2003: 46). Arthur Andersen once was regarded as the Marine Corps of the accounting business (Ley Toffler, 2003). The ethical climate that corresponds to such an image was internally and externally passed down by these stories. However, Arthur Andersen is not only an example of how organizations create and live out rules, norms and values. It is also an example of how such a highly reputed climate might be corrupted and how corporations might stumble on an ethical climate becoming corrupted. Ethical climates might be corrupted due to unethical leadership, normative changes in the environment which the organization might not be capable of catching up to or obstacles and inconsistencies created by elements within the organizational structure. In most cases, corrupting the ethical climate is a result of a combination of these factors, as in the case of Arthur Andersen (Ley Toffler, 2003).

## Organizational Structure

The formal structure of a corporation can promote either ethical or unethical behavior. James (2000) for instance argued that there is a direct effect of structural conditions on employee behavior. He distinguishes between three strongly related dimensions of organizational structure:

1. “The structure of monetary and non-monetary rewards.
2. The performance-evaluation, monitoring, and control processes for individuals and business units.
3. The systems of partitioning and assigning decision-making rights and responsibilities to workers, including job design and the level of empowerment” (James, 2000: 45).

Inconsistencies between ethics training programs and structural demands might provoke cynism and disorientation, while inconsistencies between corporate norms and values and structural incentives might even directly trigger the wrong behavior. Such inconsistencies might for instance exist between the communicated “fair relationship with suppliers” and the incentive system for purchasing agents that reward those who attempt to squeeze suppliers. Organizational structures set limits for employee activities and the signals they send might be stronger than those



given by codes of conduct. Again, the Enron case clearly demonstrates how monetary incentives and performance-evaluation methods motivate employees to completely ignore the official corporate values (in the Enron case: respect, communication, excellence, integrity) and to subvert even their own values. Corporate pressure to make the numbers, contributes to an increased readiness to constantly move on and even cross the thin line between ethical and unethical behavior (James, 2000). The level of empowerment as the third key aspect of organizational structure has been widely examined for its impact on decision-making. If employees feel that someone else is in charge of making decisions or assuming responsibilities, they do not act or even ignore deviant behavior. Trevino has described this aspect as the locus of control. People with an internal locus of control have the impression that outcomes result from their efforts while people with an external locus of control regard events as being beyond their control. She concludes that “managers whose locus of control is internal will exhibit more consistency between moral judgment and moral action than managers whose locus of control is external” (Trevino, 1996: 610).

## Societal Environment

It can be assumed that the societal context in which a corporation operates might influence the ethical quality of its behavior. A weak governance context can be regarded as a key driver for illegal and unethical behavior. In weak governance contexts, corporations are sometimes involved in violating employee human rights, murder of union representatives, money laundering, manipulation of financial statements, pollution, corruption or illegally dumping toxic waste in third world countries.

The absence of legal rules or the weakness of a third party enforcer (hard law) as well as the absence of shared norms (soft law) can be mainly found in three different contexts: deregulated markets (Levine, 2005), unregulated markets in transformation economies (Rawlinson, 2002; Rossouw, 1998) and on global markets that are not embedded in stable political institutions (Seidman, 2003). In all three cases, corporations navigate in a governance vacuum that offers considerable incentives for morally opportunistic and legally deviant behavior. In the absence of both forms of regulation, the profit motive might get out of control and create uncivilized forms of capitalism and capitalist actors. Rampant problems with corporate crime in some transition economies provide some evidence for these problems. Rossouw (1998) pointed to the fact that white collar crime more than doubled in the first year of transition from the South African Apartheid regime to the democratically formed government. In Russia, the post-communist era was dominated by an uncontrolled “gangster capitalism” (Rawlinson 2002, 301). “Unethical business practices can transform these young political democracies and market economies of newly formed democracies into kleptocracies” (Rossouw, 1998, 1564). In Russia as well as in South Africa the new market economies over-

emphasized the idea of self-interest as the main driving force for business transactions (Rawlinson, 2002; Rossouw, 1998) and both transition economies were dominated by a legally and morally undamped interpretation of the profit motive. The lack of legitimacy common to new forms of economy often result from the broadly shared idea that liberal market economies and newly emerging forms of Robber Baronism are the same or at least strongly linked phenomena – uncivilized business practices as the unavoidable precondition for free markets (Rossouw, 1998). The self-centred behavior of the corporate actors is not balanced by broader responsibilities: “There seems to be a lack of commitment to curb unethical behavior that might harm the new society” (Rossouw, 1998, 1567).

## Network Effects

It has been argued that beyond the dichotomic view of individual or organizational and societal aspects behind ethical decision-making there is “an important additional consideration: relationships among actors” (Brass, Butterfield & Skaggs, 1998, 14). Interacting with individual, organizational and societal aspects, interpersonal relationships influence the behavior of actors within organizations. Brass et al (1998) examined how different types and structures of relationships lead to network effects and how these effects influence organizational integrity. Four of their assumptions should be advanced to illustrate the impact of network effects on organizational ethics: the strength of ties, the status of an actor in a network, the impact of structural holes and the network centrality of an actor.

The starting point of their reflections upon network effects is Granovetter’s idea of relationship strength. Granovetter (1973) argued that the dynamic between actors partly depends on whether they are linked by strong ties or by weak ties (e.g. along emotional, normative, frequency lines). Brass et al (1998) conclude that strong relationships between organizational actors might outweigh the impact of personal and contextual aspects of organizational integrity. In a network of *strong ties*, an individual might for instance act against his or her convictions. Whistleblowing is often the result of highly ethical actors in an unethical context who have the courage to resist “the normal” behavior and who run tremendous risks for their own careers in order to stand up for ethical convictions. However, since potential whistleblowers know the risks of making bad corporate practices public, most of them might never blow the whistle but remain silent or even adopt a behavior they deem wrong. Brass et al. further suppose that individual *status* influences ethical behavior: The risk of being treated unethically is higher for low status actors but the probability that low status actors will behave unethically is lower because they might fear organizational backlashes. The importance of leadership for organizational integrity illustrates the role of status: Wherever top managers are led by values, the risk of deviant behavior among lower status employees is reduced. *Structural holes* refers to the consequences of the lack of interconnect-edness between different actors: If actor A has a relationship with both B and C,

while B and C are not connected, the opportunity for A to act unethically increases. If B is the customer and C is a worker in the supply chain, A might violate the human rights of C without any impact on B's consumption decision. If the gap is filled, e.g. by NGO activists who make the unethical behavior of A public, B might start to boycott A's products. *Centrality*, corresponds to an actor's position within a network. It refers to "the extent to which an individual can reach all others in the network in the fewest number of direct and indirect links" (Brass et al. 1988, p. 21). Central actors' unethical behavior is linked to high reputational risks while isolated actors in contrast have nothing to loose in terms of reputation.

As Brass et al. argue, network effects do not replace the individual or contextual perspective but in combination with these prevailing driving forces might deliver a more holistic view of organizational integrity. Ethical or unethical behavior then is much more than a function of bad apples or bad barrels and might include a thorough analysis of the "relationships among the apples as well" (Brass et al. 1988, p. 28).

## Managing Organizational Ethics

Analyzing actor, context and relationship based determinants of organizational integrity contributes to a better understanding of ethical and unethical behavior in corporations. It furthermore delivers a solid knowledge base for the *management* of organizational integrity. In the last paragraph of the paper I will shortly elaborate on some implications for the managerial practice of organizational integrity. Why and how do corporations manage ethics?

More and more corporations regard ethics as a management issue and have already started to systematically deal with ethical and legal compliance. A firm's motivation for these activities can be attributed to several sources that constitute two distinct types: compliance and integrity (Paine, 1994; Waddock, 2005; Weaver et al., 1999). Compliance includes fear of legal sanctions (Parker, 2002), the hope of reputation gain (Porter & Kramer, 2002) and increased profitability (Waldman & Siegel, 2005). Especially companies with a US-background often implement ethics in the form of a legal compliance program. This can be explained by the legal context in which these firms operate. There are strong positive and negative incentives for corporations to comply with the US Federal Sentencing Guidelines or the Sarbanes Oxley Act. Having a sophisticated ethics management program in place might protect from punishment or at least substantially reduce fines that have to be paid in case of disclosed deviant behavior (Paine, 1994). Weaver et al., (1999) have characterized the compliance driven business ethics mindset to be coercion and control oriented. It is seen as inherently calculative, operating within a cost/benefit framework (Waldman & Siegel, 2005), and has been criticized for limited effectiveness and ethical shallowness (Paine, 1994). Compliance might simply constitute "the outcome of an

equation: the benefits of non-compliance versus the probability of being discovered and punished, and the severity of the penalty” (Parker, 2002: 67). Logsdon and Wood (2002) have illustrated the potential negative effects of a compliance mindset in their discussion of multinational corporations. A merely legal interpretation of ethics and responsibility often leads to systematic exploitation of the existing legal vacuum on the global playing field, prompting even immoral or illegal behaviors if the perceived risk is low.

Paine (1994) pointed to the limits of a merely law and control-driven ethics program (compliance) and proposed a value-based approach that rather builds upon creating and fostering a moral climate of shared values (integrity). Organizational ethics that operates with an integrity mindset is not motivated by one or more of the mentioned external sources for compliance but instead builds upon the values of the corporations and its leaders and/or owners. It is inspired by a broader vision of managerial responsibility (Lerner & Fryxell, 1994; Werre, 2003). Swanson (1999: 506) argued that the link between business and society ought to be “inherently normative, because it seeks to explain what corporations should do or should not do on behalf of the social good”. Likewise, Paine (1994) has claimed the integrity approach to a firm’s thinking about business ethics and corporate responsibility to be deeper and broader than that guided by compliance: broader because it builds on ethical principles and deeper on account of its power to influence decision making. Her assumption is that intrinsically motivated employees might show a more stable and calculable behavior than those employees who are trained to follow legal demands and who feel threatened by sanctions. Explicit incentives or sanctions can even lead to an erosion of the moral climate, e.g. by reducing the level of mutual trust (Frey, 1997). Distrust towards employees that is displayed in sophisticated control and monitoring mechanisms can become self-fulfilling and provoke the very behavior that mechanisms seek to prevent (Ghoshal and Moran, 1996). Instead, integrity programs are strongly linked to the example and commitment of top management (Weaver, et al., 1999). Integrity does not replace compliance but strengthens its effects. “Case-based research and theoretical research have suggested that value-oriented programs or combined values and compliance programs should be more effective” (Weaver et al., 1999: 55).

Indeed, the successful management of organizational ethics depends on a suitable balance between the empowerment of the individual actors, the design of a context that promotes ethical behavior and the institutionalization of control systems. The bigger the barrel, the higher the probability of finding some bad apples in it which are immune against ethical trainings or ethical incentives. They have to be kept in check. At the same time, treating all apples as bad or at least potentially bad apples would represent a profound misunderstanding of human nature. Therefore, managing organizational ethics means walking the fine thin line between control and trust.

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# Enron – Pride Comes Before the Fall<sup>1</sup>

*Alejo Sison*

At first it seemed as if Enron was just too big, just too important and just too valuable to fail (Walker 2002). It ranked seventh among the world's largest corporations in the Fortune 500 list, and for six consecutive years since the mid-1990s, it was voted "America's Most Innovative Company". During that period, Enron reported an almost eight-fold increase in sales from \$13.3 billion to \$100.8 billion, with a market capitalization of \$63 billion. Its financial statement in 2000 reported a record-setting net income of \$1.3 billion, with recurring earnings per share up by 25 per cent, and a total return to shareholders of nearly 89 per cent. Even as late as 2001, Enron's board of directors was named the third best board in the US by Chief Executive magazine. Yet on 3 December 2001, the unbelievable became inevitable and Enron became the largest corporation ever to file for bankruptcy in American history (Oppel & Sorkin 2001). Enron and its affiliates sought Chapter 11 court protection for assets worth \$49.8 billion and debts of \$31.2 billion. The air was heavy with accusations of accounting fraud, insider trading and other securities law violations.

Until its untimely demise, Enron was the epitome of a new-economy company, a thinkingoutside-the-box, paradigm-shifting, market-making firm (Keller 2002). Founded in 1983, Enron got its big break when state-regulated monopolies in the production, distribution and sale of natural gas and electricity in the US were broken up, and a trading platform became necessary. According to Paul R. Kleindorfer, public policy professor at the Wharton Business School, "In the early 1990s the company [Enron] single-handedly produced the backbone infrastructure that has led to a whole industry of broker intermediation." (Knowledge at Wharton 2001). Enron transformed energy supplies into financial instruments or "derivatives" that could be traded online like stocks and bonds. Thanks to Enron's intervention, the market could be guaranteed a steady supply of energy at a predictable price. However, instead of sticking to its core competence as an energy broker, Enron figured that it could expand into buying and selling everything else, such as newsprint, television advertising time, insurance risk, high speed data transmission, etc. in the new virtual marketplace. Enron poured billions into these trading ven-

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tures, and as could be expected, some of them precipitously failed. Although the company was excellent in inventing businesses, it turned out to be terrible in managing them, judging by its appalling internal audit practices. So far, hardly any wrongdoing, except perhaps for some erroneous business judgments for which one could always give the benefit of the doubt.

But instead of coming out in the open and declaring its losses in public – something that could have readily stripped the firm of its mystique, not to mention the havoc such an action would have wrought on stock price – Enron chose a less than honest solution. It set up thousands of partnerships that allowed it to hide its losses – thereby avoiding credit rating downgrades – and to generate fictitious revenues. By the time those debts and losses were properly recorded on Enron's books in October 2001, they meant a reduction of about \$1.2 billion in shareholder equity, a large chunk of which was in employees' 401(k) plans. Furthermore, the corrected financial statements also wiped out close to \$600 million in net income between 1997 and 2000. That triggered the beginning of Enron's downward spiral.

The chief architect and strategist of such partnerships was Andrew S. Fastow, Enron's senior vice president of finance since 1990 and, beginning 1998, its chief financial officer until his ouster in October 2001 (Barboza & Schwartz 2002). Securities and accounting regulations allowed debts accumulated by a subsidiary to be kept off a parent company's records as long as the parent did not own more than 50 per cent of the subsidiary. Exploiting this loophole, Fastow created a myriad of such unconsolidated entities. In principle, there was nothing wrong with the constitution of these subsidiaries. They reflected a common financing technique consisting of decreasing a company's risk by moving its holdings into separate entities which in turn could be sold to outside investors. Cactus, the first one created way back in 1991, was so successful that Calpers, the California Public Employees' Retirement System, even approached Enron to form a joint venture called Jedi, or Joint Energy Development Investment, in 1993. Later on, however, Fastow seemed to have abused these accounting provisions and created partnerships that served no other purpose than to shuffle accounts and keep debts and losses off the balance sheet. It was not clear to what extent Enron directors were aware of these initiatives and had authorized them.

Certainly there were instances of conflicts of interest, for Fastow and some other Enron executives served as managing partners – if not ultimately controlled – many of these supposedly independent subsidiaries. In recompense for his efforts in the LJM Cayman and LJM Co-Investment partnerships, for example, Fastow was able to pocket at least \$30 million; while in the Southampton Place partnership he held with other Enron employees, an initial investment of \$25,000 netted him \$4.5 million after only two months (Eichenwald 2002). Besides a hefty salary, Fastow also earned around \$23 million in 1999 and 2000 from the sale of Enron stock options. So much for a man honored by CFO magazine in 1999 for having invented a groundbreaking financing structure and praised by Jeffrey K. Skilling, then Enron president and CEO, in the following words: "We needed someone to rethink the entire financing structure at Enron from soup to nuts. We didn't

want someone stuck in the past, since the industry of yesterday is no longer. Andy has the intelligence and the youthful exuberance to think in new ways. He deserves every accolade tossed his way.”

No one could ever doubt Fastow’s financial wizardry and, up to a point, this served Enron well. But only up to a point because soon enough, Fastow used his skills to mislead the public about Enron’s finances. He also neglected his fiduciary duties toward the company’s investors, dedicating himself to deals resulting in self-enrichment through those complicated partnerships instead of maximizing investor returns.

On 14 August 2001, a mere six months after his appointment as Enron CEO, Jeffrey K. Skilling announced his sudden resignation for personal reasons. On that occasion he made the following remarks: “We built a company that 10 years from now, 20 years from now, is going to be factor to be reckoned with in the energy business” (Zellner 2001). Three and a half months later, Enron’s bankruptcy filing proved this once lauded visionary CEO dead wrong. Was it possible that even up to the moment of his resignation he did not have the slightest inkling of what was going on?

Skilling first came in contact with Enron in the late 1980s as a McKinsey consultant (Schwartz 2002). In 1990, he jumped ship from the consultancy and began to take charge of Enron’s nascent trading operations. By 1996, he had risen to the post of COO, and in February, 2001, as the chairman Kenneth L. Lay’s protégé, he was named CEO. As a hands-on, down-to-the-details manager, Skilling was perceived to be complementary to Lay’s more detached, more congenial and highly political leadership style. Some co-workers called Skilling Darth Vader, a moniker that he didn’t mind, and even seemed proud of. However, other executives thought that for the lack of scruples he was more comparable with Machiavelli than with the Star Wars villain. Apparently, in a meeting of corporate vice presidents in 2000, Skilling had singled out a certain Louise Kitchen for praise. Ms. Kitchen’s merit consisted in starting out the company’s Internet trading operation, Enron Online, despite Skilling’s repeated refusals to allow her. Kitchen stealthily used funds allocated for other purposes and set up the network just the same. The moral of the story then, as a senior manager put it, was that one could break the rules, cheat or lie, but as long as he made money – at least in Enron, with Skilling – this mode of conduct was perfectly alright. Between 1999 and 2000, Skilling earned \$10.3 million in salary and bonuses, and a few months before Enron’s collapse, during the blackout period that prevented employees from trading their holdings, he cashed in the equivalent of around \$30.6 million in stock options (Oppel 2001).

Unlike many former Enron colleagues, Skilling did not invoke his Fifth Amendment rights against self-incrimination when called upon by Congress to testify in February 2002 (Labaton and Oppel 2002c). At issue was his knowledge and oversight of the partnerships and the transactions carried out by Fastow. Skilling admitted that the structure of the initial Fastow partnerships were approved by the board. The board then appointed members of top management – the chief ac-

counting officer, Richard A. Causey, the chief risk officer, Richard B. Buy, the CEO (Skilling himself) and the Chairman (Lay) – to closely monitor the transactions of these partnerships.

As early as March 2000, Jeffrey McMahon, then Enron's treasurer and a subordinate of Fastow, supposedly warned Skilling of conflicts of interest and self-dealing in one of the partnerships. This resulted in a confrontation between Fastow and McMahon, and the latter's replacement by a Fastow chum and co-investor in one of the partnerships, Ben F. Glisan. Skilling acknowledged having met McMahon in March 2000, but he said that the topic of conversation was simply whether McMahon's compensation would be affected by his tense relations with Fastow and nothing more. Two Enron directors, Robert K. Jaedicke and Herbert S. Winokur, Jr., claimed that in a board meeting in October, 2000, Fastow affirmed that Skilling had reviewed and approved the subsequent partnership deals. The minutes of the meeting confirm Jaedicke's and Winokur's account. Skilling said that he had no such recollection and that he was probably distracted because during that meeting, the lights had gone out. Lastly, on 22 May 2001, a senior Enron lawyer, Jordan Mintz, supposedly sent a memo to Skilling expressing his concern about some unsigned approval sheets pertaining to the transactions of the Fastow partnerships for the year 2000. Mintz offered to send the approval sheets to Skilling for signature but he got no response whatsoever.

Therefore, in the face of contradictory testimonies and despite his reputation as a micromanager, all that Skilling could summon in his defense before the Congress committee was that Enron was a very large corporation and that it was impossible – even for a CEO like himself – to know everything that was happening.

What about Kenneth L. Lay, Enron's Chairman and since Skilling's resignation in August, 2001, its CEO as well? What did he know about the Fastow partnerships and the state of the company's finances? On 14 August 2001, immediately after Skilling's departure, Lay sent the following message to all Enron employees: "I want to assure you that I have never felt better about the prospects for the company" (Herbert 2002). And almost two weeks later, on 27 August, came this follow-up e-mail, "One of my highest priorities is to restore investor confidence in Enron. This should result in a significantly higher stock price."

At around this time, however, Lay had already received an explicit warning through an unsigned letter that was later on traced to Sherron S. Watkins, a vice president of corporate development at Enron (Van Natta and Berenson 2002). Watkins began her letter by saying, "Has Enron become a risky place to work? For those of use who didn't get rich over the last few years, can we afford to stay?" She then continued expressing her anguish over the dubious accounting practices of which members of senior management were aware but didn't seem interested in stopping. She concretely referred to one of the Fastow partnerships, "we booked the Condor deals in 1999 and 2000, we enjoyed a wonderfully high stock price, many executives sold stock, we then try to reverse or fix the deals in 2001 and it's a bit like robbing the bank in one year and trying to pay back two years later." All that Lay did in reaction was to forward the letter to the Vinson &

Elkins law firm. The lawyers limited themselves to examining whether the letter offered new information, without looking into the veracity of the claims, and a few months later they concluded that Enron had committed no wrongdoing and gave it a clean slate.

While the e-mails and the warnings transpired, and well before the definitive collapse of Enron stock, Lay had already sold around \$40 million worth of shares – at a profit of about \$21 million – during the first half of 2001 (Herbert 2002, Norris 2002). This figure nevertheless paled in comparison with his previous earnings of \$131.7 million in 2000, \$49 million in 1999, and more than \$300 million cumulatively since 1989.

Not until November 2001, did Lay publicly admit that all was not well with Enron, “Enron became overleveraged” (The New York Times 2001). Lay said that he basically understood what was going on, but that he left crucial details to others who have since departed and as a result, he no longer fully grasped the reality of Enron. On 23 January 2002, Lay announced his resignation as chairman and CEO, although he clarified that he would remain on the board (Yardley and Schwartz 2002). Scarcely a couple of weeks later, on 10 February 2002, Lay decided that he would exercise his right against self-incrimination and refused to testify before Congress (Oppel 2002c). He may have been influenced in his decision by a special committee report released on 2 February 2002 alleging that Lay had failed to properly oversee Enron and that he bore significant responsibility for the deals that brought the company down.

Thus far the story of Kenneth L. Lay, a man who had dedicated at least the last three decades of his life to championing the cause of energy deregulation, while accumulating vast amounts of political influence (Yardley 2002). His friendly nature and polite, engaging manners were definitely a big help. In the mid 1990s, he even came to be known as Mr. Houston, for the enormous amount of money he had spread all over the city, including the local football and baseball stadium which came to be called Enron field. But by far his most rewarding investments were those made on “reputational capital”, especially among politicians. Way back in 1994, Lay and Enron donated nearly \$575,000 to George W. Bush’s political race to the Texas Governorship; and for the Bush campaign for presidency in 2000, another \$100,000 was raised, aside from an additional \$300,000 for the inauguration ceremonies (Eichenwald and Henriques 2002). Around two-thirds of the incumbent members of Congress could also be counted as beneficiaries of Enron’s and Lay’s financial largesse. Cultivating a high-profile public image and dispensing financial favors among the members of the political class were the wings that propelled this modern day Icarus to undreamt of heights. But flying high and getting close to the sun were one and the same thing and, due to an excess of hubris, in the end Lay got singed.

How about the auditors, the accountants from Arthur Andersen? Were they, like Nero, just fiddling away while their client Enron burned to ashes? Well, almost.

The last five years have proven to be specially tumultuous for Arthur Andersen, one of the Big Five auditing firms. Apart from its acrimonious divorce from its consulting arm, now known as Accenture, it has also been involved in a series of prominent and very costly scandals (Weber et al. 2001). In 1996, the SEC ruled that Andersen had engaged in improper professional conduct and that its reports on the firm Waste Management were materially false, having overstated income by more than \$1 billion from 1992 to 1996. Without either admitting or denying responsibility, Andersen accepted an antifraud injunction, shelling out \$7 million as civil penalty and agreeing to pay part of a \$220 million class action settlement as well. Once more, in 1997, the SEC accused Andersen of having certified statements containing false sales and profits on behalf of the Sunbeam company. True to form, without admitting or denying any wrongdoing, Andersen this time disbursed \$110 million to settle shareholder litigation. Then came Enron.

Aside from potentially crippling financial damages, Andersen faced a formidable challenge to its already tarnished reputation. Joseph F. Berardino, Andersen's CEO, acknowledged in an interview, "The integrity of this firm is in question... Our reputation is our most important asset" (Oppel and Eichenwald 2002). During Congressional hearings, Berardino was careful to portray Andersen's role as that of an auditor that stuck by the rules but was unfortunately lied to, thereby pinning the blame on its client, Enron, in first place, and possibly, to regulators as well, since they had set accounting standards that later on proved too lax. Never mind if Enron happened to be Andersen's second biggest client in 2000, from which it received combined auditing and consultancy revenues of more than \$50 million.

This might have been a plausible defense of Andersen's innocence. However, since August, 2001, its chief auditor for Enron, David B. Duncan had already been advised about possible illegal transactions by Sherron Watkins, the same executive who had sent a letter to Enron chairman Lay (Oppel 2002a). Apparently, even in February of that same year, some Andersen officials had already discussed dropping Enron from its list of clients, due to concerns about dodgy accounting practices. Nevertheless, Andersen just decided to look the other way and carry on with Enron's account, giving the company its seal of approval.

Meanwhile, once Enron figures were restated in the third quarter of 2001 and the SEC inquiries commenced, Andersen auditor Duncan, with the knowledge of in-house legal counsel Nancy Temple, entered into a frenzy of computer file purging and document shredding (Oppel 2002b). A parallel operation transpired within Enron itself (Glater and Brick 2002). The destruction of what was potentially incriminating evidence did not stop until further notice was given by Andersen lawyer, Temple, in November 2001. On 15 January 2002, Duncan was fired from Andersen, together with four other partners who had worked on the Enron audits (Oppel and Eichenwald 2002). Finally, on 24 January 2002, after having admitted participation in the destruction of records, Duncan sought refuge in the Fifth Amendment and declined to respond to questions fielded by the members of Congress (Oppel and Labaton 2002).

At this point, no one knows for sure when and to what extent Andersen CEO Berardino became aware of the destruction of Enron audit documents by Duncan. In any case, if the auditing firm did not have anything to hide, and all its transactions with Enron were above board, why the rush to get rid of records?

What did fellows such as Fastow, Skilling, Lay and Duncan have in common? We could say that amongst them, they undoubtedly held tons of human and intellectual capital. They were all educated in the country's premier business schools, had received excellent professional training, and each one was an over-achiever and a star performer in his own right. They also enjoyed huge endowments of social capital, in terms of networks of influence and amount of public trust. Mainly for these reasons, they had always been held to a higher standard, because they were thought to be beyond suspicion – initially, at least – by their investors and employees, the regulators, government and society at large. But all of these assets which at first powered their rocket-like ascent, in the end, were squandered and turned mercilessly against them. They lacked nothing but honesty, the bias of putting the interests of the people whom they were supposed to serve before their own, diligence in the performance of their oversight duties, and trustworthiness. In short, they lacked moral capital.

As we have seen, social capital builds up on the gains or merits of human capital, intellectual capital and cultural capital, like a nest of tables or a collection of Russian dolls. But insofar as social capital could sometimes lead to disastrous consequences, there must be something else beyond trust that is the true source of value among persons working in a corporation. This seems to be the role that moral capital is meant to play.

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# Andersen. No Fairy Tale Ending<sup>1</sup>

*Alejo Sison*

The Arthur Andersen auditing firm was founded in 1913 by an accounting professor of the same name. After Mr. Andersen's death in 1947, the firm found itself on the verge of collapse. But in the end it was saved thanks to the efforts of Leonard Spacek, who convinced partners to remain together despite looming uncertainty. Spacek, who was Andersen's chief executive from 1947 to 1963, had the reputation of being the "conscience" of the auditing profession (Norris 2002a). He was among the first to warn that the auditing profession's very existence could be put in danger if it did not show sufficient independence from clients. He also complained whenever the US Accounting Principles Board yielded too quickly to pressure from companies which thought that auditing rules would significantly reduce profits. Spacek always insisted that Andersen provide above all high-quality accounting, in accordance with its corporate motto, "Think straight. Talk straight".

In 1965, with Spacek already retired, the US Accounting Principles Board delayed action on the treatment of deferred taxes on installment sales, for fear of offending retailers. Andersen took the initiative of bringing the matter to the attention of the Securities and Exchange Commission (SEC), and moved to have a tough rule adopted. In the late 1970s, Andersen once more spearheaded reforms in accounting for pensions, despite their being unpopular among companies which feared negative effects on profit margins.

Since then, however, Andersen's reputation had gone downhill. First was its bitter and distracting corporate divorce from Andersen Consulting – later re-branded as Accenture – between 1997 and mid-2000 (The Economist 2001). Although an arbitrator granted Andersen custody of the brand name, it was only awarded \$1 billion in damages, far short of the \$15 billion it had demanded. Furthermore, because of the break-up, Andersen slipped from the top to the bottom of the ranking among the Big Five global accounting firms. In 2001, Andersen reported revenues of \$9.3 billion, less than half of those earned by PriceWaterhouseCoopers, which occupied the first place.

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During the late 1990s, Andersen found itself desperately embroiled in some very costly auditing scandals. In the Waste Management and Sunbeam cases, it had to disburse close to \$120 million in combined penalties and settlements. One of Andersen's own studies revealed that between 1998 and 2000, the number of earnings restatements made by the firm had increased from 158 to 233; that is, a full 47 per cent rise over three years (Coffee 2002). Even then, the quality of Andersen audits was still to reach its nadir.

This was the sorry state of affairs at Andersen when Joseph Berardino took over as CEO in 2001, replacing Jim Wadia (*The Economist* 2001). Compared to his predecessor, who was given to managing through consensus, Berardino generally followed a more direct and straight-talking style. Among his first moves was that of pruning Andersen's management committee from 17 members to five, reinforcing its powers and attributions. Berardino was likewise known – aside from his professional competence – for two other outstanding traits, his trustworthiness and his ability to listen.

When asked about the strengths that differentiated Andersen from other professional service firms, Berardino cited in first place the cohesiveness of its culture – “There is one name over the door. We're not an alphabet soup.” While its rivals struggled with a complicated array of country-specific partnerships, Andersen partners enjoyed the benefits of a unique pay system, with each one receiving a list of what he had earned in the previous year. This transparency or openness – at least, at partner level – together with the emphasis on teambuilding contributed to Andersen's rapid growth in recent years. This was the reward for the 135 hours of formal training that the firm invested on the average per employee each year. The optimism at the beginning of Berardino's tenure at Andersen was such that some partners had even begun to expect an average income growth of 15 per cent a year indefinitely.

Then came Enron. There is no question that some management teams will always overstate their income, or understate their liabilities, or “massage” their earnings reports. Enron was not unique in this sense. The issue was how Andersen, as an independent auditor, failed to detect Enron's shenanigans, not withdrawing its stamp of approval until barely a month before the energy company folded-up. That Andersen provided Enron with both auditing and consultancy services, gaining \$27 million from the former and \$28 million from the latter in 2001, made it too beholden to its client. In relationships like these, where there is so much room for serious conflicts of interests and loyalties, auditors are forced to become extremely friendly with their clients, making a mockery of their so-called “independence”.

How did Andersen react to the Enron imbroglio? After informing the SEC and the Justice Department that Enron-related documents had been disposed of, and after a series of testimonies by some of its key executives, including Joseph Berardino, before the US Congress, Andersen announced the formation of an Independent Oversight Board to steer the firm through the crisis (Andersen 2002a). Paul A. Volcker, the former US Federal Reserve chairman, was appointed head of

the Board. The Board was granted full authority to mandate revisions in Andersen policies and practices, and the means to implement them. More specifically, it was conferred the right to make decisions regarding the dismissal, assignment and retention of key personnel with which Andersen would be obliged to comply.

In a previous appearance before the US Senate Banking Committee, Volcker expressed his desire that accounting firms change their priorities and attitudes, putting greater weight on ethics and the quality of audits (Glater 2001). To achieve this he proposed the introduction of new legislation and new internal procedures. In principle, Volcker could try to change Andersen's structure by tightening its chain of command and opting for greater centralization. For example, he could bring more senior executives to just one location, nudging them to rely less on conference calls and e-mail messages and more on personal contact. Although the Board's initial focus was on Arthur Andersen LLP (Limited Liability Partnership) of the US, the scope of its findings and suggestions could be widened to cover the whole of Andersen Worldwide SC (a Swiss Societe Cooperative). Andersen Worldwide SC was the coordinating body for autonomous member firms – each with its own governance and capital structure – which shared a common brand and philosophy, as well as technologies and practice methods.

Volcker seemed inclined towards the definitive separation of the auditing practice from the management consultancy business. This was in keeping with the Board's belief that the auditing profession required such an allegiance to objectivity and independence, that whatever activity in conflict with these values had to be dispensed with. These values should, henceforth, form an integral part of the new Arthur Andersen culture. However, since 1 January 2002 until the time the Board first communicated its resolutions, a score of publicly traded companies – Delta Air Lines, Merck and FedEx among them – had already defected from Andersen. In the succeeding months, more were to follow in what amounted to a veritable stampede out of Andersen's door.

On 11 March 2001, the same day when the Independent Oversight Board released its preliminary findings, the possible sale of Andersen to Deloitte Touche Tohmatsu, another Big Five accounting firm, was announced (Eichenwald 2002a). Negotiations did not center on the price, unlike in most acquisition talks, but on how Deloitte could avoid assuming Andersen's legal and financial liabilities, particularly those arising from the Enron debacle. One possible solution was for Deloitte to buy all of Andersen's assets, with the exception of its American operations. The US business would then be left as a stand-alone unit while it negotiated Enron-related problems. People close to the deal said that in any case, the Andersen name would most certainly have to disappear if the deal with Deloitte were to push through. At that time, Deloitte occupied the number 2 position behind PriceWaterhouseCoopers, but the purchase of Andersen would almost allow it to catch up. Despite the Independent Oversight Board's efforts to salvage Andersen, the disclosure of the possible sale was interpreted as a sign that the firm was no longer viable as an independent organization (Norris 2002a).

Soon afterwards, separate negotiation teams from other big rivals such as KPMG and Ernst & Young met with Andersen executives to consider their respective takeover options (Eichenwald and Ross Sorkin 2002). KPMG expressed its interest primarily in Andersen's overseas operations, while Ernst & Young soon came to the conclusion that its teaming up with Andersen was going to be particularly problematic. Elsewhere, Andersen affiliates outside of the US were pretty much left on their own. At first, the London practice said that it was not even considering seceding from the global network or merging with rivals, while the Canadian business at once manifested its desire follow whatever course Andersen Worldwide took. On the other hand, operations in Belgium and Poland, for example, had already initiated talks with other auditing firms such as Deloitte and KPMG.

However, it was the US Justice Department with its charge of obstruction of justice for the destruction of Enron-related documents that hit the nail on Andersen's coffin on 15 March 2001 (Eichenwald 2002c). It was the first ever criminal indictment brought against a major accounting firm in the country. Until then, these firms were almost untouchable, considered as repositories of public trust as they went about the performance of audit functions.

The US Justice Department alleged that beginning 23 October 2001, Andersen partners working for Enron launched a "wholesale destruction of documents" at their Houston, Texas office and that in the following weeks, they also instructed employees in Portland, Oregon, Chicago, Illinois and London, England to do the same. The claim, therefore, was that Andersen as a firm had indulged in a coordinated and pervasive effort to get rid of possibly incriminating evidence on the Enron case.

Indeed there was no question that documentation was discarded, but insofar as Andersen was concerned, all this had occurred before receiving any subpoena from the SEC (Andersen 2002b). Secondly, the disposal was carried out by the members of the Enron audit team on their own initiative, without any evidence that they had consulted with other senior Andersen officials, in Houston, Chicago or elsewhere. Thirdly, the shredding was done according to the firm's usual practice, in broad daylight, with nary an effort to conceal the activity or particular instructions as to what documents to destroy first and the like. Fourthly, the indictment did not specify the nature of the records destroyed, nor did it narrowly claim that these referred to transactions involving Enron's chief financial officer, Andrew Fastow. This was probably because the paper documents and e-mails were of the type that would ordinarily be destroyed after an audit assignment had been completed. Lastly, the government's charges also failed to consider that the vast bulk of Andersen's Enron-related materials were either retained or had been retrieved thanks to computer backup systems.

Concretely, around 1500 boxes of desk files (containing approximately 3 million sheets of paper), corresponding to 4800 official files and reports plus hundreds of thousands of e-mails had been turned over to authorities upon their request.

On the issue of a purported “firm-wide misconduct”, Andersen offered the following clarifications in its defense (Andersen 2002b). On 23 October 2001, a member of the Enron audit team in Houston sent a voice-mail to a colleague in Portland, Oregon leading to the deletion of Enron-related e-mails by that employee. When this employee forwarded the message to other Andersen executives in Portland involved with Enron, the practice director ordered the members of the team to disregard it. There was no proof that any more documents were destroyed as a result of the request from Houston. During that same week, two Houston partners called a London colleague previously engaged in Enron, telling him to purge his Enron files. But no further evidence was offered by the US Department of Justice as to the nature or amount of the files purged in London, nor as to who were actually involved in the purging. Finally, regarding the destruction of records at Andersen’s Chicago office, it turned out that the initiative did not even originate from anyone in the Houston practice involved with Enron. In late September and early October 2001, Andersen’s Professional Standards Group in Chicago participated in discussions regarding Enron accounting with Nancy Temple, an in-house legal counsel. At that time, she reminded Andersen accountants that under the firm’s document retention policy, superseded drafts of memos should be disposed of promptly. Thus, in compliance with Andersen’s routine policy and upon Temple’s advice, documents were discarded in the Chicago office. But all of this had happened before Andersen’s receipt of the request for information from the SEC on 17 October 2001. For all of the above-mentioned reasons, Andersen decided to plead not guilty to the charge of obstruction of justice (Eichenwald 2002b).

Upon learning of the indictment, Andersen’s potential suitors, Deloitte Touche Tohmatsu and Ernst & Young withdrew their offers, leaving KPMG alone at the negotiating table, albeit with vastly reduced hopes for a salvage deal. Andersen lawyers found the charges to be “a gross abuse of governmental power”, for although some partners and employees undeniably exercised poor judgment, a criminal prosecution against the entire firm “would be both factually and legally baseless” (Eichenwald 2002b). The proceedings against Andersen would destroy the firm, denying thousands of conscientious and reputable employees their source of livelihood, and substantially diminishing the chances for recovery of the company’s claimants.

The \$500,000 fine representing the maximum legal penalty that the indictment carried was the least of Andersen’s worries (Norris 2002b). Rather, it was the corporate “death penalty” which came with the charge that seemed virtually certain. Instead of combating charges, Andersen could choose either to disband – eliminating the government’s ability to prosecute – or declare itself bankrupt – scaring away the remaining clients and making itself an even less attractive target to potential acquirers – (Glater and Brick 2002). Clearly there was no easy way out of the dilemma for Andersen. Even Volcker’s plan to salvage the company by transforming it into an audit only firm was put in serious jeopardy (Andersen 2002 Mar 22). That line of action would require – aside from the government’s dropping its criminal case – the commitment of a critical mass of partners to stay, as well as

the settlement of a welter of Enron-related SEC proceedings and civil lawsuits. Andersen had already offered \$750 million for this purpose, but it had been rejected by Enron investors (Glater 2002c).

Meanwhile, there was a very strong contrast between the reactions of some Andersen employees and clients who stood by the firm, on the one hand, (Schwartz 2002a), and those of a certain group of former partners who even sued the firm to protect their retirement benefits, on the other (The New York Times 2002).

In an incredible display of loyalty, the members of a certain Andersen audit team, after having been dismissed by Merck & Co., began looking for their next opportunity within the firm instead of participating in a massive exodus (Schwartz 2002b). They formed part of the majority of the 85,000 workers who, in defiance or hope, remained steadfast in their dedication to their jobs. In the succeeding weeks, Andersen employees or “androids” (as they were often called derisively within the industry) bought full-page advertisements in major US dailies declaring, “our attorneys are absolutely convinced that no one in this firm committed a crime, and we are confident that our firm will be absolved at trial” (Schwartz 2002c). Rallies were held in support of Andersen in Houston, Philadelphia and Washington. An internal web page was likewise set-up to allow employees to send messages to lawmakers and media professionals.

In the past, Andersen partners were guaranteed to receive hundreds of thousands of dollars each year, a result of which they could retire relatively young, thanks to the returns on the equity they had invested in the firm (Glater 2002a). But after the Enron scandal, should partners decide to withdraw or join other firms, they run the risk of being sued for stripping their collapsing organization of money. A further disincentive was that partners normally received their equity investment back only after a period of 10 years from their retirement. But due to Andersen’s involvement with Enron, many other individuals and institutions would now have the right to stake their claims first against the accounting firm’s capital, leaving the partners’ payback in limbo.

What’s worse, retired Andersen partners did not have typical pensions backed by the Pension Benefits Guaranty Corporation nor employer-sponsored 401(k) plans. Instead, they were encouraged to invest for their own retirements through Keogh accounts for unincorporated businesses. However, a \$3,500 monthly stipend that worked like a safety net was put in place, should those investments go awry (Schwartz 2002d). Through their lawsuit, the retired partners wanted to halt efforts by current Andersen partners to disband, in effect forcing them to guarantee retirement benefits and equity repayment (The New York Times 2002). In any case, jumping ship was already harder for Andersen partners in the US as compared to those from other countries, due to the non-compete clauses in their contracts.

As far as Andersen’s foreign affiliates were concerned, it was an altogether different story (Glater 2002b). As an off-shoot of the US government’s case, Andersen’s Spanish and Chilean offices announced that they would sever ties with the firm. Branches in Italy, Poland, Portugal and Switzerland admitted considering

similar steps, deciding either to operate independently or to be acquired by a rival firm. At around that time, firms such as Sara Lee, Abbot Laboratories and Northeast Utilities – among Andersen's 20 largest and most longstanding clients – revealed that they too would no longer avail of the firm's auditing services.

On 26 March 2002, Joseph F. Berardino declared that he would be stepping down as Andersen's chief executive. Berardino released the following statement upon his resignation: "I have concluded that my continuing as worldwide CEO could become an impediment to the efforts of Mr. Volcker and many others to save the US firm. (...) While my nature is to keep fighting and protect our clients, the fact is that the improper shredding of documents took place on my watch – and I believe it is now in the best interests of the firm for me to step down" (Glater and Schwartz 2002). When Berardino assumed the top post in Andersen barely 15 months ago, he did so with a clear mandate to help the firm recover from a slew of serious accounting scandals. "We have been prepared to lead some significant change for this firm and the industry, but we have been unable to get that message heard. I only had one more bullet left, and that was the one I used yesterday. But that bullet also sends the message to our people to keep fighting" (Eichenwald 2002e).

Berardino admitted that it was the demonstrations of Andersen staff that prodded him towards his decision: "Over the last week I have watched our people have rallies, basically crying for their dignity, and I just wanted to help. I just felt the best signal I could give to our people was to sacrifice the only thing I have left to give: my job" (Eichenwald 2002e). It was far from clear, however, whether Berardino's departure provided the troubled firm a better chance for survival or on the contrary, it simply hastened its destruction.

On 30 March 2002, scarcely a few days after the announcement of Berardino's resignation, the already leaderless Andersen was still dealt with another devastating blow. In a separate case involving the Baptist Foundation of Arizona, Andersen had been accused of faulty auditing in what had become the largest non-profit bankruptcy in the US, costing about 13,000 investors a total loss of \$570 million. Andersen had initially agreed to a \$217 million settlement, but when the payment was due on 15 April 2002, it notified parties that its insurance carrier, the Professional Services Insurance Company, would be unable to meet those obligations. This was due largely to the fact that Andersen itself had a outstanding bill of more than \$100 million towards the payment of its insurance premium, and for this reason the Professional Services Insurance Company was rendered technically insolvent. John P. Coffey, lead trial lawyer for the Baptist Foundation of Arizona Liquidating Trust, offered these words as commentary, "This is treachery of the highest of the highest order. It's a second stab in the back to everyone who lost money" (Eichenwald 2002f).

It was at this juncture when the idea of a deferred prosecution of an acknowledged wrongdoing was floated (Eichenwald 2002g). Previously, Volcker had tried to persuade the government to drop its charges on the promise of re-engineering a "new and improved version" of Andersen (Eichenwald 2002d). But the US Justice

Department responded that it would not even consider elaborating such a deal, unless Andersen was prepared to admit that it had committed a crime. Later on, the US Justice Department gave signs that it could in principle accept deferring Andersen's prosecution if the firm publicly acknowledged the illegal destruction of documents in the Enron investigation and agreed to restrictions similar to those of a "corporate probation". Once approved by a judge, prosecution would be deferred for a number of years, after which the indictment would be dismissed. But if the defendant were to commit other misdeeds during the deferral period, the trial would proceed and the admission could then be used against the defendant as evidence. In lieu of Volcker's suggestion of a withdrawal of the indictment "without prejudice", a deferral without an admission would certainly have been most advantageous to Andersen. But the US government was unwilling to give in on the requirement of Andersen's admission. This condition exacerbated Andersen's dilemma. The acceptance of precisely that sort of guilt was tantamount to committing corporate suicide for an auditing firm, granted that its integrity and good reputation were by far its most valuable assets.

Meanwhile, an extraordinary pressure mounted on Andersen to admit wrongdoing shortly after David B. Duncan, the former partner in charge of Enron's audits, entered a guilty plea to a single felony: he admitted to having orchestrated a large-scale effort to destroy documents and obstruct a federal inquiry (Eichenwald 2002h). In principle, Duncan's testimony could be used by the government as evidence as it went about Andersen's prosecution. But in the end, not even Duncan's defection was sufficient to push Andersen towards an admission of guilt, and on 6 May 2002 the trial began. The basic issues were simple: Was the shredding of documents related to Enron's finances done with a corrupt intent of impeding an official investigation? And if so, should Andersen as a firm be held accountable for its employees who committed the crime? (Eichenwald 2002i).

After a six week trial – including 10 full days during which a deadlocked jury agonized over its verdict – Andersen was finally convicted of obstruction of justice in the Enron case (Eichenwald 2002k). Shortly before releasing its decision, the jury was instructed by judge Melinda F. Harmon that it could declare the firm guilty even if it did not agree as to which of the employees had the intent to commit the crime (the "corrupt persuader"), thus setting a precedent for corporate criminal liability cases (Eichenwald 2002j). Although sentencing was scheduled for 11 October 2002, Andersen announced that it would cease auditing publicly traded companies by the end of August. 31 August 2002 would then effectively signal the demise of a once proud, 89 year old accounting firm.

In the final analysis, the jury reached its verdict on the basis of the deletion of a few words from a single memorandum (Eichenwald 2002k). Surprisingly, the one truly responsible for the removal wasn't even David B. Duncan, the Andersen partner in charge of the Enron audits who had previously admitted committing a felony. Some time in mid-October 2001, Duncan prepared a memorandum for a news release regarding Enron's third quarter earnings. In the draft, Duncan had characterized certain losses reported by Enron to be "nonrecurring". Upon review,



Nancy Temple, an Andersen lawyer, suggested that Duncan remove that specific portion of the memorandum for such a representation could be found misleading. Certainly, this type of advice not to put something in writing was the kind that lawyers routinely give their clients, to protect them from creating documents that could later on be used against them (Gillers 2002).

Just the same, the jury referred to that memorandum as the “smoking gun”. It concluded that Temple had “corruptly persuaded” Duncan to alter information for the purpose of impeding an official investigation by the SEC. Temple suggested that Duncan delete the mention of something that could be misleading in Enron’s public statements about its financial condition. According to this reasoning, Duncan, who had already entered a guilty plea to obstruction, in effect did not commit any crime.

The jurors acknowledged that the shredding of documents in itself was not an issue. They were convinced that it was done in good faith and not intended to hinder any official investigation. However, in the jurors’ opinion, the disposal of records did not cease being a misguided effort on the part of ill-trained employees to comply with Andersen’s document retention policies (Glater 2002e).

By that time, Andersen was already but a mere shadow of its former self. Since 1 January 2001, 690 of its 2,311 public company clients had already abandoned it. Moreover, from its original US workforce of around 27,000 employees, only about 10,000 remained, as the combined result of layoffs and defections of entire offices and practices to other competing firms (Eichenwald 2002k). Deloitte had already acquired the bulk of Andersen’s tax business in April, 2002 (Glater 2002d), while in May, KPMG announced that it had signed a letter of intent to acquire the consulting units of Andersen Worldwide member firms, for a total price of \$284 million (Andersen 2002d).

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# How to Discover and Avoid Corruption in Companies

*Caspar von Hauenschild*

## Why Does It Matter?

### Increasing Public Pressure

It all started in the late 90s. Allegations of corruption led to the resignation of the team of EU-Commissioners under Jacques Delors. The International Olympic Committee (IOC) had to investigate corruption inside their prominent delegates. Presidents of a significant number of countries – from the Philippines to Kenya – were forced out of office because of charges of bribery and corruption. Even the crash of the total economies in Asia and Russia in 1998 was to some extent related to the tradition of nepotism and the culture of bribery and corruption. In 2002 also the crash of Argentina – 45 years ago among the top 5 richest countries of the world – was argued as being the result of a culture of bribery and corruption – widely spread in the upper and medium class. All this caused poverty and destruction of still rather weak social welfare systems. The middle class was completely wiped out and the wealthier people moved more funds to offshore-financial-centers or even completely left their ailing home countries. The collapse of Enron, WorldCom and Parmalat was also attributed to corrupt business practices and caused heavy losses for shareholders and thousands of pensioners. Last but not least thousands of people lost their jobs.

New laws with tougher sentencing guidelines came into force in 1998. All OECD-countries – counting for 80% of foreign direct investments and 60% of world exports – abolished the tax-deductibility of bribes and agreed on an Anti-Bribery-Convention which also made the bribing of a foreign public official a criminal offence in the country of the bribing company. In the commercial world bribery and corruption tended to be a very sensitive topic. It was regarded as an eternal problem which cannot be solved in a world of different cultures and histories. On the other hand no one would ever dare to defend actively bribery and corruption as it certainly distorts competition – the buzzword of any “credo of a business man” in today’s market economies. “Corruption is no longer a total taboo” (CRG 2002, p. 3) thanks to the OECD-Convention and the attention of the media.

Today the business world is very much concerned about the risk of reputational damages.

## No More Secrecy

“The rapid expansion of international trade has increased the incentives of winning business by the ‘back door’”. (CRG 2002, p. 3) On top of that computerized banking and the “mushrooming of offshore-financial-centers” facilitate the moving of funds from bribery and corruption between different jurisdictions. On the other hand “the temptation to break the rules may have increased, but so have the risks”! (CRG 2002, p. 3) Corruption as any other crime requires secrecy. And secrecy in a world of rapid communication from Beijing to London is very difficult to be maintained. Also thanks to the global capital market a corruption scandal in Germany is also registered by investors in Australia. It is not only CNN with his reports from everywhere but also any regional newspaper for consumers or investors which will report on scandals of the multinational companies as well as of SMEs – small and medium sized enterprises – with strong local roots. It looks like the “good old banking secrecy” is coming under pressure. Once a “holy taboo of the commercial banking world” it is already substantially “de-mystified” in Germany by the fact that tax offices and social welfare institutions can investigate the existence of accounts or security portfolios of any citizen. And this will go on – also in Switzerland, Austria, Luxemburg and 70 OFC from Liechtenstein to Cayman Islands around the world competing for trillions of untaxed funds including those from bribery and corruption estimated by Worldbank to reach “only” € 50 billion a year. The amounts involved are simply too big to allow any Minister of Finance to close his eyes in view of huge budget deficits of even the strongest nations of the world.

It might take another 5 years before a new OECD Directive will try to harmonize taxation schemes. But it will happen. And it will further support all efforts countering bribery and corruption.

## Employees and Managers “on the Grill”

With increasing public pressure in a dynamic process of globalization the pressure on prosecutors will also increase. Almost all OECD countries have substantially beefed up the number of prosecutors and have built up special task forces for bribery and corruption cases. This in turn will lead to more cases taken to court. In some countries – like Germany – a company cannot be taken to court but only an individual. As a consequence we will see more employees and their managers facing court proceedings. In Germany you can go to jail for up to 3 years if you have bribed a local or foreign official. The judge can even send you to jail for up to 5 years if you have bribed your counterpart in a normal commercial transaction. By the way it is important to understand that the taker of bribes is very often con-

demned for two different offences: for being bribed and tax avoidance. The taker of illicit payments never declares in his income tax bill an “income from bribery” or alike – for obvious reasons. In short, in some jurisdictions like Germany it is first of all the employee who is on the grill not the company. To what extent the company will “bail out” its employees can only be found out after the case.

So there are three answers to the first question: why does it matter to discover and avoid bribery and corruption in companies?

- The public opinion is furious about global corruption scandals and moral pressure is mounting in a dynamic global environment.
- The temptation to break the rules may have increased, but so have the “risks”, notably the reputational risk for companies!
- With more professional prosecutors also individual employees can go to jail!

So what to do in a complex global market environment with a lot of pressure of the public and more risks for individuals and companies?

My experience is to do three things first:

- start to do your homework and discover the level of corruption in your company!
- complete your homework and implement a strict anti-corruption policy!
- and then fine tune your homework by going for alliances against bribery and corruption in manageable market segments!

## **How to Discover Corruption in Companies?**

Corruption is the abuse of a political or economic position for private gain – according to Transparency International, the NGO countering bribery and corruption in 95 countries. You can find this definition in the preface of almost all Codes of Conduct of any institution. But what is regarded as “abuse” by law or by ethical standards of the company? Is your acceptance of an invitation to a soccer match by a supplier already a potential abuse of an economic position? Or is this acceptable marketing? Or is it only abuse when the soccer match event is enriched by a night club visit and a hotel accommodation? And what do you do as a regional manager in Brazil, Russia, China and India – the most dynamic markets of the world? No company with a potential “global product” can afford to abstain from competing on those growing markets. Many companies send their sales people first to those markets. They open sales offices with very few people or engage with agents or joint-venture partners. Business ethics are not investigated in advance, but experienced by doing. Very often companies then get involved in bribery and corruption cases without knowing how to deal with it. Regional managers like to argue that corruption in those countries is part of the culture. It is not realis-

tic to expect international companies to behave differently. CRG counters: “this argument is hazardous. All of the world’s great religious and moral traditions condemn corruption; the key variable is not so much ‘culture’ as power. No one likes paying bribes. If ordinary people pay, this is usually because they have no choice, not because they find the practice acceptable.” CRG experts conclude that “poorer people suffer most from petty bribery. Far from regarding petty corruption as normal, people often feel a deep sense of anger.” This should be considered in particular by international companies operating in those countries. They are judged by individuals with different standards. CRG polarizes the issue: “all forms of bribery are problematic, but most people see a clear difference between paying small bribe to secure essential medicines and paying a large bribe to secure a defense contract. If a company’s actions contradict popular values that in itself is a source of risk. No one will come to its defense when it runs into trouble”. (CRG 2002, p. 10) Some huge multinationals – also from Germany – were already totally banned from doing any business in some countries because of bribing directly or indirectly government officials. CRG rightly ask whether “the growth of Islamic extremism in the Middle East is in part a reaction to governmental corruption. International companies that are too closely associated with corrupt regimes are storing up future political risks for themselves” (CRG 2002, p. 10). To get this message across to all regional managers and internal strategic “think tanks” are very important. To do this successfully means to open an internal dialogue on dilemmas and conflicts in doing business in markets and countries with a high degree of corrupt business practices. It all starts with a detailed description of corrupt business practices and their “movers and shakers”, the law and the rules, the role of prosecutors and judges as well as the level playing field of agents, lawyers or any other intermediaries who offer their “ethical and unethical services”.

The exercise to simply describe and analyze dilemmas and conflicts will in many cases lead to the identification of strategies to avoid corrupt business practices in the country of the planned investment. The exercise of a thorough analysis is also important to avoid a painful and costly withdrawal following a possible ban of the company or a dangerous uncontrollable situation with blackmailing and violence. It goes without saying that this analysis as a kind of “corruption mapping” should be done with all parties concerned – the front line managers, the compliance officers and the representatives of the legal and human resources department. At this early point in time also the final decision makers should be involved. They carry the responsibility for an investment in a potentially corrupt market or for the disinvestment in case the risk is considered to be too high. Too often the senior managers are not involved at an early point in time. Sometimes it looks like this is done on purpose. The CEO would not be able to speak in public on perfect business ethics and the values of the company anymore. This is a very dangerous strategy in a world of transparency and communication. It will also lead to the famous “credibility trap” which is created when there is no consistency between “what you say” and “what you do”. Nobody would listen to the CEO anymore in times of crises management and restructuring efforts. His authority would be se-

verely damaged and the majority of employees would follow his “pep talks” only halfheartedly. Some CEOs lost their jobs being caught in the “credibility trap”.

In short, to discover corruption in an open and concerted dialogue in a company is more than just a project “how to counter bribery and corruption in some critical markets”. When you want all individuals concerned including the CEO involved and get their enthusiasm about solving dilemmas and conflicts resulting from corrupt markets then you have to re-design the corporate culture of a company.

## **How to Implement an Anti-corruption Policy in a Strong Corporate Culture**

“Zero-tolerance” on bribery and corruption is a corporate culture project which in turn is a “jumbo-project”. It takes 1-2 years to be carried out. And it is a never ending process because markets change and create new dilemmas and conflicts which have to be discussed and hopefully being dissolved. A strong corporate culture requires a systematic management of values. Josef Wieland, one of the leading scientists of corporate business ethics in Germany designed a “WerteManagementSystem” (WMS) (Wieland 2004, p. 25) which consist of two subsystems: a “Werteviereck” – a square of four value families – and a very strict implementation process with a code of conduct, communication, implementation and integration of the system into other management systems.

The code of conduct is based on four value families:

- Values of performance like competence and creativity
- Values of cooperation like loyalty and team spirit
- Values of communication like respect and transparency
- Values of moral and ethics like fairness, responsibility and accountability.

The codes must be communicated to all employees, vendors, customers, the media and the public. This is particularly important in markets with a so-called ‘culture of corruption’. The message of “zero-tolerance vis-à-vis bribery and corruption” is a prerequisite for avoiding to get caught in local corruption traps. Spreading the message of the codes to all stakeholders is a tough thing to do. Is it naïve to demand this proactive communication? Maybe, yes, in some markets, especially as a small newcomer to the market! Maybe, no, if a company really wants to avoid being sucked into a cycle of bribery and corruption or related blackmailing. There is a wonderful Arab proverb on this: “when the camel puts his head into the tent, the rest of his body soon will follow!” (CRG 2002, p. 8) After communicating the codes must be implemented in order to get them into day-to-day operations and procedures. This requires that the codes and their values must become a part of the yearly individual performance appraisals or goals programs and of the compliance programs. As a result not adhering to the codes has an immediate effect on the in-



dividual bonus of the year or can even lead to getting fired. In short, the codes should also be integrated into the HR-management systems. More advanced companies like BP publishes in his CSR-report the number of employees – not their names – being sacked for breaching the codes – including cases of bribery and corruption. This would admittedly be the end to a widely spread behavior of some fellow employees who prefer to read the codes, laugh about it and then file it somewhere – the fate of many codes of conduct in many companies around the world. They do not know what risk they are running as explained above. And last but not least the codes must be fully integrated into other management and controlling systems of the company – such as the MIS (management information system), any risk management system, the product management systems and the total IT-world of the company. This is a very cumbersome and expensive process. But it is easy to understand – doing business in China or Russia with a more corrupt business environment than doing business in West-Europe should be mirrored in the risk management system and the MIS system of the company.

The integration of a value management system also means that modern instruments of internal communication channels have to be made available. Not everybody is strong enough to report illegal or illegitimate behavior of colleagues to his supervisor or to the compliance officer. He might be afraid of sanctions and mobbing. A recent study of PWC on corporate crimes in Germany concluded that 40% of the cases were reported by so-called “whistleblowers”. Those are employees who did not dare to use the direct reporting lines but preferred to use internal or external hotlines or ombudsmen. As a result more and more companies start to protect the whistleblower and even encourage the use of computer based lock-boxes where the whistleblower can remain unidentified even after being re-contacted by any investigating body. Companies found out that the protection of whistleblowers is part of a reputational risk management rather than a destruction of corporate culture. It is interesting to note that the best international airlines have so-called “non-punitive controlling systems” in order to minimize disastrous failures in the cockpit and the technical services. A pilot failing to notice an alarm signal and a technician forgetting a screw driver in a turbine has to report this in writing. And he knows that his colleague will have to do the same as witness of the failure. And the colleague does it as a fully accepted and protected “whistleblower”. This is to maximize security and total quality management in a company which has to manage operational risks which in turn can cause devastating consequences for the company. Summarizing the implementation of an effective anti-corruption policy is a very challenging project. To send around some new brochures with the new codes of conduct will not be a successful prevention against bribery and corruption. It is the entire corporate culture which has to be redesigned with a very cumbersome process of communication, implementation and integration. The thinking and behaving of the seniors and the entire infrastructure of the company will be affected. Is this a typical exaggeration of a representative of an NGO which always tend to believe their messages have to set the priorities in politics and the economy? Maybe, yes, it is exaggerated for some companies which are operating in solid growth mar-

kets with a fair and strong competitive environment. Maybe, no, it is not exaggerated for those companies which are already “on the grill” of the capital market because investors “hate” surprises – in particular when the surprises are caused by unethical behavior of senior managers and a poor corporate governance. The “Enron-shock” is not digested yet. Unethical behavior cannot only destroy enormous shareholder value in a couple of days but also the credibility and the trustworthiness of senior management for ever – a disaster for the next crises to be managed.

In short, anybody who really wishes to implement an effective anti-corruption policy with zero-tolerance will have to kick-off a project on the level of value management rather than mailing some nicely designed codes of conducts. Only then the company will be able to counter grand corruption but also deal with petty corruption and grease payments in countries and markets with corruptive business practices. Dilemmas and conflicts will be discussed in advance. Solutions will be found after consulting experts and jointly with the individuals concerned. And decisions against or for a “conflicting piece of business” will be taken by those who carry the ultimate responsibility. All this was only to put the own house in order, by introducing anti-corruption policies and integrating the whole effort into a value driven corporate culture. But what are the competitors doing? Is the market dropping corrupt business ethics because a few competitors put their own houses in order?

## **How to Go for Alliances Against Bribery and Corruption in Manageable Market Segments**

An increasing number of companies push forward the anti-corruption agenda by cooperating with governments and some serious representatives of the civil society. More and more companies recognize that the OECD guidelines or the ICC codes addressing anti-corruption policies are not an unrealistic bureaucratic imposition but an important step forward to secure fair competition on any global market. As a result they press their own governments for effective actions or start to participate in joint initiatives of their own associations or join other initiatives on anti-corruption in local markets.

To mention just a few:

- Construction companies in the state of Bavaria concluded an agreement in which each participant signed a commitment for “putting his house in order” first – with regard to corrupt business practices – 2002.
- Three major publishing houses forced their Scandinavian paper supplier to make sure by checks + balances that there are no “illicit offshore payments” to the Russian wood exporter – 2005.

According to the Control Risks Group survey on business attitudes to corruption from 2002 40% of the respondents decided not to pursue an otherwise attractive investment because of concerns about the host country’s reputation for corruption.

The new laws following the OECD initiative from the late 90ties will not be repealed. And the prosecution will become slowly but steadily more efficient. Companies will be forced to conclude alliances against corrupt business practices in order to improve the competitive environment of their markets. Prudent managers with a long term view have no interest in a “race to the bottom” because of bribery and corruption in their global markets.

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PART IV:

## **Business in Society**

# The Path to Corporate Responsibility<sup>1</sup>

*Simon Zadek*

Companies don't become model citizens overnight. Nike's metamorphosis from the poster child for irresponsibility to a leader in progressive practices reveals the five stages of organizational growth.

Nike's tagline, "Just Do it", is an inspirational call to action for the millions who wear the company's athletic gear. But in terms of corporate responsibility, the company hasn't always followed its own advice. In the 1990s, protesters railed against sweatshop conditions at its overseas suppliers and made Nike the global poster child for corporate ethical fecklessness. Nike's every move was scrutinized, and every problem discovered was touted as proof of the organization's irresponsibility and greed. The real story, of course, is not so simple.

Nike's business model – to market high-end consumer products manufactured in cost-efficient supply chains – is no different from that of thousands of other companies. But the intense pressure that activists exerted on the athletic giant forced it to take a long, hard look at corporate responsibility faster than it might have otherwise. Since the 1990s, Nike has traveled a bumpy road on this front, but it has ended up in a much better place for its troubles. And the lessons it has learned will help other companies traverse this same ground.

Over the past decade, I have worked with many global organizations, including Nike, as they grappled with the complex challenges of responsible business practices. This experience has shown me that while every organization learns in unique ways, most pass through five discernable stages in how they handle corporate responsibility. Moreover, just as organizations' views of an issue grow and mature, so does society's. Beyond getting their own houses in order, companies need to stay abreast of the public's evolving ideas about corporate roles and responsibilities. A company's journey through these two dimensions of learning – organizational and societal – invariably leads it to engage in what I call "civil learning." (To map this process for your organization, see the "The Civil-Learning Tool" in the appendix).

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## Organizational Learning

Organizations' learning pathways are complex and iterative. Companies can make great strides in one area only to take a few steps backward when a new demand is made of them. Nevertheless, as they move along the learning curve, companies almost invariably go through the following five stages.

### “It’s Not Our Job to Fix That”

In the *defensive* stage, the company is faced with often unexpected criticism, usually from civil activists and the media but sometimes from direct stakeholders such as customers, employees, and investors. The company's responses are designed and implemented by legal and communications teams and tend to involve either outright rejections of allegations (“It didn’t happen”) or denials of the links between the company's practices and the alleged negative outcomes (“It wasn’t our fault”). Think of Royal Dutch/Shell's handling of the controversy around carbon emissions. For years, the company – along with the rest of the energy sector – denied its responsibility for emissions created by the production and distribution of its energy products. Today, Royal Dutch/Shell acknowledges some accountability. But unlike some of its competitors, the company continues to resist environmentalists' demands that it accept responsibility for emissions from its products after they have been sold.

### “We’ll Do Just as Much as We Have to”

At the *compliance* stage, it's clear that a corporate policy must be established and observed, usually in ways that can be made visible to critics (“We ensure that we don’t do what we agreed not to do”). Compliance is understood as a cost of doing business; it creates value by protecting the company's reputation and reducing the risk of litigation. Until recently, for example, much of the food industry has understood “health” as the avoidance of legally unacceptable “nonhealth”. When Nestlé came under fire for the health dangers of its infant formula – activists claimed that mothers in developing countries would end up mixing the powder with contaminated water, thereby compromising their children's health – its response for many years was to shift its marketing policies to make this hazard clear to new mothers rather than, for example, trying to educate them generally about ways to ensure their babies' overall nutrition. The current public debate on obesity highlights the same dynamics – food companies' instinct is to simply aim for compliance, while the public clearly wants a far greater commitment from them.

### “It’s the Business, Stupid”

At the *managerial* stage, the company realizes that it's facing a long-term problem that cannot be swatted away with attempts at compliance or a public relations

strategy. The company will have to give managers of the core business responsibility for the problem and its solution. Nike and other leading companies in the apparel and footwear industries increasingly understand that compliance with agreed upon labor standards in their global supply chains is difficult if not impossible without changes to how they set procurement incentives, forecast sales, and manage inventory.

### “It Gives Us a Competitive Edge”

A company at the *strategic* stage learns how realigning its strategy to address responsible business practices can give it a leg up on the competition and contribute to the organization’s long-term success. Automobile companies know that their future depends on their ability to develop environmentally safer forms of mobility. Food companies are struggling to develop a different consciousness about how their products affect their customers’ health. And pharmaceutical companies are exploring how to integrate health maintenance into their business models alongside their traditional focus on treating illnesses.

### “We Need to Make Sure Everybody Does It”

In the final *civil* stage, companies promote collective action to address society’s concerns. Sometimes this is linked directly to strategy. For instance, Diageo and other top alcohol companies know that as sure as night follows day, restrictive legislation will come unless they can drive the whole sector toward responsible practices that extend well beyond fair marketing. Among other activities, these companies have been involved in educational initiatives that promote responsible drinking. Likewise, energy companies understand that their industry has to grapple with the sometimes unethical ways in which governments use the windfall royalties they earn from oil and gas extraction. So they are supporting the UK’s Extractive Industries Transparency Initiative, which urges governments to report the aggregate revenues they derive from resource extraction. Some organizations look even further ahead and think about metastrategy: the future role of business in society and the stability and openness of global society itself.

## Societal Learning

A generation ago, most people didn’t think tobacco was a dangerous health threat. Just a few years ago, obesity was seen as a combination of genetics and unhealthy lifestyle choices – certainly not the responsibility of food companies. Today, ageism is rarely seen as a corporate responsibility issue beyond compliance with the law – but in an era of dramatic demographic shifts, it soon will be.

The trick, then, is for companies to be able to predict and credibly respond to society's changing awareness of particular issues. The task is daunting, given the complexity of the issues as well as stakeholders' volatile and sometimes underinformed expectations about business' capacities and responsibilities to address societal problems. Many civil advocates, for instance, believe pharmaceutical companies should sell lifesaving drugs to the poor at reduced prices; after all, the drug companies can afford it more than the patients can. The pharmaceutical industry has claimed over the years that such price limits would choke off its research and development efforts. But today, drug companies are exploring how to sustain R&D while pursuing price reductions in developing countries and how to integrate the prevention of illness into their business models.

Danish pharmaceutical company Novo Nordisk has created a practical tool to track societal learning on some of its core business issues – animal testing, genetically modified organisms, and access to drugs. The drugmaker's approach can be adapted and used by any company facing any number of issues. (See "The Four Stages of Issue Maturity" In the appendix). In the early stages, issues tend to be vague and their potential significance well below conventional thresholds used by the financial community to determine materiality. These issues are often first identified through a company's interactions with nontraditional sources of knowledge, such as social activists. As one senior business manager explains, when he deals with nongovernmental organizations, "I see the future of our markets, our products, and this business".

As issues mature, they become absorbed into mainstream professional debate and eventually into practice. Once leading companies adopt unconventional commitments and practices around certain societal issues, laggards must either follow suit or risk the consequences. In 1991, when Levi Strauss publicly launched its "terms of engagement" – which defined the labor standards for Levi's business partners and was one of the world's first corporate conduct policies – every other company in its industry looked the other way, arguing that labor standards in other people's factories weren't their responsibility. When the Body Shop adopted human rights policies in the mid-1990s, most mainstream companies deemed its practices unfeasible. And when BP CEO Sir John Browne acknowledged in his infamous Stanford Business School speech that BP had a co-responsibility to address the challenges associated with global warming, he was taking a leadership role and betting that others would have to follow – as indeed they did. Each of these actions played a big part in dragging the rest of the players in the industry toward common approaches to responsible business practices.

## **How Nike Just Did It**

Nike's story illuminates better than most the tensions inherent in managing corporate performance and societal expectations. In the 1990s, the company was blindsided when activists launched an all-out campaign against it because of worker



conditions in its supply chain. There's no doubt that Nike managed to make some extraordinary errors. But it also learned some important lessons. Today, the company is participating in, facilitating, convening, and financing initiatives to improve worker conditions in global supply chains and promote corporate responsibility more generally.

## From Denial to Compliance

Nike's business model is based exclusively on global outsourcing. Simply put, the company has rarely produced a shoe or a T-shirt outside of its design studio. By the time the company was singled out in a 1992 Harper's Magazine article for the appalling working conditions in some of its suppliers' factories, almost all of its competitors were using a similar sourcing model. Labor activists in the early 1990s were exerting enormous pressure on premium-brand companies to adopt codes of conduct in their global supply chains. These groups targeted Nike because of its high-profile brand, not because its business practices were any worse than its competitors'.

The company's first reaction was defensive. "We said, 'Wait a minute; we've got the best corporate values in the world, so why aren't you yelling at the other folks?'" one of Nike's senior managers recalls. "That was a stupid thing to do. It didn't get us anywhere. If anything, it raised the volume higher." The company realized it couldn't just shut out the noise. It eventually responded to activists' demands for labor codes and, after further pressure, agreed to external audits to verify whether these codes were being enforced.

Nike hired high-profile firms or individuals to conduct the audits, which were initially one-off events. But these companies and individuals had little actual auditing experience or credibility in labor circles, and the approach backfired. Statements such as former UN Ambassador Andrew Young's casual conclusions that all was well in Nike's supply chains were publicly challenged and subsequently proved to be flawed or overly simplistic. Consequently, many labor activists believed Nike's early, failed attempts at building credibility were proof of insincerity.

Companies frequently resist accepting new responsibilities because they see how risk-taking organizations are criticized for their efforts to do just that. But the pressure on Nike was so intense that it couldn't afford to wait until the whole sector advanced. Labor activists' demands for action were cascading into Nike's core and highly profitable youth markets in North America and Europe. So in 1996, Nike "went professional" in creating its first department specifically responsible for managing its supply chain partners' compliance with labor standards. And in 1998, Nike established a Corporate Responsibility department, acknowledging that acting responsibly was far more than just reaching compliance; it was an aspect of the business that had to be managed like any other.

## Managing Responsibility

By the turn of the millennium, Nike's labor-compliance team was more than 80 strong. The company had also hired costly external professionals to audit its roughly 900 suppliers. Even so, new revelations about Nike's failure to adhere to its own labor codes constantly came to light. Many outsiders took this as proof that the company still lacked any real commitment to address labor standards. Those inside Nike's walls were incredibly frustrated by their failure to move past this ongoing crisis. After a particularly painful documentary on Nike aired in the United Kingdom, the CEO assembled a team of senior managers and outsiders led by Nike's vice president for corporate responsibility, Maria Eitel. The team was instructed to leave no stone unturned in figuring out how to get beyond the company's continued failure to effectively comply with its own labor codes.

The team's review didn't focus on the behaviors of factory managers and workers, as many previous studies did; the group considered issues at the factory level symptoms of a larger systemic problem. Instead of looking down the supply chain, the team studied the up-stream drivers. After six months, it concluded that the root of the problem was not so much the quality of the company's programs to improve worker conditions as Nike's (and the industry's) approach to doing business.

Like its competitors, Nike offered performance incentives to its procurement teams based on price, quality, and delivery times. This standard industry practice undermined Nike's many positive efforts to comply with its own codes of conduct; it had the unintended effect of actively encouraging its buyers to circumvent code compliance to hit targets and secure bonuses. And there were other tensions between Nike's short-term financial goals and its longer-term strategic need to protect the brand. For instance, the company's tight inventory management often led to shortages when forecasting errors were made. That created urgent short-term needs for more goods to satisfy market demand, which drove procurement teams to take what they could get. Often, this would force suppliers to cut corners to push the envelope on delivery times, which would drive up overtime in the factories – exactly what Nike's labor code was trying to prevent. To cap it all, when something went wrong and Nike's reputation took a hit, the procurement, marketing, and inventory management teams weren't the ones that suffered financially. The brand shouldered the burden, and the legal and other costs were charged to the corporate center, not to those whose behavior had caused the problem in the first place.

Nike realized that it had to manage corporate responsibility as a core part of the business. Technically, it was relatively easy to reengineer procurement incentives. The review team proposed that Nike grade all factories according to their labor conditions and then tax or reward procurement teams based on the grade of the supplier they used. But commercially and culturally, it wasn't so simple. Nike's entrepreneurial culture extended from brand management to procurement. Any

challenge to that spirit was considered by many as an affront to a business model that had delivered almost continual financial success for three decades.

Nike's resistance to shifting its procurement methods cannot be dismissed as some irrational distaste for change. It knew that constraining its procurement teams would involve real costs and commercial risks. And the hard reality was that Nike's efforts to secure adequate worker conditions delivered little to the financial bottom line in the short term – which was the sole focus for the bulk of the company's mainstream investors. (For more on the business implications of doing good, see “Being Good Doesn't Always Pay” in the appendix). Nike's challenge was to adjust its business model to embrace responsible practices – effectively building tomorrow's business success without compromising today's bottom line. And to do this, it had to offset any first mover disadvantage by getting both its competitors and suppliers involved.

It has turned out to be a long and rocky path for Nike and other companies working to get the labor piece right. Several multistakeholder initiatives were launched that focused on the development of credible and technically robust approaches to compliance. Most well-known in the United States are the Fair Labor Association (FLA), which was initially established with support from the Clinton administration as the Apparel Industry Partnership, and the SA8000 standard, which evolved with help from parties outside the United States. The multistakeholder Ethical Trading Initiative (ETI) emerged from the United Kingdom. Each initiative has distinct characteristics, involves diverse companies, and associates with different NGOs, labor organizations, and public bodies. But all have broadly responded to the same need to develop, monitor, and comply with now commonly accepted labor standards underpinned by UN conventions.

## Responsible Business Strategies

Nike's underlying business strategy wasn't static as it moved up the corporate responsibility learning curve. The prevailing trade agreement in the apparel industry, the Multifiber Arrangement (MFA), was nearing its end. The MFA had established country-based garment import quotas to the all-important U.S. market. The growth of Nike's apparel supply chains during the 1990s was partly driven by cost grazing – the ongoing search for lower prices. But the MFA had reinforced that need to graze because companies had to search the world for spare quota. The MFA also inhibited businesses like Nike from making longer-term procurement commitments to their suppliers and thwarted the stable conditions needed to advance opportunities for brands to invest in technological and managerial progress.

The MFA's expiration on January 1, 2005, will accelerate the consolidation of supply chains. With disperse supplier relationships and no quotas to destabilize, experts argue, the scene is set for changes in the apparel industry that will be as significant as the advent of globalized supply chains themselves, which was a major factor in Nike's original success.

It's not just that there will be fewer and larger suppliers. Intensified competition is pushing apparel makers to shorten the time between design and market even as they continue to cut costs. The industry will probably move to some form of lean manufacturing shifting away from traditional top-down managerial styles toward greater worker self-management that delivers more flexibility and productivity. Some estimates suggest possible manufacturer cost savings of up to 25%.

In terms of worker conditions, the move toward lean manufacturing could reduce the total number of people employed, especially if fewer, more stable supply chains lead to advanced production technologies. But the shift could also improve conditions for the remaining workers over time. Because lean manufacturing requires employees to learn new skills, it would put upward pressure on wages and improve management's behavior toward workers. Clearly, Nike and its competitors will soon have new opportunities to create value and new ways to align those opportunities with responsible business practices. The challenge is to manage the transition to a post-MFA world in a responsible fashion.

Nike's 2004 acquisition of the athletic apparel and footwear brand Starter also affects Nike's strategy in terms of corporate responsibility. Starter is sold at large retailers such as Wal-Mart, Kmart, and Target, and the acquisition is a key element of Nike's growth strategy as the company reaches the limits of organic growth in some of its core markets. Now that it has entered the world of value-channel economics, Nike must concern itself with high product volumes and low margins while also maintaining its commitment to its labor codes.

Although it is a king-size operator in the market for premium goods, Nike has far less leverage in the market for value items, in which it must deal with retailers like notorious cost-squeezer Wal-Mart. Furthermore, value customers focus on price and are generally less responsive to ethical propositions – particularly those involving far away problems like worker conditions in Asia or Latin America. Nike's public position on these issues is clear: It is committed to maintaining its labor compliance standards in all product lines and in all supply chains. But the business model underlying value-channel economics requires that Nike find new ways to keep its social commitments. Part of Nike's response to this challenge has been to argue for regulated international labor standards, which would offset any possible competitive disadvantage that Nike would incur if it had to go it alone.

Collective responsibility simply makes sense. After the acquisition of Starter, Nike sent out letters to stakeholders explaining its approach: "Whatever the channel where Nike products are sold, we have a growing conviction that it is essential to work with others to move toward the adoption of a common approach to labor compliance codes, monitoring, and reporting to help ensure broader accountability across the whole industry. This will take time, but through these efforts and with the active participation of all the major players, we believe we can further contribute to the evolution of supply chain practices, including in the value channel." Nike recognized that its long-term success required it to expand its focus from its own practices to those of the entire sector.

## Toward Civil Action

Nike has been involved in various initiatives designed to bridge corporate responsibility and public policy, starting with the FLA in 1998. In July 2000, CEO Phil Knight attended the launch of the Global Compact, UN Secretary-General Kofi Annan's multistakeholder initiative designed to encourage responsible business practices. Knight was one of the 50 or so chief executives of companies, NGOs, and labor organizations from around the world who were at the event. He was the only CEO of a U.S. company in attendance; since then, many more U.S. organizations have associated themselves with the initiative. At the launch, Knight announced Nike's "support of mandatory global standards for social auditing", asserting that "every company should have to report on their performance" against these standards. His proposal meant that Nike's suppliers and competitors would have to share the financial burden of securing a regulated level of worker conditions in global supply chains. When the social performance records of all the companies were made public, Knight believed, Nike would be revealed as a leader, which would help protect the brand.

In early 2004, Nike convened high-profile players from the international labor, development, human rights, and environmental movements at its Beaverton, Oregon, headquarters. Their willingness to attend was itself a testament to how far Nike had progressed from a target of attack to a convener of erstwhile critics. Even more notable was the fact that the topics discussed weren't specific to Nike's operations. The conversations focused on the potential negative fallout from the MFA's demise.

The end of the agreement raises the challenge of how to assist countries with garment industries that may be suddenly rendered far less competitive in international markets. For example, a significant portion of the export-oriented garment industry in Bangladesh is at risk. Today, that sector employs upward of two million people and accounts for 75% of the country's foreign exchange earnings. Similar data for countries in Latin America, Africa, and Asia highlight the potentially disastrous social and economic fallout if the transition to a post-MFA world is botched.

The MFA is ending partly because of the lobbying by NGOs and governments of key exporting countries; they argued that the agreement was a barrier to trade for developing countries. Even though companies will be downsizing, relocating, and consolidating in response to the MFA's demise, the business community was not a significant player in this trade change and, in fairness, cannot be held responsible. However, the public is already focusing on which companies are laying off workers and with what effects. Nike is one of a few companies that believe, regardless of how this situation arose, they must be part of the solution if they don't want to be seen as part of the problem.

So Nike has joined a group of organizations – including companies such as U.S. retailer the Gap and UK retailer Asda; NGOs such as Oxfam International

and AccountAbility; labor organizations such as the International Textile, Garment, and Leather Workers Federation; and multistakeholder initiatives such as the ETI, the FLA, and the Global Compact – to explore how such an alliance could help to address the challenges of a post-MFA world. This alliance might be well placed to advise governments and agencies like the World Bank on ways to develop public programs to assist workers in the transition; establish a framework to guide companies in their realignment of their supply chains; or lobby for changes to trade policies that would confer benefits to factories and countries that took labor issues into greater account.

Nike is, of course, a business, and as such is accountable to its shareholders. But the company has taken significant steps in evolving a strategy and practice that shifts it from being an object of civil activism to a key participant in civil society initiatives and processes.

In dealing with the challenges of corporate responsibility, Nike has come to view the issue as integral to the realities of globalization – and a major source of learning, relevant to its core business strategy and practices. That learning prompted the company to adopt codes of labor conduct, forge alliances with labor and civil society organizations, develop nonfinancial metrics for compliance that are linked to the company's management and its broader governance, and engage in the international debate about the role of business in society and in public policy.

As Nike's experience shows, the often talked-up business benefits of corporate responsibility are, at best, hard-won and frequently, in the short term, ephemeral or nonexistent. When accusations arise, it's easy for companies to focus on the low-hanging fruit employee morale, for instance, or the immediate need to defend the brand. But making business logic out of a deeper sense of corporate responsibility requires courageous leadership – in particular, civil leadership – insightful learning, and a grounded process for organizational innovation.

## **Appendix**

### **The Civil-Learning Tool**

The civil-learning tool is intended to help companies see where they and their competitors fall on a particular societal issue. It can help organizations figure out how to develop and position their future business strategies in ways that society will embrace.

The tool factors in the two different types of learning, organizational and societal. When an issue is just starting to evolve, companies can get away with defensive actions and deflections of responsibility. But the more mature an issue becomes, the further up the learning curve an organization must be to avoid risk and to take advantage of opportunities.

As the tool makes clear, there is a point where the risky red zone turns into the higher-opportunity green zone. The question for most companies is, “Where is that line for my organization?” The answer depends on a host of factors, and a company’s actions can actually shift the line in its favor. A company might step way out in front of an immature issue while most of its rivals are still in defensive mode. Cases in point: BP’s aggressive stance on publishing the amount of royalties it pays to host governments; Rio Tinto’s adoption of a human rights policy when most companies would not go near the idea; and Levi Strauss’s groundbreaking “terms of engagement”, which set out the company’s responsibilities to workers in its global supply chains.

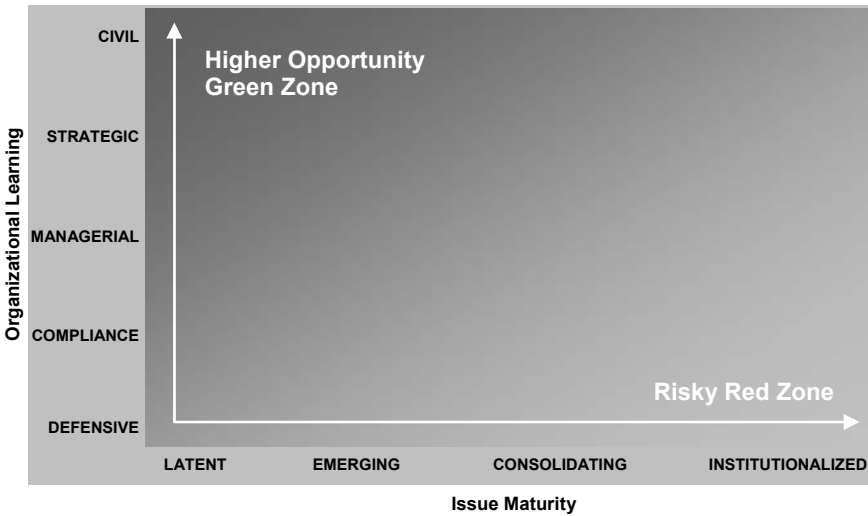


Fig. 1. Civil-Learning Tool

Additionally, events in one industry can affect companies in a different industry or organizations in the same industry that are facing different issues. For example, the heated public debate about the pricing of drugs in poorer communities has created a broader debate about the fundamentals of intellectual property rights and the merits of a preventive approach to health at a time when the pharmaceutical industry makes its money from treating illnesses. Similarly, the emergence of obesity as an issue for the food industry has been accelerated by both rising health care costs and the devastating impact of litigation on the tobacco industry.

## The Five Stages of Organizational Learning

When it comes to developing a sense of corporate responsibility, organizations typically go through five stages as they move along the learning curve.

**Table 1.** Five Stages of Organizational Learning

<b>Stage</b>	<b>What Organizations Do</b>	<b>Why they Do it</b>
<i>Defensive</i>	Deny practices, outcomes, or responsibilities	To defend against attacks to their reputation that in the short term could affect sales, recruitment, productivity, and the brand
<i>Compliance</i>	Adopt a policy-based compliance approach as a cost of doing business	To mitigate the erosion of economic value in the medium term because of ongoing reputation and litigation risks
<i>Managerial</i>	Embed the societal issue in their core management processes	To mitigate the erosion of economic value in the medium term and to achieve longer-term gains by integrating responsible business practices into their daily operations
<i>Strategic</i>	Integrate the societal issue into their core business strategies	To enhance economic value in the long term and to gain first-mover advantage by aligning strategy and process innovations with the societal issue
<i>Civil</i>	Promote broad industry participation in corporate responsibility	To enhance long-term economic value by overcoming any first-mover disadvantages and to realize gains through collective action

## The Four Stages of Issue Maturity

Pharmaceutical company Novo Nordisk created a scale to measure the maturity of societal issues and the public's expectations around the issues. An adaptation of the scale appears below and can be used by any company facing any number of societal issues.



**Table 2.** Four Stages of Issue Maturity

<b>Stage</b>	<b>Characteristics</b>
<i>Latent</i>	Activist communities and NGOs are aware of the societal issue. There is weak scientific or other hard evidence. The issue is largely ignored or dismissed by the business community.
<i>Emerging</i>	There is political and media awareness of the societal issue. There is an emerging body of research, but data are still weak. Leading businesses experiment with approaches to dealing with the issue.
<i>Consolidating</i>	There is an emerging body of business practices around the societal issue. Sectorwide and issue-based voluntary initiatives are established. There is litigation and an increasing view of the need for legislation. Voluntary standards are developed, and collective action occurs.
<i>Institutionalized</i>	Legislation or business norms are established. The embedded practices become a normal part of a business-excellence model.

## Being Good Doesn't Always Pay

There is no universal business case for being good, despite what we might wish. Civil regulation, attacks by NGOs to damage corporate reputations, and the like rarely cause measurable, long-term damage to a fundamentally strong business. In the short term, which is what most investors focus on, variations in financial performance are usually attributable to business fundamentals such as design, cost of sales, and market forecasting.

Nike has been highly profitable the past three decades – a period in which it was also subjected to continuous and vociferous opposition to its business practices. Consider the global media coverage of the company's alleged malpractices and the widespread anti-Nike protests at North American universities (a core market segment for Nike). Yet institutional investors have shown a startling disinterest in Nike's handling of its labor standards.

The high-profile, two-year case of activist Marc Kasky versus Nike brought the company before the California and federal supreme courts for allegedly misrepresenting the state of labor standards in its supplier factories. Even now, after an out-of-court settlement, the case raises the specter of further legal action against Nike and others based on similar claims of commercial misstatements. Yet the case has barely raised an eyebrow from the mainstream investment community. Coping with such challenges, it seems, is simply an acceptable overhead cost of doing business.

That's not to say, however, that responsible business practices cannot pay. As with any business opportunity, the chances to make money by being good must be created, not found. Reinventing one's business isn't easy. And doing so in socially responsible ways involves a major shift in managerial mindset – from a risk-

based, reputational view of corporate responsibility to one focused on product and process innovations that will help to realign the business and the market according to shifting societal concerns.

# The Social Responsibility of Business Is to Increase Its Profits<sup>1</sup>

*Milton Friedman*

When I hear businessmen speak eloquently about the “social responsibilities of business in a free-enterprise system”, I am reminded of the wonderful line about the Frenchman who discovered at the age of 70 that he had been speaking prose all his life. The businessmen believe that they are defending free enterprise when they declaim that business is not concerned “merely” with profit but also with promoting desirable “social” ends; that business has a “social conscience” and takes seriously its responsibilities for providing employment, eliminating discrimination, avoiding pollution and whatever else may be the catchwords of the contemporary crop of reformers. In fact they are – or would be if they or anyone else took them seriously –preaching pure and unadulterated socialism. Businessmen who talk this way are unwitting puppets of the intellectual forces that have been undermining the basis of a free society these past decades.

The discussions of the “social responsibilities of business” are notable for their analytical looseness and lack of rigor. What does it mean to say that “business” has responsibilities? Only people can have responsibilities. A corporation is an artificial person and in this sense may have artificial responsibilities, but “business” as a whole cannot be said to have responsibilities, even in this vague sense. The first step toward clarity in examining the doctrine of the social responsibility of business is to ask precisely what it implies for whom.

Presumably, the individuals who are to be responsible are businessmen, which means individual proprietors or corporate executives. Most of the discussion of social responsibility is directed at corporations, so in what follows I shall mostly neglect the individual proprietors and speak of corporate executives.

In a free-enterprise, private-property system, a corporate executive is an employee of the owners of the business. He has direct responsibility to his employers. That responsibility is to conduct the business in accordance with their desires, which generally will be to make as much money as possible while conforming to the basic rules of the society, both those embodied in law and those embodied in

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<sup>1</sup> Published in: The New York Times Magazine, September 13, 1970. Copyright © 1970 by The New York Times Company. Reprinted by permission of The New York Times Syndicate, Paris, France.

ethical custom. Of course, in some cases his employers may have a different objective. A group of persons might establish a corporation for an eleemosynary purpose – for example, a hospital or a school. The manager of such a corporation will not have money profit as his objective but the rendering of certain services.

In either case, the key point is that, in his capacity as a corporate executive, the manager is the agent of the individuals who own the corporation or establish the eleemosynary institution, and his primary responsibility is to them.

Needless to say, this does not mean that it is easy to judge how well he is performing his task. But at least the criterion of performance is straightforward, and the persons among whom a voluntary contractual arrangement exists are clearly defined.

Of course, the corporate executive is also a person in his own right. As a person, he may have many other responsibilities that he recognizes or assumes voluntarily – to his family, his conscience, his feelings of charity, his church, his clubs, his city, his country. He may feel impelled by these responsibilities to devote part of his income to causes he regards as worthy, to refuse to work for particular corporations, even to leave his job, for example, to join his country's armed forces. If we wish, we may refer to some of these responsibilities as "social responsibilities". But in these respects he is acting as a principal, not an agent; he is spending his own money or time or energy, not the money of his employers or the time or energy he has contracted to devote to their purposes. If these are "social responsibilities", they are the social responsibilities of individuals, not of business.

What does it mean to say that the corporate executive has a "social responsibility" in his capacity as businessman? If this statement is not pure rhetoric, it must mean that he is to act in some way that is not in the interest of his employers. For example, that he is to refrain from increasing the price of the product in order to contribute to the social objective of preventing inflation, even though a price increase would be in the best interests of the corporation. Or that he is to make expenditures on reducing pollution beyond the amount that is in the best interests of the corporation or that is required by law in order to contribute to the social objective of improving the environment. Or that, at the expense of corporate profits, he is to hire "hardcore" unemployed instead of better qualified available workmen to contribute to the social objective of reducing poverty.

In each of these cases, the corporate executive would be spending someone else's money for a general social interest. Insofar as his actions in accord with his "social responsibility" reduce returns to stockholders, he is spending their money. Insofar as his actions raise the price to customers, he is spending the customers' money. Insofar as his actions lower the wages of some employees, he is spending their money.

The stockholders or the customers or the employees could separately spend their own money on the particular action if they wished to do so. The executive is exercising a distinct "social responsibility", rather than serving as an agent of the stockholders or the customers or the employees, only if he spends the money in a different way than they would have spent it.

But if he does this, he is in effect imposing taxes, on the one hand, and deciding how the tax proceeds shall be spent, on the other.

This process raises political questions on two levels: principle and consequences. On the level of political principle, the imposition of taxes and the expenditure of tax proceeds are governmental functions. We have established elaborate constitutional, parliamentary and judicial provisions to control these functions, to assure that taxes are imposed so far as possible in accordance with the preferences and desires of the public – after all, “taxation without representation” was one of the battle cries of the American Revolution. We have a system of checks and balances to separate the legislative function of imposing taxes and enacting expenditures from the executive function of collecting taxes and administering expenditure programs and from the judicial function of mediating disputes and interpreting the law.

Here the businessman – self-selected or appointed directly or indirectly by stockholders – is to be simultaneously legislator, executive and, jurist. He is to decide whom to tax by how much and for what purpose, and he is to spend the proceeds – all this guided only by general exhortations from on high to restrain inflation, improve the environment, fight poverty and so on and on.

The whole justification for permitting the corporate executive to be selected by the stockholders is that the executive is an agent serving the interests of his principal. This justification disappears when the corporate executive imposes taxes and spends the proceeds for “social” purposes. He becomes in effect a public employee, a civil servant, even though he remains in name an employee of a private enterprise. On grounds of political principle, it is intolerable that such civil servants – insofar as their actions in the name of social responsibility are real and not just window-dressing – should be selected as they are now. If they are to be civil servants, then they must be elected through a political process. If they are to impose taxes and make expenditures to foster “social” objectives, then political machinery must be set up to make the assessment of taxes and to determine through a political process the objectives to be served.

This is the basic reason why the doctrine of “social responsibility” involves the acceptance of the socialist view that political mechanisms, not market mechanisms, are the appropriate way to determine the allocation of scarce resources to alternative uses.

On the grounds of consequences, can the corporate executive in fact discharge his alleged “social responsibilities”? On the other hand, suppose he could get away with spending the stockholders’ or customers’ or employees’ money. How is he to know how to spend it? He is told that he must contribute to fighting inflation. How is he to know what action of his will contribute to that end? He is presumably an expert in running his company – in producing a product or selling it or financing it. But nothing about his selection makes him an expert on inflation. Will his holding down the price of his product reduce inflationary pressure? Or, by leaving more spending power in the hands of his customers, simply divert it elsewhere? Or, by forcing him to produce less because of the lower price, will it sim-

ply contribute to shortages? Even if he could answer these questions, how much cost is he justified in imposing on his stockholders, customers and employees for this social purpose? What is his appropriate share and what is the appropriate share of others?

And, whether he wants to or not, can he get away with spending his stockholders', customers' or employees' money? Will not the stockholders fire him? (Either the present ones or those who take over when his actions in the name of social responsibility have reduced the corporation's profits and the price of its stock). His customers and his employees can desert him for other producers and employers less scrupulous in exercising their social responsibilities.

This facet of "social responsibility" doctrine is brought into sharp relief when the doctrine is used to justify wage restraint by trade unions. The conflict of interest is naked and clear when union officials are asked to subordinate the interest of their members to some more general purpose. If the union officials try to enforce wage restraint, the consequence is likely to be wildcat strikes, rank-and-file revolts and the emergence of strong competitors for their jobs. We thus have the ironic phenomenon that union leaders – at least in the U.S.–have objected to Government interference with the market far more consistently and courageously than have business leaders.

The difficulty of exercising "social responsibility" illustrates, of course, the great virtue of private competitive enterprise – it forces people to be responsible for their own actions and makes it difficult for them to "exploit" other people for either selfish or unselfish purposes. They can do good – but only at their own expense.

Many a reader who has followed the argument this far may be tempted to re-monstrate that it is all well and good to speak of Government's having the responsibility to impose taxes and determine expenditures for such "social" purposes as controlling pollution or training the hard-core unemployed, but that the problems are too urgent to wait on the slow course of political processes, that the exercise of social responsibility by businessmen is a quicker and surer way to solve pressing current problems.

Aside from the question of fact – I share Adam Smith's skepticism about the benefits that can be expected from "those who affected to trade for the public good" – this argument must be rejected on grounds of principle. What it amounts to is an assertion that those who favor the taxes and expenditures in question have failed to persuade a majority of their fellow citizens to be of like mind and that they are seeking to attain by undemocratic procedures what they cannot attain by democratic procedures. In a free society, it is hard for "evil" people to do "evil", especially since one man's good is another's evil.

I have, for simplicity, concentrated on the special case of the corporate executive, except only for the brief digression on trade unions. But precisely the same argument applies to the newer phenomenon of calling upon stockholders to require corporations to exercise social responsibility (the recent G.M. crusade for example). In most of these cases, what is in effect involved is some stockholders try-

ing to get other stockholders (or customers or employees) to contribute against their will to “social” causes favored by the activists. Insofar as they succeed, they are again imposing taxes and spending the proceeds.

The situation of the individual proprietor is somewhat different. If he acts to reduce the returns of his enterprise in order to exercise his “social responsibility”, he is spending his own money, not someone else’s. If he wishes to spend his money on such purposes, that is his right, and I cannot see that there is any objection to his doing so. In the process, he, too, may impose costs on employees and customers. However, because he is far less likely than a large corporation or union to have monopolistic power, any such side effects will tend to be minor.

Of course, in practice the doctrine of social responsibility is frequently a cloak for actions that are justified on other grounds rather than a reason for those actions.

To illustrate, it may well be in the long run interest of a corporation that is a major employer in a small community to devote resources to providing amenities to that community or to improving its government. That may make it easier to attract desirable employees, it may reduce the wage bill or lessen losses from pilferage and sabotage or have other worthwhile effects. Or it may be that, given the laws about the deductibility of corporate charitable contributions, the stockholders can contribute more to charities they favor by having the corporation make the gift than by doing it themselves, since they can in that way contribute an amount that would otherwise have been paid as corporate taxes.

In each of these – and many similar – cases, there is a strong temptation to rationalize these actions as an exercise of “social responsibility”. In the present climate of opinion, with its wide spread aversion to “capitalism”, “profits”, the “soulless corporation” and so on, this is one way for a corporation to generate goodwill as a by-product of expenditures that are entirely justified in its own self-interest.

It would be inconsistent of me to call on corporate executives to refrain from this hypocritical window-dressing because it harms the foundations of a free society. That would be to call on them to exercise a “social responsibility”! If our institutions, and the attitudes of the public make it in their self-interest to cloak their actions in this way, I cannot summon much indignation to denounce them. At the same time, I can express admiration for those individual proprietors or owners of closely held corporations or stockholders of more broadly held corporations who disdain such tactics as approaching fraud.

Whether blameworthy or not, the use of the cloak of social responsibility, and the nonsense spoken in its name by influential and prestigious businessmen, does clearly harm the foundations of a free society. I have been impressed time and again by the schizophrenic character of many businessmen. They are capable of being extremely farsighted and clearheaded in matters that are internal to their businesses. They are incredibly shortsighted and muddleheaded in matters that are outside their businesses but affect the possible survival of business in general. This shortsightedness is strikingly exemplified in the calls from many business-

men for wage and price guidelines or controls or income policies. There is nothing that could do more in a brief period to destroy a market system and replace it by a centrally controlled system than effective governmental control of prices and wages.

The shortsightedness is also exemplified in speeches by businessmen on social responsibility. This may gain them kudos in the short run. But it helps to strengthen the already too prevalent view that the pursuit of profits is wicked and immoral and must be curbed and controlled by external forces. Once this view is adopted, the external forces that curb the market will not be the social consciences, however highly developed, of the pontificating executives; it will be the iron fist of Government bureaucrats. Here, as with price and wage controls, businessmen seem to me to reveal a suicidal impulse.

The political principle that underlies the market mechanism is unanimity. In an ideal free market resting on private property, no individual can coerce any other, all cooperation is voluntary, all parties to such cooperation benefit or they need not participate. There are no values, no “social” responsibilities in any sense other than the shared values and responsibilities of individuals. Society is a collection of individuals and of the various groups they voluntarily form.

The political principle that underlies the political mechanism is conformity. The individual must serve a more general social interest – whether that be determined by a church or a dictator or a majority. The individual may have a vote and say in what is to be done, but if he is overruled, he must conform. It is appropriate for some to require others to contribute to a general social purpose whether they wish to or not.

Unfortunately, unanimity is not always feasible. There are some respects in which conformity appears unavoidable, so I do not see how one can avoid the use of the political mechanism altogether.

But the doctrine of “social responsibility” taken seriously would extend the scope of the political mechanism to every human activity. It does not differ in philosophy from the most explicitly collectivist doctrine. It differs only by professing to believe that collectivist ends can be attained without collectivist means. That is why, in my book *Capitalism and Freedom*, I have called it a “fundamentally subversive doctrine” in a free society, and have said that in such a society, “there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud”.



# Pan-European Approach. A Conceptual Framework for Understanding CSR<sup>1</sup>

*Dirk Matten and Jeremy Moon*

## Introduction

In recent years the concept of corporate social responsibility (CSR) has gained unprecedented momentum in Europe. Even the sceptical Martin Wolff, Chief Economics Correspondent of the *Financial Times* commented that “CSR is an idea whose time has come” (Wolff, 2002: 62). CSR is a cluster concept which overlaps with such concepts as business ethics, corporate philanthropy, corporate citizenship, sustainability and environmental responsibility. It is a dynamic and contestable concept that is embedded in each social, political, economic and institutional context.

Notwithstanding this recent flurry of CSR activity in Europe, business social responsibility was traditionally regarded in Europe as a peculiarly American phenomenon, reflecting American traditions of participation, self-help and small or at least indirect government. There is, however, no evidence that those taking a comparative view of business-society relations on either side of the north Atlantic over the twentieth century would necessarily argue, by virtue of the relative low salience of CSR in Europe, that its businesses were socially *irresponsible*. Indeed there is evidence to the contrary. Vogel concluded that UK business is “more susceptible to social pressure both from government officials and from other forums to behave ‘responsibly’” (1986: 50). This raises broad questions about the changing nature of, and the reasons, for European corporate social responsibility. In particular it raises a conceptual paradox: was it possible for business in Europe to be socially responsible in the absence of a language of CSR in Europe. And, to what extent does the recent adoption of a language of CSR in Europe reflect a fashion in management, or something genuinely new in the European corporate landscape. We reserve the term “genuinely new” to describe a situation in which the advent of modern CSR implies a previous disregard by corporations in Europe to live up to a set of responsibilities towards society, however defined.

Our argument developed in this chapter is that CSR in Europe, as defined by the majority of recent academic writings and corporate publications, is only “new” in

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<sup>1</sup> Published in: Habisch, A./Jonker, J./Wegner, M./Schmidpeter, R. (eds.): CSR across Europe, Berlin (Springer) 2004, pp. 339-360.

the sense that it represents an innovation in *corporate policies*. While we would maintain that there is a long tradition of business involvement in many of the issues associated with modern CSR. These have been tackled by corporations in Europe for most of the last century (in some cases even longer). However, this company-social engagement was understood, articulated and performed in different ways.<sup>2</sup>

We seek to reconcile this contradiction by proposing a distinction between “*explicit*” and “*implicit*” CSR. We conceptualise CSR as a way of thinking and a set of practices enacted and addressed by – mostly voluntary – corporate policies, which *explicitly* circumscribe the responsibilities towards society, which corporations seek to address. On the other hand, the majority of issues which count as corporate responsibilities towards society in a European context are not part of the corporation’s explicit policies but they are *implicitly* codified in the norms, standards and legal framework of Europe and its nations.

We use the distinction between explicit and implicit CSR to make sense of:

1. the rise and role of the new CSR in Europe, and
2. the way this approach to CSR interacts with deeply embedded national institutional contexts as CSR transforms from an implicit to an explicit form; and
3. the contextualisation of CSR in different national cultures, particularly those without a history of the Anglo-Saxon system of capitalism.

As background, we recognise that twentieth century Europe has experienced a wide range of political and economic systems including systems in which business motivated by profit and open and democratic forms of civil society have been suppressed; those with no independent business sector; those where corruption and irresponsibility flourished. However, we would argue that there are certain similarities between European countries, which manifest themselves in the way CSR is understood and practised and that this understanding is different from, for instance, the USA. We also acknowledge that there are still significant differences among European countries and that most of our thinking is informed by the experiences of CSR in west and north European countries and only to a lesser degree Central and Eastern Europe. The first group of countries have enjoyed extended periods of liberalism, democracy and regulated capitalism in a mixed economy and which, all things being equal, we would expect to resemble American business-society relations.<sup>3</sup> Secondly, we recognise that some features of American

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<sup>2</sup> A study of CSR in Japan echoes this puzzle of reconciling a traditional and a new CSR. Fukukawa, K., & Moon, J. 2004. A Japanese Model of Corporate Social Responsibility?

<sup>3</sup> The comparison of business-society relations of pre-democratic Spain and Portugal and communist Eastern Europe with those of the USA would be a very different exercise. It is noteworthy that following democratisation and market liberalisation Spain and Portugal have witnessed increases in the welfare state, economic regulation and CSR, and following the reduced scope of state welfare and regulation, some of the former communist countries have witnessed an interest in CSR.

societal governance have similarity with features of the European model. Indeed in some cases the USA pioneered regulation for social responsibility (e.g. the postcivil war pensions and public sector employment, the New Deal, the regulatory work of the Environmental Protection Agency in the 1960s).

## What Is CSR?

A wealth of literature has been published on CSR over the last 30 years, many containing their own definition of CSR and related concepts (see for an overview Crane & Matten, 2004a: 37 – 71). Despite the variety of definitions, probably the most widely accepted and referred to conceptualisation of CSR found in the business and management literature is that of Archie Carroll, who sees CSR as a construct relating to four different areas of business-society relations (Carroll, 1979, 1991).

- *Economic responsibility.* Companies have shareholders who demand a reasonable return on their investments; they have employees who want safe and fairly paid jobs; they have customers who demand good quality products at a fair price etc. By definition this is the reason why businesses are set up in society and their first responsibility is to function properly as an economic unit and to stay in business. All subsequent responsibilities are based on this first layer of CSR. According to Carroll, the satisfaction of economic responsibilities is thus *required* of all corporations.
- *Legal responsibility.* The responsibility of corporations in relation to law demands that they abide by its provisions and “play by the rules of the game”. Carroll suggests that the satisfaction of legal responsibilities is *required* of all corporations seeking to be socially responsible.
- *Ethical responsibility.* This responsibility obliges corporations to do what is right, just and fair, even when they are not obliged to by the legal framework. Carroll argues that ethical responsibilities therefore consist of what is generally *expected* by society over and above economic and legal expectations.
- *Philanthropic responsibility.* The fourth level of CSR looks at the philanthropic responsibilities of corporations. This aspect of CSR addresses a great variety of issues, including things such as charitable donations, the building of recreation facilities for employees and their families, support for local schools, or sponsoring of art and sports events. According to Carroll philanthropic responsibilities are merely *desired* of corporations.

A core debate in CSR is the idea of voluntary initiative by the corporation. This certainly applies in the areas of ethical and philanthropic responsibilities, but would also apply to the first two levels. The underlying rationale of explicitly stating economic and legal “responsibilities” as “requirements” of corporations assumes

that – certainly on a short term basis – corporations have discretion in the way they live up to these responsibilities. Businesses can choose to, or by virtue of neglect, fail to meet responsibilities to the major stakeholders of companies, shareholders and employees.

However, the more familiar face of CSR does not centre on economic obligations to shareholders and employees or obligations to obey the law but to voluntary initiatives, programmes, policies and strategies of corporations to assume responsibilities towards society based on some ethical or philanthropic motivation. A plethora of other definitions and views on CSR have been suggested and discussed over the years but we would argue that Carroll's definition captures probably the lowest common denominator of CSR.

## **CSR in a European Context**

Carroll also sets CSR and the development of related concepts, such as corporate social performance, business ethics, corporate citizenship, in an American context (Carroll, 1999). The corporate world and the academic literature suggest that the notion of corporations adopting CSR policies in order to live up to their “responsible” role in society derives first and predominantly from the United States. Given the recent attention to CSR in Europe this leads us to ask:

- Why has the US been ahead?
- How has it been possible that European corporations could have neglected the important issue of their responsibility to society?
- Why is it that European corporations are only now discovering their responsibilities towards society and are, as it were, catching up?

Our argument is that CSR as a voluntary corporate policy is a fairly recent and still scattered phenomenon in a European context. Corporations in most European countries are adopting CSR policies while the need to address and define a European approach to CSR has been more clearly felt on a political level. This has led the Commission of the European Communities (2001: 6) to define CSR as “a concept whereby companies integrate social and environmental concerns in their business operations and in their interaction with their stakeholders on a voluntary basis”. This echoes the Anglo-American view of CSR. However, the fact the European Commission should make this statement in 2001 does not imply that CSR was previously neglected in Europe.

Table 1 provides some examples of issues, which would be the subject of CSR policies in an American and European context. While there is more granularity at the level of individual firms and countries, our intention here is to make a broad contrast.

**Table 1.** CSR issues in the American and European contexts (examples)

	<b>American Context</b>	<b>European Context</b>
<i>Economic responsibilities</i>	Corporate policies with regard to “good corporate governance”, “remuneration” or “consumer protection”	Legal framework, codifying corporate constitution („Betriebsverfassungsgesetz”), the 35h-week, minimum wage legislation or lengthy and elaborate legislation for developing and testing pharmaceuticals
<i>Legal responsibilities</i>	Relatively low level of legal obligations on business	Relatively high levels of legislation on business activity
<i>Ethical responsibilities</i>	Corporate policies with regard to local communities	High level of taxation in connection with high level of welfare state provision of local public services
<i>Philanthropic responsibilities</i>	Corporate initiatives to sponsor art, culture or fund university education	High level of taxation sees governments as the prime provider of culture, education etc.

We suggest that the key reason CSR has not been discussed to the same extent in Europe as it has been in the US is that the legal framework and institutional fabric in Europe has been inclusive of many of the issues that arise under CSR. These derive from historically different models of trust and authority relations from those that prevail in the more liberal USA. This is captured in Albert’s (1991) vivid conception of the “Rhenish model” of capitalism – a model in which formal institutions integrate and embed the social responsibility of corporations (such as laws, regulation, mandatory requirements) but have also given rise to less formal institutions, values, attitudes, customs or traditions which locate the role of the corporation in society much closer to societal goals and agendas than is found in the American system.

The precise nature of these formal and informal institutions and the drivers behind their development clearly varies among countries. Sweden’s nineteenth century constitutional monarchy always stressed the need for consensus-seeking procedures among the estates and set a ground on which the democracy that emerged in the twentieth century was founded. The German guild tradition informed the habits of employers for over four hundred years through the guild providing apprenticeships for the good of society as well as business. This continues to underpin the German industrial training system. From the early nineteenth century the British parliament developed a regulatory framework and inspectorates to address the most anti-social manifestations of industrialisation – from slavery, to child labour, working conditions, industrial location and pollution.

More recently, while the foundation for European post-war settlements differed between nations, they set much of Europe apart from the USA in terms of today's public policies and private duties. In the post-war UK, a shared desire to avoid the political and social divisions of the 1930s meant that key aspects of Labour's health and welfare reforms were sustained by the Conservatives. The main provision of post-war public housing was under Conservatives. Conservatives and Labour alike developed a tri-partite (government-business-labour) approach to a range of policy issues from prices and incomes policy to education, training and technology. For its part Sweden continued to build on its historic consensus-seeking neo-corporatist approaches to public issues. In West Germany, the imperative of developing a mainstream consensus to isolate fascist and communist groups as a political force resulted in a system of corporate governance, which provided employees with a legal status of equal standing to shareholders. These legal mechanisms in Germany were supported by a consensus mentality and informal institutions which have influenced the discretion of corporations which impact wider society's social and environmental interests and concerns (e.g. Lane, 1989, 1992; Lane, 1994).

Our point is that the social responsibilities of European corporations have been less a matter of their individual discretion than their USA counterparts. The social responsibilities of European business have been played out in a context with more deeply entrenched and embedded relationships between business, society and the state.

In the literature (Whitley, 1997, 1999) we can identify typical areas which constitute national specific elements of a particular national business system which all closely relate to CSR:

- *The role of the state in risk sharing/economic activity*

The involvement of European governments in large and mandatory insurance systems for health, pensions and other social commodities gave rise to pressure on corporations to take over significant responsibility for these issues as a result of mandatory regulation. Governments with stakes as major shareholders or sometimes owners of corporations place issues of social risk at the top-level of corporate concerns. In the US social commodities and risks are a much more discretionary issue. The main impact of government in America is the provision of incentives to employers through negative tax expenditures. Corporations may well provide pension schemes, not as a result of compliance but of calculation of labour market factors, employee relations and CSR profile.

- *Less stronger influence of capital markets*

In credit-based systems of corporate capital sourcing there is an institutionalised propensity of corporations to regard stakeholder claims other than those of shareholders as more legitimate than in market-based systems. For example corporations already seek to safeguard the employment part of their corporate policies and regard it as legitimate to "sacrifice" some degree of profitability to these policy goals.

- *Regulation of labour markets, role of trade unions and industry association*  
A particular area of CSR policies would be the role of employees and the position of labour as a production factor. Many of the firm-based policies, which are described as CSR in America, are redundant in a European institutional setting as it is mandatory for corporations to fulfil such measures.

## Explicit and Implicit CSR – A Definition

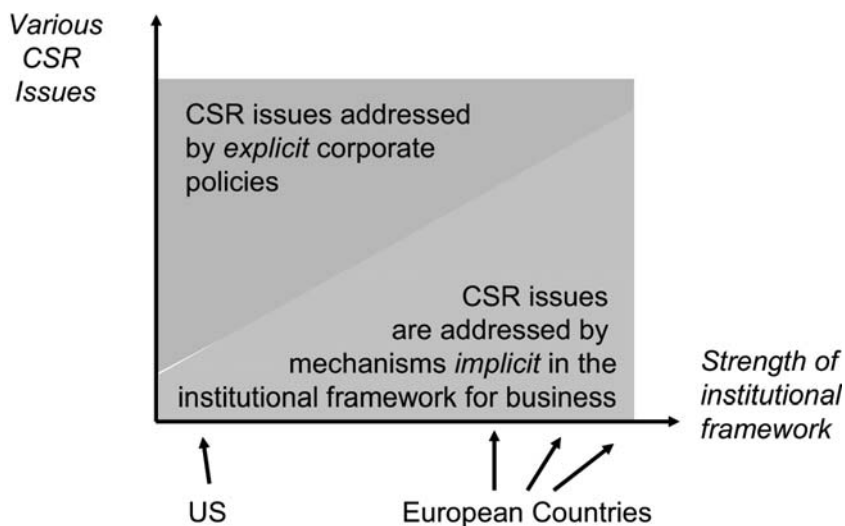
The conclusion of our discussion so far is that CSR as a policy of voluntary engagement to meet the corporation's obligations towards society has not been an overt feature of European economies. Nevertheless, corporations in Europe have participated in activities and policies with a similar orientation not so much on a voluntary basis but as a result of requirements of their social environment, enacted by the institutional framework of business. Moreover, in Europe business associations have normally participated with other social and political actors in the design, review and re-design of such systems. This legitimises the obligations in the eyes of most corporations.

It could be asked why conformance with the law would count as corporate social responsibility? Much of the CSR literature argues that this could not be regarded as CSR as it is not a discretionary activity at the level of the corporation (e.g. Friedman, 1970; McWilliams & Siegel, 2001), notwithstanding the fact that corporations are part of a system which is responsible to society. Yet other authors (e.g. Carroll above) would recognise that business participation in such a regulatory system could be regarded as corporate social responsibility as it entails obedience to the law.

Our analysis of the character and modality of social responsibility in North America and Europe leads us to distinguish between implicit and explicit CSR. We propose the following definitions:

**Explicit CSR** refers to *corporate policies* that lead companies to assume responsibility for some interests of society. Explicit CSR would normally involve voluntary, self-interest driven policies, programmes and strategies of corporations to address issues perceived by the company and/or its stakeholders as part of their social responsibility.

**Implicit CSR** refers to a country's *formal and informal institutions* through which the corporations' responsibility for society's interests are agreed and assigned to corporations. Implicit CSR normally consists of values, norms and rules, which result in (mostly) mandatory requirements for corporations to address issues, which social, political and economic interests consider a proper and reasonable obligation upon corporate actors.



**Fig. 1.** Implicit and explicit CSR

Figure 1 shows how explicit and implicit CSR relate to each other. Implicit and explicit CSR are both approaches to deal with the same kind of issues, namely social issues in the relations of corporations to their stakeholders in the broadest sense. Both types of CSR represent competing approaches and – as the figure indicates – are present in most societies at the same time. The significant difference though lies in which approach assumes dominance. So, for instance in the US, while the general approach seems to be that the majority social issues are dealt with in the form of explicit CSR policies of corporations, there are still significant elements of (implicit) corporate social responsibilities regulated by the legal framework, for instance worker's rights issues and the role of trade unions. Similarly, in Europe, despite a strong emphasis on implicit CSR there is and has always been quite a substantial amount of explicit CSR in the form of philanthropy.

This distinction can be fleshed out further. *Implicit* CSR is embedded in the business-society-government relations within a political system. It may result from strong norms, which all parties recognise and in which all participate. These norms may inform regulation whose legitimacy is confirmed by its democratic context or prevailing approach to policy-making, such as participatory consensus-seeking practices. In these circumstances we would expect strong systems of social capital to grow up around the development and performance of the norms and the regulation.

*Explicit* CSR represents a departure from the more implicit CSR through its special focus on the corporation; the imperatives and drivers for social responsibility acting on corporations; and the tools for social responsibility that corporations can deploy. This special focus on the corporation can be encouraged by: corporations themselves, other business drivers such as public policy and government ideology, business associations and societal representatives.



Our point in making this distinction between implicit and explicit CSR is not simply to enable a better theoretical base for trans-Atlantic comparisons of CSR but also to make sense of the recent evidence of a move toward a more explicit form of CSR in Europe.

## **Evidence of More Explicit CSR in Europe**

There are various factors that have contributed to a shift in the balance between implicit and explicit CSR in Europe toward the explicit. The first is the emergence and growth of CSR business associations or umbrella organisations. At the European level CSR Europe was established in 1996 consisting of 60 member companies and 18 national partner organisations from sixteen different countries. The most prominent and longest standing of the national partners is the British Business in the Community with a membership of over 700 firms accounting for 20 % of the national private sector employment mainly based in the UK.

Secondly, there is a wide range of other organisations that have grown up around the theme of CSR. These include CSR “vanguard” organisations, which are dedicated to raising standards of corporate practice. There is also an emerging industry of CSR consultants who work to assist corporations with their CSR policies, stakeholder relations and CSR reporting (Fernandez Young, Moon & Young, 2003). Some of these are general consultants who have developed a CSR portfolio whereas others are dedicated entirely to CSR. Yet other organisations have come into operation to provide services to the CSR industry such as conferences and newsletters.

Thirdly, CSR has a more explicit status within companies, particularly in the form of dedicated board level responsibilities, senior managers, CSR professionals, organisational sections, processes, codes, programmes and budgets. Companies are increasingly likely to report their CSR policies and position within their annual reports, in freestanding reports or in their general corporate communications.

CSR is also the subject of increasing attention outside companies and the CSR organisations. Concern about CSR has now increased in the investment community with the growth of socially responsible investment funds, particularly in the UK but also in many other European countries. CSR has become a subject of increasing media attention, both as exposure to poor performance and also in the call for better and more explicit standards. In business education CSR appears to have a significantly more explicit profile in European universities and business schools, with new centres and dedicated teaching and research programmes (Matten & Moon, 2004). Finally, CSR is increasingly a concern of governments who are deploying various means encouraging companies to raise their CSR standards at home and abroad. This is specifically true of the European Union which has contributed to the debate on CSR in various documents and initiatives (e.g. Commission of the European Communities, 2001, 2002).

## Why Explicit CSR in Europe?

The earlier discussion identifies the trend toward a more explicit CSR in Europe but it does not really explain the shift from implicit to more explicit CSR.

We hypothesise that this shift could be expected to result from some disjuncture in the wider system of social governance or national business system resulting from government/governance failures, new market imperatives or new social demands. In practice these conceptualisations are usually related, but for present purposes it helps to distinguish them.

The most dramatic example of government or institutional failure is where there is a complete breakdown of systems of societal governance, as was the case in the former Eastern Europe. In these circumstances, new systems emerge although their development is necessarily slow and tentative, especially in the absence of the sort of social capital predicated upon a well established civil society and longstanding habits of business responsibility which many of these systems face. However, explicit CSR may prove one among a range of governance solutions here and there is evidence that this is the case in Poland, Hungary and the Czech Republic (coincidentally countries which retained some vestiges of civil society through the periods of communism).

For all their well-established governance systems, even the west European countries can face deficits in governance. Perhaps the most dramatic has been the case of mass unemployment, urban unrest and fiscal stress experienced in the UK in the late 1970s and early 1980s. This is more or less the case for most Western European countries where corporate decisions on downsizing, relocation and mechanisation of production processes have been met by heated debate on the responsibility of corporations for a particular town, region or country. Interestingly, in the case of Denmark, record levels of unemployment and dependency on government in the 1990s prompted the Social Democratic Minister for Social Affairs to encourage various forms of CSR alongside government responses (Jespersen, 2003). In a similar vein, there is a broad literature arguing that corporations have increasingly stepped into a “sub political” (Beck, 1997) role in the area of environmental (in the sense of ecological) issues as governments have blatantly failed to avoid or handle the undesired side-effects of an energy intensive form of production and consumption (e.g. global warming, nuclear power), new technologies (e.g. GM food) or scandals (e.g. mad cow disease), just to name a few examples (Matten, 2004).

Similarly, new market imperatives may prompt business to adopt a more explicit CSR. At the most basic level the new imperative may concern the social licence of business to operate. Again, this was clearly articulated in the context of the UK governance crisis alluded to above. As *The Economist* commented of Marks & Spencer’s expenditure on community work and charity, the firm was “making a sensible investment in its market place. If urban disorders become a regular fact of life, many of its 260 stores would not survive.” (20.2.1982)

Another motivation for business may concern the perceived threat of new and unwelcome regulation. This was expressed by the leading UK business association, the Confederation of British Industry, in the context of the UK governance crisis: “companies fear that if they make no attempt to find solutions to community problems, the government may increasingly take on the responsibility itself. This might prove costly to employers both in terms of new obligations and greater intervention in the labour market. Many companies prefer to be one step ahead of government legislation or intervention, to anticipate social pressures themselves and hence be able to develop their own policies in response to them” (CBI 1981 quoted in Moon, 2004b).

Another relevant market imperative may be the growing importance of financial markets for business success. In this context explicit CSR may be regarded as a prerequisite for attracting global capital and the more European companies source their capital globally the more they have to comply with the requirements of international investors, particularly in the US. In a similar vein, CSR has been encouraged by a particular group of investors which integrate social and ethical criteria into their rationale, leading to developments such as the Dow Jones Sustainability Index or, in Europe, the FTSE4Good index (further reasons for an increase in CSR in Europe are discussed by Crane & Matten, 2004b).

## **Specifics of Explicit CSR in Europe**

Though we argue that explicit CSR is gaining momentum in Europe and as such can be seen as part of a growing evidence about a potential Anglo-Saxonisation of European businesses (Mayer & Whittington, 2002) there are, however, distinctly European features in the CSR engagement of European companies. Traditionally, the key issues in business-society relations have been played out around the question of the roles and the rights of employees. During the 1970s and 1980s, however, green issues and environmental protection became a key political issue in Europe and entered the business agenda relatively early. So, for instance in Germany, the first textbook for environmental management education in business schools was published already in 1980 (Strebel, 1980). Though the issues quickly became part of the “implicit” framework for CSR, the styles and approaches in tackling green issues in European societies remain distinct, most notably from the USA (Lofstedt & Vogel, 2001). This particularly applies to “new” issues such as genetic engineering, BSE and other risk related issues (Levidov & Carr, 2000; Wynne & Dressel, 2001). A recent manifestation of these changes became visible in the decision of Shell and BP to leave the Global Climate Coalition, a group of mainly American oil companies, set up to lobby against the implementation of the Kyoto Protocol and other measures of environmental protection (Levy & Egan, 2000; Levy & Kolk, 2002).

While we stressed the importance of implicit elements in the CSR framework in Europe one might also argue that part of the explicit CSR activities of companies consists in an active participation in changing and innovating the negotiated

legal framework. In contrast to the US, where lobbying would be the key “weapon of choice” for corporations (McGrath, 2002) many European corporations have become active and key players in various efforts of self-regulation, reflexive regulation and other regulatory efforts (Orts & Deketelaere, 2001). On the other hand, European corporations are less inclined to engage in philanthropy than their North American counterparts (Palazzo, 2002). The most consistent explanation for this could be the fact that in Europe, relatively high levels of taxation in conjunction with a somewhat more developed welfare state infrastructure causes corporations to perceive issues such as funding of education or arts as being more in the responsibility of governments.

Interesting differences also seem to emerge in the field of actors in CSR in Europe. Next to corporations, CSR activities seem to be embedded in multistakeholder coalitions including trade unions<sup>4</sup>, business associations<sup>5</sup> and NGOs<sup>6</sup>. One finding of Maignan and Ralston’s (2002) comparison of US and European CSR is the greater preponderance of the European corporations to describe their CSR in stakeholder terms.

Most significantly, however, is the role of the government in European CSR. Although by conventional definition, CSR is regarded as incompatible with governmental regulation, explicit CSR as defined above in Europe is a key issue for regulators. The general approach seems to facilitate a new trend in business and encourage companies to assume more responsibilities, as most welfare states in Europe are increasingly facing limits to their capacities of tackling social issues in the way they traditionally did. This political activity can be observed on all levels: There are significant efforts by the European Commission, both in terms of funded projects as well as Green Papers and other publications with the intent of defining and shaping CSR in a European context (Commission of the European Communities, 2001, 2002). On the national level, many governments have attempted to shape the CSR debate, most notably and advanced in the UK, which even has a governmental minister for CSR (Moon, 2004a). Even on the sub-national level, there is meanwhile quite a number of governmental initiatives on a local and regional level to facilitate CSR and encourage corporate involvement in society<sup>7</sup>. Apart from these initiatives as a key actor in promoting explicit CSR in Europe, government still plays a significant role implicitly as they are deeply embedded in

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<sup>4</sup> An example are the activities of the European Trade Union EUROCADRES which has recently actively encouraged CSR as a trade union topic in its member organisations across Europe, see [www.eurocadres.org](http://www.eurocadres.org).

<sup>5</sup> A prominent and longstanding organisation is the British „Business in the Community” (BITC), which facilitates a plethora of CSR activities by corporations, see [www.bitc.org.uk](http://www.bitc.org.uk).

<sup>6</sup> For examples see Bendell. Bendell, J. (ed.). 2000. *Terms for endearment: business, NGOs and sustainable development*. Sheffield: Greenleaf.

<sup>7</sup> As example see the initiative of the regional government of the province of North-Rhine Westphalia at [www.corporate-citizenship.nrw.de](http://www.corporate-citizenship.nrw.de).

economic activities of business. So, for instance, governments in Germany, France or Italy directly intervene with credits, subsidies and other measures in corporations, particularly if there is the risk of mass lay-offs. Furthermore, governments still tend to own substantial amounts of shares in large European companies, Renault and Volkswagen perhaps being the most prominent examples. Consequently, governmental influence on the corporate attitudes towards social responsibility also remains implicitly strong notwithstanding the new interest in explicit CSR.

## **Implicit and Explicit CSR: Towards a New Research Agenda**

We argue that a dual view of CSR as consisting of implicit and explicit elements does not only offer a better descriptive model of CSR but that this approach also opens the way to a more theorised research agenda in CSR.

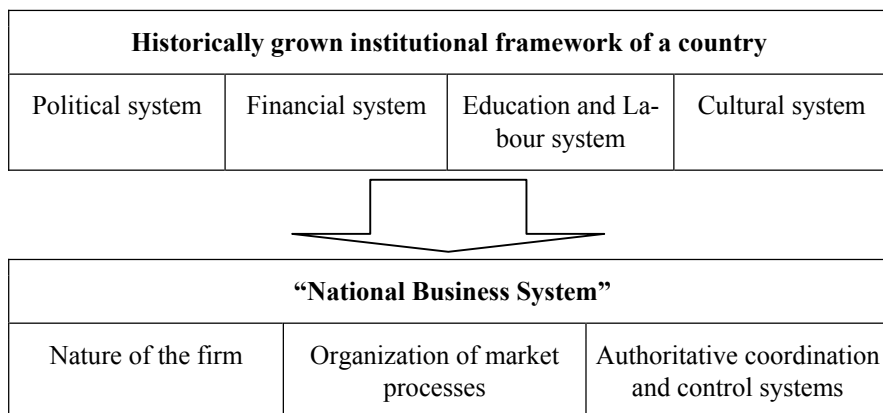
In particular, contemporary European and American institutional theory sheds an interesting light on the global spread of CSR and its societal contexts beyond its American origins. It enables us to frame CSR as a research topic in a broader context of inquiry which is currently on the agenda in organisation studies as well as international management (Tempel & Walgenbach, 2005). On the one hand, explicit CSR is part of a broader movement of the global spread of management concepts, ideologies and technologies which mostly result in some sort of “Americanisation” of management practices. On the other hand, implicit CSR is part of the institutional framework of countries’ regions and thus is considerably different from country to country. This debate about the convergence and divergence of management practice has been on the agenda in business studies for quite some time (Child, 2000), in particular in a European context (Geppert, Matten & Williams, 2002), and we would suggest institutional theories as the most propitious framework to explain “implicit” and “explicit” CSR.

## **Implicit CSR and the National Business Systems Approach**

Starting with implicit CSR we would argue that its occurrence, forms and specific national differences can be explained by perspectives discussed for more than 30 years in the “national business systems” or “societal effect” approach (Maurice & Sorge, 2000; Maurice, Sorge & Warner, 1980; Sorge, 1991; Whitley, 1992, 1999, 2002a, 2002b). The basic theoretical construct of this perspective is depicted in Figure 2.

European institutionalists, as this school of research is sometimes referred to, argue that every country has a specific, historically grown institutional framework which shapes and constitutes what they call a “national business system” (Whitley, 1997) or “social system of production” (Hollingsworth & Boyer, 1997). We argue

that this national business system (NBS) precisely encapsulates the underpinnings of what we termed “implicit CSR” earlier on in this paper. Let us have a look at some examples, analysing Whitley’s three key areas of NBSs:



(based on Whitley 1992, 2002)

**Fig. 2.** Key elements of national business systems

- *Nature of the firm*: this aspect focuses primarily on forms of ownership coordination in an economy. While Anglo-Saxon countries tend to rely more on market based forms of contract based ownership, continental European countries still have a large amount of direct ownership or alliance ownership, most notably through networks of banks, insurance companies or even governmental actors. It is evident, that the nature of the firms then directly impacts on various CSR issues, such as the role of stakeholders beyond shareholders, the mechanisms of corporate governance, the accountability of corporations to wider constituencies etc.
- *Organisation of market processes*: a decisive feature of a NBS is how the economic relations between actors are organised and which coordination measures an economy prefers, the two extremes here being markets and alliances. The way these relations are organised touches on a significant number of CSR issues, such as consumer protection, product stewardship, liability for production and products, labour issues.
- *Authoritative coordination and control systems*: NBSs differ considerably in the way: employer-employee relations are organised and to which degree delegation takes place; trust governs relationships; and the discretion in the task environment granted to employees. Again, a large amount of CSR policies focuses on these issues and we would argue that the implicit framework of European CSR covers a significant number of issues which would be part of explicit CSR policies in different NBSs.

These elements of the NBS are shaped by political, financial, educational and cultural institutions, and as these institutions differ from country to country, NBSs also differ cross nationally. As we contend, that „implicit” elements of CSR are embedded in and part of the NBS, we argue that differences in what CSR actually means differ from country to country: implicit CSR, such as industrial relations, labour law or governance legislation are different from country to country which not only makes implicit CSR different cross-nationally but also the shape of explicit CSR policies: while, for instance, employee participation in corporate governance might be part of the explicit CSR policies of an American corporation, a German CSR policy would not have to address these issues as they are already predisposed by the (implicit) institutional framework of the NBS.

We suggest the NBS-approach also because it looks back on quite a rich tradition particularly in Europe (Whitley, 1992; Whitley & Kristensen, 1996, 1997), but increasingly so also in other parts of the world (Choi, Hilton & Millar, 2004). The research in this area is particularly rich in the field of comparing continental European NBSs with Anglo-Saxon versions (Lane, 1989; Sorge & Warner, 1986) which provides a fruitful basis for the analysis of (explicit) CSR as a predominantly Anglo-Saxon concept being applied increasingly in Europe. Furthermore, one of the key arguments of this school of research is that despite ongoing processes of globalisation in the sense of harmonisation and standardisation of management processes and structures, NBSs still remain distinctly different, and thus stress what empirically has been result of many studies in the area of CSR so far, that Europe (as compared to other continents) as well as different countries within Europe, provides a rather diverse picture of CSR challenges, practices and policies.

## **Explicit CSR and Institutional Legitimacy**

On the other hand, as we have argued above, there is ample evidence that CSR in the “explicit” sense is gaining momentum and spreading all over Europe (and beyond). We would suggest that the theoretical approach of “new” or “American” institutionalism (DiMaggio & Powell, 1983; Meyer, 2000; Meyer & Rowan, 1977) provides a helpful theoretical perspective on the understanding of these processes. The central focus of this school of institutionalism has been to analyse how homogenisation of institutional environments across national boundaries takes place and how regulative, normative and cognitive processes lead to more and more standardised and rationalised practices in organisations across industries and national boundaries. We would argue that new institutionalism helps to understand why and how explicit CSR is gaining momentum as a new management element or concept. The key argument of this theoretical school is that organisational practices change and become institutionalised because they are considered as legitimate. Legitimacy – as opposed to economic efficiency for instance – is regarded as the key driver of institutionalisation. This legitimacy is “produced” by three key elements or processes (DiMaggio & Powell, 1983):

- *Coercive isomorphisms*: externally codified rules, norms or laws assign legitimacy to practices. In the case of CSR in Europe one could argue that governmental initiatives, such as EU Green Papers, or the initiatives of the UK Department of Trade and Industry count among those coercive isomorphisms which foster the spread of CSR across Europe. Similarly, self-regulatory and voluntary initiatives which refer to codes and norms could be counted among these isomorphisms. So, for instance, various codes of conducts for multinational corporations issued by bodies such as the UN, the OECD, the ILO and others can be counted among drivers of CSR, certainly for MNCs, in Europe. Also the compliance with certain environmental standards, such as ISO 14000 or the EMAS scheme – often supply chain driven – coerce companies to adopt particular CSR policies. An increasingly important role here is also played by the socially responsible investment community. Indexes such as the FTSE4GOOD or the decision criteria of certain investment funds play a similar role for corporations if they want to gain or sustain access to these sources of capital. Most recently, the UN Global Compact could be seen as another driver of explicit CSR as it also externally codifies some fundamental basics of responsible corporate behaviour. However, as the membership of the UNGC is voluntary there is another element leading to legitimacy to be considered:
- *Mimetic processes*: in a business climate of increased uncertainty and increasingly complex technologies managers tend to consider certain practices as legitimate just because they are considered to be “best practice” in other parts of the organisational field. These processes would also account for the upcoming of “management fashions”, such as the recent wave of “business re-engineering”. In the area of CSR, particularly in large European MNCs, this can certainly be considered an important driver for CSR. Regular CSR reports – often in the form of “corporate citizenship” or “sustainability” reports – or flagship projects in the area of philanthropy could be considered as prominent examples here.
- *Normative pressures*: a particular role has been identified for educational and professional authorities which directly or indirectly set standards for “legitimate” organisational practices. A particular role has been identified for educational institutions, in particular for the degree of an MBA which increasingly becomes the standard formal education for decision makers in most companies in the industrialised world. With regard to CSR and its spread in Europe, we can certainly identify some significant rise of pressures from this angle. Not only have global initiatives such as for instance the “global business coalition against AIDS” or other initiatives in connection with the World Economic Forum recently encouraged CSR for its member organisation. In particular in Europe, with the foundation of the “European Academy of Business in Society (EABiS)” in 2002, or similar initiatives at national level, a growing number of professional associations



exert normative pressures on business to adopt CSR. Furthermore, as recent research among the 166 leading business schools or institutions for higher education in business has surfaced, CSR is now at least an optional, in many cases a compulsory part of business education (Matten & Moon, 2004).

This particular theoretical angle has quite a rich tradition in management research and also in particular in CSR related topics. In the area of environmental management practices there is a rich stream of research which has analysed the spread of more environmentally friendly corporate practices through the lens of new institutional theory (Hoffman, 2001; Hoffman & Ventresca, 2002). We would argue, that this lens is also particularly proficient and helpful in understanding explicit CSR in a European context.

## Conclusion

This paper has sought to identify CSR as a complex social and business phenomenon, which depends on more dimensions than just voluntary corporate policies. We argue that CSR is increasingly focusing on problems, which are tackled by a broader plethora of actors than companies and business interests. Our conceptualisation would then lead us to argue that the transfer of CSR out of the Anglo-American context unveils that voluntary corporate policies are just one among several ways of addressing social issues and problems in the relation of business and society.

This view leads to a number of consequences: First, it reassesses the societal context of corporate CSR policies and opens the circle of potential actors in CSR beyond the corporate sphere. Secondly, it has some provocative policy implications as it presents CSR as a phenomenon, which can either be tackled by corporations or by other institutions, most notably governments. Thirdly, the differentiation into CSR as a more multifaceted phenomenon entails a number of challenges for research in CSR, both on the level of theoretical conceptualisations as well as research agendas on the empirical level.

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# Corporate Social Responsibility at Volkswagen Group

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Corporate Social Responsibility (CSR) consists in a company reconciling its economic aims with sustainable growth and human progress. Although every company has its own unique approach to value-oriented corporate management, this approach is usually based on established concepts. These concepts of corporate citizenship or corporate social responsibility emphasize a company's willingness to assume social responsibility, and include components such as its attitude towards human rights, the needs of its employees and suppliers, and commitment to social issues.

Volkswagen's CSR philosophy is that increasing corporate value is the only way to achieve social responsibility and that, conversely, sustainable corporate success can only be safeguarded by social responsibility. This is the reason why the Volkswagen Group implements at each of its sites developmental processes whose objective is to attain sustainable ecological and social benefits for the company and society at large. These ethical and social principles are applied throughout the entire Volkswagen Group, which sees itself as a global player with German roots.

The following will illustrate the fundamental principles of the Volkswagen Group's CSR activities and show how these principles combine tradition with a forward-looking approach and serve as a benchmark for a long-term corporate policy.

## The Pillars of Volkswagen's CSR Strategy

Volkswagen has always seen one of the pillars of its corporate culture to be assuming social responsibility in all areas where the company is active. Of course, this philosophy is not restricted to welfare provisions or sponsoring activities. Today a company can only act in a socially responsible manner if it actively secures jobs, trains its workers and includes them in the process of shaping the company's future.

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## Workholder Value

In order to safeguard existing jobs in Germany Volkswagen has developed measures to allow it to react flexibly to production fluctuations. Employment schemes such as flexible working time, Auto 5000 and the AutoVision concept have played a major role in attaining this aim. The term Volkswagen uses to describe all these flexibility measures is the “breathing factory”. Many of these flexibility instruments have since been implemented at international Volkswagen sites and adapted to local conditions. Thus all sites have flexible tools at their disposal that allow them to “breathe” during fluctuations in plant utilization and to avoid the need to make forced redundancies. Around 95 percent of the Group’s global workforce is covered by collective bargaining agreements. Our Sustainability Agreement in Germany – concluded for around 100,000 workers in 2004 – is a milestone on the road to lower costs and increased flexibility. It envisages pay freezes and adjusted labor agreement models for new employees, and in return ensures that there will be no cuts to the workforce until 2011. Furthermore, since 1997 the company has allowed employees in Germany to invest components of their wages or overtime in “time asset bonds”, as they are called, which will be invested in the capital market. The concept of “demographic working time” gives employees the flexibility to shape their retirement based on the time asset bonds they have saved on their lifetime accounts. The Sustainability Agreement strengthens this scheme, as it allows a percentage of overtime hours to be transformed into time asset bonds.

Yet it is not the flexibility of the employees alone that is a major factor in corporate success: their level of training also plays a key role. In order to attract and keep competent and highly motivated employees within the company, a company needs to foster a corporate culture that is based around success and performance. The development of the workforce is strongly focused on the requirements of the employees’ ongoing employability and supports models for lifelong learning – a measure that is primarily a response to the demographic changes in Europe’s highly industrialized countries that have been brought about by increasing life expectancy and falling birth rates. Changes in the structure of society will have an impact on the corporate sector too, and will require it to adapt to the gradual changes in balance of generations in society. One problem is the growing number of older employees who face the prospect of a higher retirement age, coupled with a lack of qualified younger employees in the mid-term.

In the near future the average age of the workforce is set to rise and Volkswagen’s common practice of early retirement will most likely no longer be tenable in the long term due to legal changes. In this situation the main objective is to take leave of the prejudice that an aging workforce means a drop in performance. Older employees not only have a wealth of experience at their disposal, but can work hard and are rarely ill. Yet to maintain their employability, their tasks have to be adapted to their particular needs. This includes extending health care and developing models of working hours that are suitable for older employees. Thus the wide range of healthcare schemes that the Group’s companies offer and the ongoing

training based on Volkswagen's philosophy of 'lifelong learning' provided by Volkswagen Coaching<sup>2</sup> are all becoming increasingly important. Youth training schemes are operated at all sites and adapted to local conditions by the individual companies. Volkswagen Coaching provides hands-on training based on the concept of tailoring training to business and production processes: in 2005 4,462 young people underwent training in 27 professions at Volkswagen's German sites.

If a company wants to ensure lifelong employability, it has to support not only expertise and skills but also the compatibility of family and working life. Volkswagen offers a range of part-time work schemes in both the production and service sectors. Various shift schemes give single parents the opportunity to tailor their work better to their needs and those of their family. For example, employees can take up to eight years parental leave over the legally stipulated period of time with a guarantee of a job to return to. Additionally, Volkswagen has cooperation agreements with childcare support bodies at its production sites that can organize nursery or kindergarten places. Employees who return to the company after parental leave can also attend courses on family management.

Equal opportunities regardless of sex, age, origins or religion are a basic right for all employees that is set down in our Social Charta. In accordance with the corporate agreement on "Cooperative Behavior at the Workplace", sexual harassment, and all forms of persecution and discrimination are considered an offence against human dignity and lead to severe penalties. Volkswagen has supported equal opportunities for men and women since the mid-1980s. The Women's Advancement Department in the Group's Personnel Section and the women's representatives on site offer a range of schemes such as mentoring for female high potentials, the creation of networks, and measures to increase the number of women in technical professions and management. The principles of the Social Charta are also applied to Volkswagen's suppliers, forbidding all forms of forced and child labor. Minimum social standards apply to activities at all levels and form the basis for Volkswagen's ongoing efforts to find solutions for new challenges. The explicit aim of the employees' protection policy, passed in 2004 and implemented throughout the world, is to safeguard and if possible improve the health, performance and job satisfaction of employees. Special guidelines have been drawn up on the key issue of health protection with a clear focus on preventative measures. They range from the prevention of back problems and cancer screening to the prevention of HIV / Aids in Brazil and South Africa. Together with the International Labor Organization (ILO) and the Society for Technical Cooperation (GTZ) Volkswagen plans to support safety and health protection measures in its supplier companies in developing countries.

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<sup>2</sup> Volkswagen Coaching GmbH employs around 900 staff and provides services on the free market for the ongoing training and development of the Volkswagen management. In 2004 it conducted around 4,100 training courses for approximately 36,000 participants at its sites in Wolfsburg, Hannover, Braunschweig, Kassel, Emden, Salzgitter, Zwickau, Chemnitz and Dresden.



## The Opportunities of Globalization

The consequences of globalization, a process which has increasingly gained pace since the early 1990s, can be seen in many areas of life, not just in the world of business. In Europe the public mainly sees globalization as a threat, as most people associate it with increased competition and job losses. They accuse corporate global players of arbitrarily their production sites at will to any countries where workers are particularly cheap and where environmental regulations are lax. This distorted picture conflicts with the hopes of the people in newly industrializing and developing countries, who are eager for better opportunities to develop and participate in global wealth. For the Volkswagen Group, globalization is more than just part of the framework for sustainable business activities. We are convinced that the international division of labor, coupled with free access to markets in industrialized, newly industrializing and developing countries, will encourage growth and wealth. For this reason the Volkswagen Group took a pioneering role among automotive companies, being one of the first to drive on its own internationalization process – whether in Latin America, where it has been producing for 50 years, in South Africa, Asia or Eastern Europe. Yet this revolutionary role was always coupled with the duty to take the lead in ensuring environmental protection and social awareness, and thus to contribute to creating responsible globalization.

Thus Volkswagen was one of the first companies to draw up binding principles to protect the environment and resources in its Environmental Policy Statement of May 1995. Since 2002 all production sites across the globe have been subject to eleven environmental standards. In 2002 the “Corporate Declaration on Social Rights and Industrial Relations” set internationally valid standards securing employees’ interests – breaking new ground within the automotive industry. The company-wide Health and Safety Policy implemented in 2004 added principles and duties in the field of work safety to the global strategic framework.

## Partnerships for Sustainability

Global challenges can only be tackled by companies, governments and people in unison. The current debate is focused on rethinking the responsibilities of the private and public sectors. Yet a key role is played by the consumer, who can use the power of the purchasing decisions they make on a daily basis. This is why Volkswagen seeks to engage in a dialogue and indeed debate with all partners who can help to contribute to creating sustainable mobility.

As an automotive company, it is our duty to face the criticisms put forward by non-governmental organizations (NGOs), who have been calling for models with even lower fuel consumption and new fuel technologies. Clearly, given the good will of both parties, a constructive dialogue is indeed possible, as is shown by Volkswagen’s cooperation with the German Nature Conservation Association (NABU), which offers jointly-held courses on fuel-saving measures. Volkswagen

is also engaged in a critical and productive exchange of ideas with the German Association for the Environment and Nature Conservation (BUND) in Lower Saxony, the Öko-Institut e. V., and similar institutions.

Volkswagen is also an active member of national and international dialogue forums. As a founding member of the World Business Council for Sustainable Development (WBCSD), the company is involved in the joint Sustainable Mobility project initiated in 2004.<sup>3</sup> The car manufacturers, oil companies and car parts suppliers that are participating in the project are developing a joint vision and a range of options for worldwide mobility in the year 2030. During the project, discussions were held with stakeholders at locations all over the world, including Tokyo, Beijing, Manila, São Paulo, New Delhi and Washington. The Volkswagen Group also participates in the Mobility Forum of the United Nations Environment Program (UNEP), a forum for exchanging experience and joint learning. One result of this project was the “Automotive Supplement” to the Global Reporting Initiative (GRI), which sets down indicators for sustainability reporting in the automotive sector. Volkswagen is also a founding member of the corporate initiative Corporate Social Responsibility Europe (CSR Europe)<sup>4</sup> and of “econsense”<sup>5</sup>, the sustainability

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<sup>3</sup> The World Business Council for Sustainable Development (WBCSD) was founded in 1992 as a result of the union of the Business Council for Sustainable Development (BCSD) in Geneva and the World Industry Council for the Environment (WICE) in Paris. The WBCSD sees itself as a pioneer and catalyst on the road to sustainable development. It aims to push forward the role of eco-efficiency, innovation and corporate social responsibility by building on the results of the Rio summit and Agenda 21. Its work is based on the view that future development must be designed to ensure that economic, ecological and social objectives are given equal priority. Achieving this aim requires strengthening the cooperation between business, government and NGOs.

The WBCSD is the oldest and politically most influential alliance of multinational companies at an international level to subscribe to the concept of sustainable development. For some time the network has grown beyond being a platform for learning and dialogue into a facilitator for joint projects (e.g. Sustainable Mobility 2030, Greenhouse Gas Protocol, Energy and Climate Change – Facts and Trends 2050, Global Road Safety).

<sup>4</sup> The European Business Network for Social Cohesion, the predecessor of CSR Europe, was founded in 1995 in the wake of the European Manifesto against Social Exclusion on the initiative of the then President of the European Commission, Jacques Delors. CSR Europe is based in Brussels and has more than 60 companies and 18 state partner organizations as members, a number which continues to grow. With these partner organizations it forms a network of more than 1000 companies in Europe. The only German members are Volkswagen – a founding member – and BASF.

CSR Europe sees itself as a business-to-business network for the support of corporate social responsibility at a European level. CSR Europe sees its task as supporting its members in integrating CSR into their corporate strategy in order to foster „sustainable growth” and „humane, innovative progress”.

<sup>5</sup> Econsense was founded in July 2000 on the initiative of the Federation of German Industries (BDI) by representatives of leading German companies and economic organizations that are active at a national and global level. One of the main reasons for its forma-

forum of the German corporate sector. Both initiatives focus primarily on exchanging experience between the participating companies and on leading an active dialogue with stakeholders. Volkswagen also joined the Global Compact following the Global Conference on Sustainable Development in Johannesburg in 2002.<sup>6</sup>

## Local Roots

Wherever the Volkswagen Group is active, be it in Germany, Brazil or China, it plays a major role not only as an employer but also for infrastructure and regional development. A site with 20,000 workers indirectly employs at least as many workers again elsewhere – at suppliers and in infrastructural facilities such as schools, public transport, commerce, public administration and catering. This comes hand in hand with great social responsibility for these areas, a responsibility which is fulfilled by providing above-average working conditions and payment, contributions to local structural development and the transfer of modern technologies and processes throughout the Volkswagen Group. One important aspect of long-term corporate management is respect for international legal norms. In industrialized countries this is a self-evident duty, but in developing regions it presents even more of a challenge. Economic efficiency can only flourish where human rights and laws are respected. Volkswagen was one of the first companies

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tion was the founders' desire for sustainable development to no longer be the responsibility of politics and NGOs and to bring the topic to the attention of the private sector in an attempt to improve the public debate. Their aim is also to break up the coupling of sustainability and environmental within the „Triple Bottom Line” paradigm (the economy – environment – society).

Econsense published an extensive dialogue paper (2003) containing fundamental positions on the entire range of issues within the sustainability debate, as well as a „CSR-Memorandum” (2004) and an IPP status paper on „Product responsibility in the 21<sup>st</sup> century” (2005).

<sup>6</sup> The notion of the „Global Compact” was presented by the General Secretary of the UN, Kofi Annan, in 1999 on the occasion of the World Economic Forum in Davos. The concept envisages that companies should directly assume responsibility for the application and implementation of international law and governance. The Global Compact was founded in July 2000 in New York, and involves managers from around 50 international companies and representatives of employees, human rights, environmental and developmental organizations.

The participating companies have committed themselves to implement ten principles from the fields of human rights, employment and the environment. The comprehensive approach behind the principle aims to help the private sector to reduce the complexity of their strategies and organizational instruments, and to establish a global orientation framework at a UN level. The members are obliged to report on their activities in annual reports and other publications, and to publish progress reports documenting the implementation of the principles. Volkswagen regularly reports on the activities of the UN initiative in the political news magazine p:news and operates the internet site [www.globalcompact.org](http://www.globalcompact.org).

to support the move towards a democratic society in South Africa in the 1970s by recognizing non-racist trade unions and training young blacks. At an early stage it saw the opportunities globalization held for development. From the very beginning Volkswagen complied to international guidelines that aim to raise ecological and social standards in newly industrializing and developing countries. The benchmarks that Volkswagen uses for these efforts are the OECD guidelines for multinational companies and the ILO standards, even if regional norms do not guarantee this level of protection. Volkswagen once again took on a pioneering role in the negotiations with the International Metalworkers' Federation and Volkswagen's Global Group Employees' Committee – a body the company had created on a voluntary basis – in establishing the Group Regulations on Social Rights and Industrial Relations (2002) and the Work Safety Policy (2004).

A particularly noteworthy local responsibility scheme is Wolfsburg AG (WOB AG), a public-private partnership between the Volkswagen Group and the city of Wolfsburg which has implemented the AutoVision concept since it was established in 1999. Its aim is to strengthen the regions' long-term economic power and to open up new employment perspectives. The main activities of WOB AG include attracting suppliers, supporting start-up companies, expanding the service sector, and supporting its job agency and the Sustainability and Business Network. This network aims to open up potentials in the field of the closed-loop economy faced with the challenge of dwindling energy resources and the problem of waste disposal. Since April 2003 it has also dealt with the topic of sustainability. For WOB AG the main focus is to use innovation to create and sustain employment. By the end of 2004, around 8,000 new jobs had been created in Wolfsburg.

## Transparency and Fairness

Responsible and transparent corporate management is essential for stable long-term development. Volkswagen predominantly bases its transparency measures on the German Corporate Governance Codex. In Germany the executive board is advised by a competent and independent supervisory board to ensure transparent management. The supervisory board is informed about economic developments, corporate planning and risks in at least two sessions a year. In accordance with the German Co-Determination Law, it consists of equal numbers of representatives of both shareholders and employees. Transparent corporate practice also includes proactive measures against corruption and attempted bribery.

### Transparency

Large companies are often criticized for influencing legislation through lobbying activities. Yet it is legitimate and often necessary to communicate the expertise bundled in the company to the sphere of politics and public administration and to

bring corporate experience into the process of creating a socially responsible framework for the private sector. Of course, this must take place in an open and accountable manner. As an active member of civil society, the Volkswagen Group complies with the national environmental and social laws at all of its sites. Indeed, by transferring technology and processes, it often goes far beyond the legally required standards.

CSR reporting is legally required to a certain degree in countries such as France and Italy, but as yet is not based on standardized criteria. There has been wide support for the Global Reporting Initiative (GRI), but as yet it has not been made binding. The question of whether a regulation will come into force on this matter is still open. An ISO standardization process has since been implemented which will hopefully lead to the creation of guidelines. Interestingly, more and more consumer protection organizations have begun to investigate the sustainability criteria and the CSR performance of products and the companies that produce them. At present this has had little impact on the market, but the development is a noteworthy one. Both the conventions of the International Labor Organization (ILO) and the "Guidelines for Multinational Companies" of the Organization for Economic Co-operation and Development (OECD) are presently considered to be binding. In addition, all sites implement the Environmental Management Norm 14001 of the International Organization for Standardization (ISO) and the European Eco-Management and Audit Scheme (EMAS). Almost all of the Volkswagen Group's production sites are audited according to these regulations and have an externally recognized eco-management system; this is set to be implemented throughout the whole Group by the end of 2006.

In December 2005 the first company-wide sustainability report was presented. In drawing up the sustainability report the Volkswagen group followed the guidelines of the Global Reporting Initiative (GRI) to ensure comparability. An accredited external expert was commissioned to check that the report was complete and consistent, and to list its strengths and weaknesses. The auditor's assessment is included in the report. This company sustainability report is complemented by reports and internet portals published by the individual Volkswagen brands and companies. The internet portal of the Volkswagen brand now carries on year-long tradition of publishing the Volkswagen Environmental Report. Specific information on plants, models and environmental data can now only be found in the internet. By moving to an internet publication, the Volkswagen group gives its sustainability report a higher profile and in years to come will focus more on the interlinking of print and online media. Additionally, the company also informs the public via a specially created sustainability portal, and a range of brochures and newsletters.

## Ombudsman System

Corruption is not a trivial matter; it damages the company and its employees. Corruption occurs when someone uses his position in the company to his own advantage or to the advantage of a third party, or misuses it to the detriment of the com-

pany. This has negative consequences for both the employee and the company. For the employee corruption leads to even more corruption until the employee and his business partners are caught in a net of mutual dependency that continually damages the company. The legal penalties for corruption in business matters are regulated by the German Penal Code. Accepting bribes, for instance, can lead to a prison sentence of up to five years. From a corporate perspective it is not the best and most cost-effective business partner who is given the commission but a poorer and more expensive one. It is said that a company pays between five and fifteen percent more if an order is allocated by corrupt means, as the illegal payments made are then covertly charged to the company.

A corporate culture that is characterized by transparency makes life more difficult for corruption. For this reason the Chairman of Volkswagen, Dr. Bernd Pischetsrieder, declared in an open letter that Volkswagen intends to become “a transparent company both inside and out”.<sup>7</sup> To ensure this aim, a company-wide Ombudsman System has been installed. Every member of staff can turn to one of two neutral ombudsmen if they suspect that they have found evidence of corruption. By establishing the company-wide Ombudsman System, Volkswagen has created a safe haven for employees and business partners. Its aim is to prevent and combat corruption. The two lawyers involved handle all reports confidentially and only pass them on to the Volkswagen Group’s anti-corruption officer after an initial investigation. This officer is responsible for starting the necessary internal investigations via the Group’s auditing or security division. The employee who provides information on corruption remains strictly anonymous, as the ombudsmen are bound by a legal duty of confidentiality. When the ombudsmen are notified of possible corruption, they first hold a private conversation with the employee who made the report, first by telephone, then, if need be, in person. This allows information to be assessed more effectively and the credibility of the allegations to be evaluated. These talks are naturally held at neutral locations outside the company. If the internal investigation confirms the initial suspicion that a crime has been committed, the offence is reported to the police. The results of the internal investigations are made known to the ombudsmen if legal regulations permit. The ombudsmen can then pass them on to the employee who made the report, thus ensuring that all persons involved are informed. If the employee who made the report is also involved in corruption, the ombudsmen can advise them and offer assistance in breaking the vicious circle of corruption. Assistance in uncovering corruption usually leads to a more lenient penalty.

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<sup>7</sup> From a letter by Dr. Bernd Pischetsrieder in November 2005 to the entire Volkswagen AG workforce.

## Outlook

As globalization continues, politicians and the public at large are focusing their growing expectations on the corporate sector, particularly on multinational companies. Without their creativity and performance, CSR will remain a headless mass of ecological and social wishful thinking. The fear of the social consequences of globalization has fuelled the debate on the limitations of one-sided economic freedom and has notoriously led companies to be suspected of carrying out social and environmental dumping. CSR is the business response to these challenges. Individual companies, entire industries and ultimately the entire international economy are thus seeking to safeguard their license to operate not only by conforming to legal regulations and conducting appropriate risk management – through good corporate governance – but also through positive communication with all their stakeholders.

A CSR concept strengthens the sustainability of a company, consolidates its value orientation, bolsters its image and reputation and gives it a head start in recognizing risks arising from changes in the corporate environment.

# Historical Responsibility: Corporate Forms of Remembrance of National Socialist Forced Labour at the Volkswagen Plant

*Manfred Grieger*

The call to take historical responsibility is mostly found in connection with the consequences that arise from the National Socialist mass crimes.(Baer 2000) The warning “Never again” was last linked with calls for an appropriate memorial and extensive compensation for the victims.(Spoerer 2002, Thompson 2002) But there are considerable complications with the term: theologians see a comprehensive, “historical responsibility through the eyes of the present day” (Virt 1993) while educationalists prefer “education as historical responsibility”. (Mogge 1988) The dictum is used for political instrumentalisation, rather as the long-serving president of the Socialist Federative Republic of Yugoslavia, Joseph Broz Tito, assigned a historical responsibility vis-à-vis world development to his movement of non-aligned countries. Tito 1979)

Historical responsibility often comes in an appellative guise, with a speaker calling on others to act in a certain way with regard to historical events or with regard to decisions characterising the future. By contrast, as a descriptive category of their own action, there are often overtones of something affirmative, which in the sense of effective public presentation will emphasise the difference from the former abnormal behaviour. Both processes implement political and moral aspects of what is known as coming to terms with the past, without getting to the root of collective or individual responsibility. The Göttingen sociologist Wolfgang Sofsky logically warns, “Loud avowals of shame and gestures of internal remorse mean the opposite to that which they claim to indicate”. (Sofsky) The financial payments to those personally affected, their descendants or morally burdened institutions that have become payable over the last few decades after long political or legal battles, are contributing to the monetarisation of categories of responsibility, and lead at best – as Stuart Eizenstat, himself a protagonist on the international negotiating floor, maintains – to “imperfect justice”. (Eizenstat 2003) The assumption of historical responsibility by companies can therefore not follow the naive expectation that historical mistakes and failures might be purged by today’s measures. But the demand distilled from a culture of blame for a constant memorial and submissive remembrance also misses the point. Due to current market require-



ments, companies inevitably act above all as institutions of the present, which do not grant the past any overpowering significance, but which emphasise the opportunity of a new beginning. However, by leaving the past behind, there is also the risk that ethics founded on memory will become blunted. With this in mind a course ought to be adopted giving future requirements top priority, without basing it on denial.

Learning from history requires taking note of the facts unconditionally and naming the factors that made them possible. National Socialist forced labour occurred in many places during the Second World War: companies, public enterprises, communal institutions, building and labouring firms, farms and private households, not to mention the very many types of camps. The ubiquitous mass phenomenon of forced labour made the German war society, that is the economic entities, the National Socialist organisations, the state institutions and large sections of the German population, into beneficiaries of the lower classes of a mainly foreign subproletariat. (Herbert 1977, Center for Advanced Holocaust Studies 2004)

As armaments contracts were an essential prerequisite for the recruitment and allocation of forced labourers, the example of the circumstances in the then Volkswagen plant shows the close connection between the integration of this company into the German war economy and the development and specificity of the company's use of foreigners. Because of this, the dynamising factors appear to be the structures that made this possible.<sup>1</sup>

Labour control authorities and institutions made those people concerned objects of their mania for regulation. They were sent all over the place and handed over to German foremen or guards and were subject to discriminatory conditions. Looking at examples of ego documents written by forced labourers from Poland, France and the Netherlands, and at memories of Jewish survivors, highlights the subjective perspectives. The people personally affected demonstrate that forced labour is not to be seen as a closed chapter from the past but that it also has a contemporary level. This powerful effect was clearly seen in the international negotiations for suitable compensation for former forced labourers. The forced labour, which violated human rights, was a mass phenomenon, yet it is irrefutably also an inherent part of personal experience at the individual level. Tangible forms of remembrance, linked to the historical place where forced labour occurred, make it possible to reflect a historical phenomenon in the changed present day. Through intensive investigation of the early years of its history during the National Social-

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<sup>1</sup> One company history which integrates the development of forced company labour is available in the form of Mommsen, Hans / Grieger, Manfred: *Das Volkswagenwerk und seine Arbeiter im Dritten Reich*, Düsseldorf 1996; this paper is based on Grieger, Manfred: *Zwangsarbeit im Volkswagenwerk. Historische Entwicklung, persönliche Verarbeitung und betriebliche Erinnerungsformen*, published in: Hauch, Gabrielle (ed.): *Industrie und Zwangsarbeit im Nationalsozialismus. Mercedes-Benz – VW – Reichswerke Hermann Göring in Linz und Salzgitter*. Innsbruck 2003, pp. 49-65.

ist era, which in the Second World War led to the production of armaments and to the company's "employment of labour" of an estimated 20,000 forced labourers, Volkswagen AG has, over the years, developed its own corporate culture of remembrance. Its basic elements are research, youth meetings at the Auschwitz-Birkenau memorial, a permanent exhibition, 'The Place of Remembrance of Forced Labor in the Volkswagen Factory', and business policy decisions which have contributed to the corporate provision on the unresolved issue of compensation for forced labourers. (Kocks/Uhl 1999, Volkswagen 1999)

## The Plant

The Volkswagen plant was built at the beginning of 1938, not far from Fallersleben on the Mittellandkanal. It was part of an outstanding project for National Socialist social utopia, which promised the car described by Adolf Hitler as the 'Kraft-durch-Freude-Wagen' [strength-through-joy car] to all 'Volksgenossen' [people's comrades]. For this purpose, the Deutsche Arbeitsfront (DAF) [German Workers' Front], the largest National Socialist organisation, had founded a business enterprise, the 'Gesellschaft zur Vorbereitung des Deutschen Volkswagens mbH' in Berlin on 28 May 1937. One of the salient features of the factory, which got off the ground despite the odds, without taking into account the financial and economic rationalities, was that the first serious shortage of manpower was already evident halfway through the erection phase. In the summer of 1938 several thousand German construction workers were pulled out to build the Siegfried Line. As a result, there was no progress on the building sites at the Mittellandkanal. Further building became possible partly through the relinquishment of Italian construction workers in August 1938 in an agreement between the DAF and its fascist sister organisation, which was in the tradition of intergovernmental migrant work. At first it was intended to employ the Italians for only a few months, thus finding a short-term solution to the employment crisis caused by the armament. Thanks to the recruitment of several thousand Italian workers, the planned start of mass production of the car designed by Ferdinand Porsche for autumn 1939 could continue. (Mommesen/Grieger 1996, p. 117ff.)

The German invasion of Poland in September 1939 put paid to these plans. Civilian automobile manufacturing lapsed with the outbreak of war. The Volkswagen plant fell into a conversion crisis. It was revealed that armament considerations had played a minor part in the factory planning. The first version of a military variant of the KdF-Wagen, the Kübelwagen, was built in the summer of 1938, but the first design was turned down by the military. The Wehrmacht was concerned with armament planning and in 1938 could not see any military and economic use for the DAF company. The Luftwaffe alone offered to incorporate an aircraft engine factory into the developing 'main plant' in what is now Wolfsburg, although only a few foundation walls were actually built. (Ibid., p. 315ff.)

The real turning point in the development of the company occurred when the command structure was established on a war economy basis. Overnight, the allocative mechanisms were suspended and the autonomy of the company was seriously threatened by a hostile takeover bid from Junkers-Flugzeug- und Motoren-Werke AG. The compromise achieved in September 1939 turned the Volkswagen plant into an air armaments company, with a small automobile production line for unused surplus capacity. One of the anomalies of the German war economy was that the most modern automobile plant in the world was at first occupied almost exclusively with the production of wooden auxiliary tanks and the repair of damaged Ju-88 wings. It was not until the late summer of 1940 that a limited production of military cars began. (Ibid., p. 338ff.)

Unlike other big businesses whose core workforce was reduced by call-ups to the armed forces, the Volkswagen plant suffered from a shortage of key German workers from the start. While the business was changing over to armaments production, the Volkswagen plant was looking for the personnel necessary for the armaments orders that were coming in. The ‘conscription to labour service’ apparatus brought in several hundred Germans, but could not nearly cover the workforce requirement. So, after the start of the war, the company always used foreign replacement workers in order at least to keep the armaments production going. The recruitment of 300 women from Poland in the summer of 1940, their discriminatory treatment and the start of ethnic division of the work formed the transition to new forms of forced labour. In addition, from January 1941 more than 1000 German military convicts, used in particular for converting armoured vehicles and repairing Ju-88 aircraft, were forced to work. They were housed within the barracks complex in an area separated by barbed wire and were given a very hard time by their military guards. (Ibid., p. 428ff.)

In the spring of 1941, new groups of forced labourers were considered. The company was interested in the suggestion made by Heinrich Himmler himself to have around 3000 Polish Jews as forced labourers in ‘Stadt des KdF-Wagen’ [town of the strength through joy-car] and, in addition, for the prisoners to build their own concentration camp. By bringing the forced labour of Jews and concentration camp prisoners into the equation, the company was well on the way to extensive recruiting of forced labourers of every single category. (Ibid., p. 432ff., Gruner 2006)

At almost the same point in time, the Technical Director of Volkswagenwerk GmbH, Otto Dyckhoff, reflected on the permanent use of foreign labour in the extremely rationalised automobile factory. In a lecture to employees of the Reich Aviation Ministry in March 1941, he forecast that the Volkswagen plant shall “probably use more primitive people from Eastern and Southern Europe to operate the automatic machines before long”, while the “better qualified” German workforce would be promoted to fitters and toolmakers. (Dyckhoff 1941) The plan for a permanently ethnically divided workforce, in which the superior and supervisory status was reserved for Germans, was beginning to take shape.

Forced labour became a kind of permanent solution to the precarious workforce situation in the Volkswagen plant, and at the beginning of October 1941 the company adopted a pioneering role by using 650 Soviet prisoners of war as industrial workers. In the process it could be seen that the pitiful lack of nutrition and poor health of the prisoners of war assigned from the Wehrmacht's hunger camps was preventing reasonably productive industrial deployment. Some people were so weak they could not walk unaided or collapsed with exhaustion at the machines. As a result, the corporate management 'fed up' the emaciated workforce with food from the company's own farm estates. That improved the allocations of food to Soviet prisoners a little but was not really enough. For all tangible and intangible performance-oriented benefits for an increase in efficiency in the industrial deployment, the practice of discriminatory exclusion and strict punishment for deviating behaviour continued to apply. The basic care which Volkswagen gave to the Soviet prisoners of war whose health was poor over the winter of 1941/42 did not alter in any way the fact that moribund typhus patients went straight to the Wehrmacht's collection camps for the dying. Like other companies, and as also occurred later when rounding up "Ostarbeiter", the Volkswagen plant was working on its own initiative, searching the stalags at the front for specialist metal workers. (Mommensen/Grieger 1996, p. 544ff.)

After 1941, under the auspices of maximising profits and corporate expansion, the automobile factory grew to a medium-sized armaments group. Capacity utilisation increased to maximum levels hand-in-hand with the developing corporate philosophy. Through state funding and guaranteed acceptance of the products, armaments made corporate growth and war profits possible. Turnover climbed from 26 million RM in the first year of the war to 146 million RM in 1942 and reached more than 290 million RM in 1944. After initial losses of 12.7 million RM in 1940 the nominal profits as the war continued were more than 20 million RM. The corporate expansion acted as a significant link between economy and social system. The affiliation of new branch operations and subsidiaries proceeded apace – in 1941 the Luckenwalder Feintuchfabrik GmbH and the Schmiedewerk Ustron GmbH joined the Group. In 1942 the Volkswagen plant leased the large factory sheds of the Sudetenland-based Neudeker Wollkammerei und Kammgarnspinnerei AG, in order to concentrate aircraft production there. Later than Daimler-Benz AG or the Frankfurt Adler plant, the Volkswagen plant secured production capacity from a French automobile manufacturer at Peugeot in Montbéliard. The DAF company did all it could to accept what the National Socialist regime was offering in terms of economic participation. (Ibid., p. 601ff.)

It is indisputable that Volkswagen participated in the armaments boom to its own advantage, but this does not tell us anything specific. However, a close collaboration with the SS, which had shown an early interest in the military designs of the Volkswagen plant, developed through armament dealings. At the beginning of 1942 the Volkswagen plant showed the same initiative as it had with the recruitment of Soviet prisoners of war, with the transfer of concentration camp pris-

oners, who were to build a long-planned light metal foundry. In order to be able to recruit sought-after workforce groups for their own concerns, the company went to leading representatives of the National Socialist regime and the administrator of the forced labour force. On 11 January 1942 Ferdinand Porsche, chief executive of 'Volkswagen GmbH' agreed with Heinrich Himmler to relinquish 'completion, development and operation' of the foundry to the SS, which wanted to second prisoners from the concentration camps for this. A mutual business was formed: through the setting up of the 'KZ Arbeitsdorf', the Volkswagen plant obtained workers who would otherwise have been difficult to procure for a civilian post-war project, while the SS hoped to extend its influence in the armaments economy. At least it obtained its preferred off-road light personnel carrier model VW 166 for its newly set up SS units. Although the use of around 800 concentration camp prisoners in the summer of 1942 remained a brief interlude due to an intervention by Minister of Armaments Albert Speer, the unscrupulous workforce opportunism can be seen as a characteristic of the company recruitment policy. (Grieger 1996)

Occasionally German employees and managers used what freedom of action was available to improve the living conditions of foreign workers by providing extra food or transferring them to a better workplace, in the interests of seamless production or out of sympathy. But that was in no way the rule, as was made clear by the fate of the Soviet prisoners of war and the 'Ostarbeiter'. The harsh company attitude towards the daily needs of the foreign workforce was also experienced by the Italian military internees, whose treatment was characterised by the National Socialist regime taking revenge on their former allies, and the deep-rooted resentment of the German workers towards Italians.

The disparaging measures taken by the plant management, the foremen and the factory security officers was in stark contrast to the treatment of the over 1000 Italian civilian workers in the Volkswagen plant. They had previously formed a kind of worker aristocracy among the foreigners and were seen as equal to the German workforce with regard to their wages, food and treatment. In contrast, in October 1943 almost 1300 Italian military internees, followed in November 1943 by 200 officers, were "duly received as traitors and were despised, teased" and "frisked and yelled at as shirkers, cowards and weaklings" by those around them. (Täuber 1944) The inadequate food meant they were constantly hungry, particularly because a part of the proposed bonuses for "Langarbeiter" [those working long hours], a way of increasing performance, was only distributed to those who achieved top performances. The brutal treatment consisted almost exclusively of punishments such as withdrawal of food and beatings by foremen and factory security guards, about which the Italian military internees complained bitterly to the Wehrmacht. For example, after a production shutdown due to carelessness, the Italian officer prisoners of war were subject to truly punitive action, exposed to the harshest retaliatory measures and used for forced labour in a nearby quarry in Velpke. (Mommsen/Grieger 1996, p. 720ff.)

The armament production released, in particular among the megalomaniac plans of underground relocation, a dynamic of expansion and destructiveness typical of the system. Under the pretence of urgent armament orders, state financed underground workshops were set up for the Volkswagen plant between Lothringen and the Elbe, which at the beginning of 1944 would almost have doubled plant capacity, which was not being fully exploited in any event. At this point the development of ore mines, tunnel systems or asphalt mines and the operation of underground factories went hand-in-hand with the recruitment of concentration camp prisoners, who were assigned to the plant in the wake of armaments orders. To this end, Chief Executive Ferdinand Porsche also used his close links with the SS, namely with Heinrich Himmler and Oswald Pohl, in order to obtain a competitive advantage over other armaments companies through the additional allocation of concentration camp prisoners. In the company's daily routine, the discrimination and open brutality that was normal there led to a worsening of industrial working relations, in particular in the construction operations. The work tempo that was demanded, the emaciation through inadequate nutrition, the diseases caused by a lack of hygiene and being picked on by guards and German superiors led to numerous deaths among the concentration camp prisoners. By contrast, deaths among the prisoners who were deployed directly in armaments production, such as assembling the Fi 103 buzz bomb or producing anti-tank mines and Panzerfausts, were the exception. (Ibid., p. 803ff.)

Like the other industrial companies, Volkswagen only stopped war production when the allied troops arrived. The company maintained a strategy of keeping war production at the highest level until April 1945 and of safeguarding its machinery by decentralisation. In the summer of 1944, a "cannibalization policy" came into effect throughout the company, something which certainly mobilised the last reserves of capacity, but which also destroyed the sinews of the company's structure and – as a mirror image of society – advanced the complete collapse of operations. This all happened in an atmosphere of inefficiency losses and unimaginable fatalities which affected the large number of forced labourers and concentration camp prisoners in particular. In 1944 these groups made up more than two thirds of the 18,000 strong workforce. On account of the high rate of fluctuation it can be assumed that during the Second World War at least 20,000 people had been used in forced labour for the then Volkswagen company. Under the conditions in the National Socialist system, forced labour led to a process of dehumanisation of the workforce, to the degradation of people into an inanimate production factor. The return of death to the factory was the flip side of an ambivalent culture of efficiency, which could mean both life-saving functional care and being left to die. (Budraß/Grieger 1993) This development affected the Volkswagen plant as a profit-orientated company as it also did municipal authorities or public sector industrial plants, forestry commissions and even health insurance companies.

## The Forced Labourers

The memories of those personally affected by forced labour are both indispensable sources of historical research and constructs of social reality. (Jureit 1999) All serious study on local or corporate conditions today must collect and evaluate memoirs, and the present studies into foreign and forced labour in the Volkswagen plant are no exception. (More than 200 interviews were conducted a part of the research product financed by Volkswagen AG and carried out by the Ruhr-Universität Bochum, see Mommsen/Grieger 1996. In contrast, the publications of the Wolfsburg Stadtarchiv are based to a not insignificant extent on written questionnaires. Siegfried 1988) The memories serve as one of the reconstructions of historical fact. The description and analysis of areas of reality that are not reflected in the archive material in particular remain dependent on these historiographic sources. On the other hand, linked to the inclusion of memoirs by former forced labourers, is also the hope that the perspective of those affected will become apparent, as they give us their perceptions. There are numerous problems related to sources, both with interviews telling the story of their lives and with formal written questionnaires, which is why when analysing operational conditions in the Volkswagen plant through examples taken from ego documents from a French person and a Dutch person, and from the memories of Poles and Jewish survivors, the source must be thoroughly reviewed. (The methodological penetration of personal witnesses in the various categories appears to have advanced further in early contemporary research, for example see Rutz/Elit/Kraft 2002) There is no cause to doubt their historical validity taking into account the specific limitations of perception. However, due to the wide range of meanings they contain, it is necessary to make special efforts in differentiation with personal testimonies.

In general, personal testimonies, which have developed in close association with the historical situation to be reflected upon, are considered particularly convincing. While there are countless memoirs initiated by ongoing research, taking account of events going back more than 50 years, a contemporary document, the diary kept in 1944/45 by a Frenchman, was also handed in. (Schlinckert 2000) Jean Baudet, born 28 June 1922, was one of the 400 Frenchmen in the 'Jeunesse Ouvrière Français Travailleuse en Allemagne' (JOFTA) scheme, who came to the Volkswagen plant on 24 July 1943. The entries in a Catholic pocket diary ('Jeunesse Étudiante Chrétienne. Carnet Scolaire 1944'), a gift from his mother, which begin on 8 April 1944, show the dashed hopes of a young Frenchman who had applied to JOFTA to obtain certain benefits, in order to ward off recruitment to the 'Service du Travail Obligatoire' (STO). It only dawned on him gradually that there were very few of the hoped-for perks available in war-time Germany, as the entry of 15 July 1944 showed: "No milk in the mornings any more ('Only for Germans'), the same goes for the toilets, actually for everything. These men do not queue up. They are the higher race! The others are slaves." (STO, p. 39) The situation of the members of JOFTA was similar to that of the French who had

come to the Volkswagen plant through STO recruitment, and deteriorated noticeably as the war went on. On 10 February 1945 Jean Baudet noted, "Even with the food there is a doomsday atmosphere, i.e. hunger. (...) It is already very meagre, but we are afraid that soon we will really starve." (Ibid., p. 56) But at the same time he implicitly touches on a real difference from the situation of the racially segregated Poles or 'Ostarbeiter' from the Soviet Union. These people had been starving for a long time and were far more on the receiving end of the guards' repressive measures. Baudet specifically acknowledged this in his entry of 17 August 1944, "The Russians are beaten the hardest." (Ibid., p. 43)

The diary and also letters written to his parents contain hints of aspects of day-to-day life that are rather neglected in other self-penned testimonials, and of political illusions that can be seen overall as reflections of a relatively privileged life. For example, Jean Baudet played football and in the spring of 1944 made a note of the away games. "Game in Lüneburg (122 kilometres). Left at 5.00 a.m., got back at 10.30 p.m. Won 10:0. Lovely drive across the heath (...) Well-earned rest after the day before. Reading. But I had to go back to the factory in the evening, which is already almost forgotten." (Ibid., p. 34) On 7 May 1944 there was a game in Halberstadt. "Won 4:0. Whole day on the train. Landscape not so interesting, rather flat: meadows, woods, fields. (...) Pleasant journey back on the train. The 'Fräuleins' there are really very friendly." (Ibid., p. 35) Baudet noted in a reference to an evening walk through the wood, "wonderful moments", and after a visit to a cultural event, his assessment was "We are going to bed happy". (Ibid., p. 33)

The diary recorded the showing of an anti-Semitic film "Jud Süß", and the regular absenteeism. "Well, even I have got hooked on it and am not going to work tomorrow. I potter about the barracks until midday and then go into the wood to read. (...) Today I'm doing it again. It's great. Air-raid warning like yesterday. In the afternoons I go for a swim and sunbathe by the canal. You could write a book about this kind of illicit free day!" (Ibid., p. 39) The abruptness of the impressions that have not been condensed into a finished account gives the source of the diary a special value. The noted participation in a roll-call of the NSDAP-Gauleiter and the fascination with the military fanaticism of the Hitler Youth in the Volkssturm ("The Germans really are an astonishing people" (Ibid., p. 58)) are placed next to description of the brutal treatment of foreigners, which emphasised without irony the European ideology of the SS, "A Frenchman, who had only come out of hospital eight days ago, experiences the same treatment. He lies wheezing on the ground but the SS carry on beating him. Can we call that 'civilisation' and want to build a Europe on these principles?" (Ibid., p. 43) In addition, it is not untypical that Baudet used the term "forced labour" only once, to characterise the extra work of a Frenchman who had attracted the attention of a German guard. (Ibid., p. 56)

Jean Baudet's diary is thus a document that takes us right to the heart of the structures of the National Socialist forced labour system. In it there are notes on the relationships between the different national groups with the reciprocal aloofness and covetousness. It shows the different state of those affected depending on



their nationality and their legal status and at the same time makes clear that the different levels of treatment affected the behaviour and attitudes of the multinational forced labour workforce. Particularly conspicuous is the notification of youthful vitality, which highlights the subjectiveness of the actor and reporter – Jean Baudet used the freedom he had, indulged his youthful curiosity, got to know young women from the Ukraine and cherished the camaraderie with French people of the same age. Occasionally he was light-hearted and on other occasions confided his worries about future prospects to the personal notebook that was never intended for publication. All in all this thoroughly ambivalent source requires a different view, for it discloses the personal situations as ambiguous.

The written memory report of Julian Banaś (born in 1926) from Poland has to be classified in a different category. He was caught in a police raid at Dęblin station on 10 October 1942 and arrived at the Volkswagen plant on 18 October 1942 as an apprentice via Lublin and the employment office transit camp of Lower Saxony. On 12 January 1988 Julian Banaś completed his paper “Experiences of a stay in Wolfsburg during the period from 10.10.1942 to 30.11.1944”. This had come about due to a request from the Wolfsburg town archive, which had enclosed a package of questions in a letter dated 22 October 1986. Thus the text was a result of external inspiration and Julian Banaś made this clear at the start of his text. “Returning to memories of a time when people were degraded and when a person was treated like an object is an unpleasant affair. That is certainly the reason why I have only now decided to describe my experiences during the stay in Wolfsburg. Actually my friend during the misery of the war, Stefan Zurawicz, persuaded me.” (Banas 2004, p. 26) Before he replied, Julian Banaś therefore had to overcome internal limitations. He wanted his answers to also be understood as an important addition to the existing information. In the reflected understanding of subjectivity – “everyone reacts differently to different things and judges the same situation in their own way” – for him, with his view of things, it was a question of nothing less than the “basis for objective truth”. (Ibid.)

In his paper, Julian Banaś followed to the best of his knowledge and conscience the given question template in accordance with his personal data, the circumstances of his recruitment and how he came to the Volkswagen plant, where he stayed, the living conditions, the situation in the camp, the food, how free time was spent, the work and the repression in punishment and labour reform camps. In its generalising construction however, his intention to paint “a picture of the life of Polish workers (...) in the Volkswagen plant” went beyond the wish to transfer facts that had been conveyed from Wolfsburg. Thus, the text consists of both detailed statements on the fittings in the standard barracks, on exactly what they had to eat and working hours etc., and interspersed stories that were extremely important for the personal construction of the victim and the educated man.

On the question of food, Julian Banaś answered with the laconic wording “I remember it as if it were yesterday: whenever I ate the last morsel, I felt even hungrier. It was a pain that nobody can explain, if they have not experienced famine. Not enough to eat in a day, a week or a month, that is not real hunger. True hunger

only starts when your body has used up its last reserves.” In the words of Julian Banaś, hunger was a “long ordeal”, even remembering that “starts to hurt”. (Ibid., p. 34) He clearly made far more than just a reference to inadequate nourishment, he also recognised both the definition of the historical boundary between personal experience and comprehending knowledge of onlookers, and the updating of a personality-forming experience, of the long ordeal of his whole generation.

Frenzies of beating by security guards were philosophically embedded in the memoir or, in the case of the assault by a senior German, seen as a noteworthy experience, that stands as an example of the “attitude of an intelligent man”. After an unprovoked attempt at a kick by his head of department, an engineer, the same man remarked the following day on how Julian Banaś was multilingual and exchanged greetings with him as if nothing had ever happened. Regarding this turnaround, Banaś, said, “People change, and also changed 40 years ago.” (Ibid., p. 42)

The wording also reflects the persistent conciliatory trait of the humanist who supported the Polish-German rapprochement and in his visits to Wolfsburg described the conditions clearly and in a balanced way. However he never allowed there to be any doubt about the human rights violations experienced by individuals. For Julian Banaś the feeling of discrimination, the hunger and the tormenting homesickness were the worst of his time in Wolfsburg.

In contrast, the Dutchman Henk ‘t Hoen (born 1922), who as a sent-down student had to work in the Volkswagen plant between 15 June 1943 and his liberation, (Grieger 2002) produced the first notes on his time in Germany in the years immediately after the war. After a long break due to “studying, work, family and my career path” he reworked and expanded the texts after he retired, when the memories came flooding back. (‘t Hoen 2002, p. 19) For the sake of the younger generation, who were asking for the truth, he produced his notes as a representative of the last witnesses. As he said himself, his “memories consisted mostly of images”. (Ibid., p. 20) He expanded these into facts, which he took from documents or communications of his former comrades. Thus this grew into a condensed memoir, which from 1996 onwards he made available in hectographed form to those interested. Now the publication has also been translated into German.

The autobiographical book with the laconic title “Two years at the Volkswagen plant” amalgamates personal memories and images of memory with information taken from the experience of others or from historical research – the statements are thus both document and analysis. The above average powers of observation, his knowledge of languages, facilitating contact with a wide range of nationalities, his curiosity and his relatively great freedom of movement ensured that the unskilled coach-building worker, and later technical draughtsman in the construction department, had a broad field of perception. Although it is not always possible to draw a fine line between the different blends of personal memory, perception by others and scientific analysis, the description nevertheless has the effect of memorably consolidating the information, in the sense that it makes it easy to understand the corporate system of multi-ethnic forced labour. The short chapters “Film showing with consequences”, “Split trenches” and “A glimmer of light on the

horizon” revolve around typical situations, while the chapters “The Russians”, “The Italians” or “The camp elder in Laagberg concentration camp” and “Tamara” deal with groups or people who for Henk ‘t Hoen were of outstanding importance or in his view allowed typical insights into the situation of forced labourers.

The text is divided into four sections, with the themes of “Background”, “The factory”, his time “At Laagberg” and “Liberation and homecoming”. Henk ‘t Hoen describes in detail his day-to-day working life in the growing Laagberg camp, where he came into close contact with prisoners of the external labour commando of the concentration camp there, and obtained knowledge of National Socialist crimes. The personal confrontation with the powerful core of the National Socialist forced labour system affected him deeply and motivated him, directly after the war, to assist in identifying a direct culprit by making enquiries himself. The desire that the concentration camp prisoners and other victims should receive justice permeates the text as though it had happened to him personally. The author portrays himself throughout as an undamaged subject at heart. This is particularly evident for the time after his liberation, when Henk ‘t Hoen worked as an interpreter for the Allied Military Government and was commissioned by the Dutch returnees with organising the journey home. As expected, the description in the episodic book turns out to be detailed and action-packed.

The memories of four Jewish survivors based on interviews carried out in 2004/2005, which were published in May 2005 for the sixtieth anniversary of their liberation, revolve around the trauma of the annihilating persecution of Jews by the National Socialist regime, to which the overwhelming majority of family members fell victim. On behalf of the around 1800 other Jewish concentration camp prisoners who came to carry out forced labour in the Volkswagen plant via Auschwitz, one man and one woman reported on their time in the armaments factory. The presentations are expanded by typical stories of those who survived under a disguised identity as Catholic-Polish forced labourers or as ethnic Germans. They lived in mortal fear of extermination every day and this was the essential difference between their situation and that of the other forced labourers. In their recollections, they attribute their survival to the – compared with Auschwitz – better care and accommodation, and on the work based on the division of labour and determined by the rhythm of the machinery in the production process. The SS guards went easy on bullying, so there was hope for survival. The Jewish survivors make themselves available in their respective area of the historical investigation, which Julie Nicholson describes as follows: “To preserve history and learn its lessons is an essential task”. (Nicholson 2005)

The examples make it clear how the different developments are connected and what the purpose behind telling the stories is. At the same time, they highlight the individuality of the experience and how it was dealt with. If there is no allowance for the specific narrowness of the perception and the respective ways of dealing with it, there is the methodological risk that these sources are being used to illustrate the presentation perspective of the younger authors rather than to put across the perspective of those affected. No complete history of the forced labour can be

distilled from the personal testimonials, as neither the diary nor the written papers contain the whole of the experiences and conditions. In addition, among the typical ego-texts, examples of female perception are in the minority and there are no personal testimonials at all by people who were older at the time. From that point of view, most of the personal statements available today are texts produced by younger people, those who tend to be good with words and above all the survivors. The description of forced labour away from home reflects an attempt by victims of the racist National Socialist regime to make retrospective contact with their own experiences of persecution, and to relate the associated emotions and moods to themselves. Updating the traumatic experiences of being subjected to force and subjugation contributes to a comprehending subjection. (Regarding the ambivalence of subjection, see also Butler 1997, p. 2f.) While the factual report often goes hand-in-hand with silence regarding feelings, the closeness to the “grey zone” of human existence in an exclusive society can be seen time and again in the blurring and fragmentation. (Levi 1989, p. 22ff.) The personal testimonials are thus no mere source of empirical facts, but contain a wide range of meanings characterised by constructions of meaning and the rites of discourse which appear to be a constituent part of human forms of recollection. (Jureit 1999, p. 375ff.) The individuality of how experience is handled with the polyphony, the many voices of the narrative expression, corresponds to survival in the grey zone of the forced labour system. (Regarding to the ‘polyphonic moral’, see for example Bachtin 1994, p. 5ff.) There will be greater critical evaluation of methods in store for these blurred proportions in the historiography of National Socialist forced labour in the future.

## The Remembrance

The long-unresolved question of the appropriate way that German society should deal with the mass phenomenon of forced labour in the war economy affected politics, the business community and many people, and in July 2000 led to the setting up of the Federal Foundation ‘Remembrance, Responsibility and Future’. The Federal fund represented a final acknowledgement by German society that the forced labour by millions of people from all European countries and by Germans excluded by the National Socialists was a violation of human rights.

The public and corporate forms of remembrance have for many years not done justice either to the ubiquity or the mass character of forced labour. It has long remained a taboo subject at the Volkswagen plant. The company did not set up a discussion on the history of the factory in the National Socialist era until the mid-1980s. A research project at the Ruhr University Bochum followed in 1986, in order to allow an investigation into the involvement of the company in the National Socialist system of forced labour. (The result of the research project spanning several years is available as Mommsen/Grieger 1996) After many intermediate steps in discussions between management, employee representatives and the workforce,

the ‘The Place of Remembrance of Forced Labor in the Volkswagen Factory’, which is looked after by the newly founded Corporate Archives, was opened in December 1999. The concept and design of the exhibition, set up by 25 Volkswagen trainees, was geared to examining the place where the forced labour occurred in the centre of the factory and the authentic bunker rooms: this was where foreign forced labourers took shelter from air raids while they were at work, and this was where they were locked in during their stay. The ambivalent experience of unlawful detention in the search for protection, like the overall spectrum of areas of experience of the actual people concerned, is reflected in the variants of the perceptions presented.

The design and shapes use the traditional spaces as a starting point, but do not produce an atmosphere of menace. Instead of wanting to take visitors back to the past, the intention is to take an enlightened view from a civilian present at the human rights violations that took place here. Visitors can undoubtedly fill in the gaps. There is no additional emotionalisation. The choice of materials and the stereoscopic images incorporate references to the factory and are typical of the times. The combination of the architecture of the rooms and the exhibition, of contemporary documents, photos, exhibits and witness statements makes the situation of the different groups concerned clear, while at the same time referring to their individual perceptions and assessments. The explanatory texts are written as if by a news journalist and the restrained form of presentation emphasises the distanced empathy, which can be viewed as an appropriate attitude from younger people and in particular from the company.

After the entrance corridor to the air-raid shelter, in the reinforced concrete wall of which a war remnant has embedded itself, comes Room 1 over which the heading “Projekt Volkswagen” hangs. This room is characterised by the juxtaposition of stainless steel and wooden structures. It deals with the socially utopian National Socialist vision of mechanisation and the start of forced labour after armaments production began. Room 2 – “Expansion of armaments production and the systemisation of forced labour” – shows the different groups concerned in a structure of gates. The isolation of the “concentration camp prisoners” and their separation from the other factory workers are made clear in Room 3. The small Room 4 refers to the “transfer to underground sites and decentralisation” of the company in 1944/45 by means of hangings, floor variations and stylised structures that restrict the space. Room 5 takes up the cause of remembrance, because those affected took their experiences, adventures and perceptions to their (new) home and confronted German society, historians and the company with the stories they remembered. Abstract wording becomes a real witness, the participatory observation of an experience of degradation, in a narrative structure, in text. For this reason typical remarks are presented in illuminated boxes, which report on experiences polyphonically, giving us memories that have remained, or showing what has been forgotten as a form of remembrance. In an ante-room there are two information points at which you can call up information on a monitor about the “investigation into National Socialism in the corporate history”.

The memorial is open to the public if an appointment is made with the Corporate Archives, and attracts around 6000 visitors annually, including numerous groups of trainees and school classes. The catalogue, which reproduces all exhibits and text blocks, is in German and English.

Volkswagen wants to pay its respects to those affected by forced labour with this memorial. It stands on the spot linked to the forced labour of thousands of people. The permanent exhibition is the result and a part of a corporate culture of remembrance, which began with research but quickly also led to exchanges between young people and to meetings with former forced labourers. Volkswagen trainees have been involved with the concentration camp memorial at Auschwitz for fifteen years, and now after financial participation by Volkswagen AG in the international youth meeting place, remembrance groups have been created in the company. Since the Corporate Archives has been set up in the Communications division, there has been a direct responsibility for historical subjects, which provides appropriate publicity through 'Historical Notes' as apart of series of publications, but also keeps in contact with former forced labourers, in order to support them if necessary in their preparations for a visit to Wolfsburg. The 'Archive of Remembrance' holds in trust the current stories and memories – photos, diaries and letters, spoons, textiles – of former forced labourers.

There were also consequences for the corporate policy of Volkswagen AG, when they announced humanitarian payments for forced labourers of the then Volkswagen company. After 1991 project-related humanitarian aid was paid, and since then 2150 payments have been made to people in 26 countries. However, these payments were not intended as indemnification for withheld wages or as compensation for human rights violations. In the interest of rapid aid for the very old people concerned, the board of trustees, which included Shimon Peres, Dr. Franz Vranitzky und Dr. Richard von Weizsäcker, approved a standard, one-off payment of DM 10,000 (today € 5,112.92) to everyone who had been forced to work for the then Volkswagen company, regardless of the length of time worked, the level of persecution or which group they belonged to. Moreover, as part of its social responsibility, Volkswagen AG participated in the Foundation Initiative of the German Economy, a forerunner of the Federal foundation, 'Remembrance, Responsibility, Future' which has been set up in the intervening period.

For some this will not be an adequate expression of historical responsibility. But the death of most of those directly concerned shows the failure of German post-war society, that cannot be atoned for – by the population, the political class and the prospering companies of the 'Wirtschaftswunder' – to keep the millions of foreign forced labourers safe from the clutches of the National Socialist injustice. This is a bitter and irrefutable truth. However, through its historical activities, Volkswagen is making a peripheral contribution to the present-day task of ensuring European historical awareness about the social issues of war and forced labour. In this sense the investigation of historical subjects fits into the concept of corporate social responsibility. (Jonker/de Witte 2006)

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# Cross-cultural Sensitivities in Developing Corporate Ethical Strategies and Practices

*Terence Jackson*

## Understanding Culture and Cultural Differences

Geert Hofstede was one of the first to attempt to develop a universal framework for understanding cultural differences in managers' and employees' values based on a world-wide survey. Hofstede's work focuses on 'value systems' of national cultures which are represented by four dimensions:

- *Power Distance*. This is the extent to which inequalities among people are seen as normal. This dimension stretches from equal relations being seen as normal to wide inequalities being viewed as normal. The former West Germany scored (scores are nominally between 100 and 0) a relatively low 35, USA a relatively low to medium 40, Britain 35 and France a relatively high 68. Brazil scored 69 and Mexico 81. China was not included in the study. Hong Kong scored 68 and Taiwan 58. Eastern European countries were also not included in the study. An all white South African sample scored 49.
- *Uncertainty Avoidance*. This refers to a preference for structured situations versus unstructured situations. This dimension runs from being comfortable with flexibility and ambiguity to a need for extreme rigidity and situations with a high degree of certainty. The former West Germany scored a medium 65, France a high 86 on a level with Spain. US scored a relatively low 46, with Britain at 35. Brazil scored 76 and Mexico 82. Hong Kong scored 29 and Taiwan 69. The all white South African sample scored 49.
- *Individualism-Collectivism*. This looks at whether individuals are used to acting as individuals or as part of cohesive groups, which may be based on the family (which is more the case with Chinese societies or the corporation (as may be the case in Japan). This dimension ranges from collectivism (0) to individualism (100). USA is the highest (91). France scores 71 and Britain 89. The former west Germany scored 67. Brazil scored 38 and Mexico 30 (Guatemala was the most collectivist at 6). Hong Kong scored 25, and Taiwan 17. The all white South African sample scored 65.

- *Masculinity-Femininity*. Hofstede distinguishes ‘hard values’ such as assertiveness and competition, and the ‘soft’ or ‘feminine’ values of personal relations, quality of life and caring about others, where in a masculine society gender role differentiation is emphasized. The US scored a medium to high 62, with the former west Germany at 66. Britain scored 66 and France 43. Brazil scored 49 and Mexico 69. Taiwan scored 45 and Hong Kong 56. The all white South African sample scored 63.

Power distance is polarized into small and large power distance and comprises attitudes which people within the culture have about the acceptable inequalities between people in the society or organization. In small power distance cultures there is a belief that inequalities among people should be minimized, that parents should treat children as equals and that teachers expect student initiative in the classroom. Hierarchies in work organizations are established as a convenience only to manage inequality of roles. Decentralization is popular, subordinates expect to be consulted, and privileges are frowned upon in a small power distance society. Conversely, in a large power distance culture, inequalities are expected and desired, parents teach children obedience and teachers are expected to take the initiative in the classroom. Hierarchies in organizations reflect the natural order of inequalities between the higher-ups and the lower-downs, centralization is popular and subordinates expect that they are told what to do. Privilege and status symbols are expected.

Weak uncertainty avoidance cultures accept uncertainty as a feature of everyday life, there is generally low stress and people feel comfortable in ambiguous situations. People are curious with what is different. Students are happy with open-ended learning situations, and teachers can say ‘I don’t know’. Rules should only be for what is necessary, people may be lazy, and work hard only when needed. Punctuality has to be learned, and people are motivated by achievement and esteem or belonging to a group.

Strong uncertainty avoidance is characterized by the threat of uncertainty which is always present but must be fought. It is characterized by high stress and a fear of ambiguous situations and unfamiliar risk. There is a feeling that what is different must be dangerous. Students are more comfortable in a structured learning situation and like to be told the right answer: teachers are supposed to know the answers. There is an emotional need for rules, even when these may not work. There is a need to be busy, and a feeling that time is money: an inner urge to hard work. Punctuality is natural, and people are motivated by security, esteem or belongingness.

In individualist societies people look after themselves and the immediate nuclear family. A person’s identity is based on him or her as an individual. Speaking one’s mind is respected. Education is aimed at learning to learn, and academic and professional diplomas increase self respect and potential economic worth. The employer-employee contract is assumed to be based on mutual advantage, and hir-

ing decisions are supposed to be based on individual competence. Managers manage individuals, and tasks are more important than relationships.

In collectivistic societies people are born into and protected by extended families, to which they exchange loyalty. One's identity is based in the belongingness to a social group or network. Children are taught to think of 'we' not 'I'. Rather than speaking one's mind, harmony should be maintained and direct confrontation avoided. The purpose of education is to learn how to do, and diplomas provide an entry into higher status groups. Rather than purely a contract, the employer-employee relationship is seen as a moral one such as a family relationship, and when hiring or firing the employee's in-group is considered. Managers manage groups, and relationships are more important than tasks.

In a 'masculine' society values are based on material success, money and possessions. Men are expected to be assertive and ambitious, and women tender and concerned with relationships. The father deals with facts and the mother with feelings. There is sympathy for the strong and the best student is the norm: failing in school is seen as a disaster. People live in order to work. Managers are expected to be decisive and assertive, and there is a stress on competition, performance and resolution of conflict by fighting them out.

In contrast, the 'feminine' society has values of caring for others and preservation rather than progress. People and good relationships are more important than money and things, and people are expected to be modest. Both men and women are expected to be concerned with relationships, and both mother and father should deal with feelings and facts. There is sympathy for the weak, and the average student is the norm. Failing in school is a minor accident. People work in order to live. Managers use intuition and try to gain consensus. There is a stress on equality, solidarity and quality of work life. Conflicts are resolved by compromise and negotiation.

A fifth dimension was added by Hofstede to the original four. This was developed through the Chinese Cultural Connection study and in part justified by Hofstede's warning of the dangers of developing constructs from a Western point of view. The Chinese Cultural Connection was an attempt to counter this by introducing an Eastern perspective and values. The study reinforced three out of the four dimensions in Hofstede's original study: the Chinese dimension of 'human-heartedness', which incorporates values such as kindness, courtesy and social consciousness, correlates negatively with masculinity; 'integration' which encompasses the cultivation of trust, tolerance and friendship correlates negatively with power distance; 'moral discipline' including values of group responsiveness, moderation, adaptability and prudent behaviour correlates negatively with individualism.

None of the new dimensions correlated with uncertainty avoidance, but a new dimension termed Confucian Dynamism and then Long Term Orientation, with values of persistence and perseverance, ordering relationships by status and observing order, thrift and having a sense of shame. Uncertainty avoidance is concerned with absolute truth which may not be a relevant value in Chinese society

and other eastern cultures which are more concerned with Virtue. Of particular relevance is the virtue of working hard and acquiring skills, thrift, being patient and persevering: all values connected with this fifth dimension which may replace uncertainty avoidance as a relevant Eastern concept. On a scale from a minimum score of 0 to a maximum 118, Pakistan scores 0 and China 118. The Chinese societies of Hong Kong (96) and Taiwan (87) are towards the top of the scale with Japan (80) and South Korea (75) next. Brazil scores 65, Singapore 48 and Netherlands 44. Sweden (33), Poland (32) and the former west Germany (31) follow. USA scores a relatively low 29, with Britain at 25. Of African countries, Zimbabwe (25) scores the same as Britain, and Nigeria is second from bottom with 16. This seems to bear out an assumption that the eastern 'tiger' countries which have done well economically are high on this dimension, with the Anglo-Saxon countries relatively low, and African countries with a short term economic perspective scoring very low.

## Other Cultural Dimensions

Despite severe limitation in methodology and academic rigour, the work of Trompenaars has been used extensively, particularly in connection with cross-cultural management development activities. The most important dimensions are:

- *Universalism-Particularism*. In some cultures people see rules and regulations as applying universally to everyone, regardless of who they are. In cultures which are more particularist, people see relationships as more important than applying rules the same for everyone. There is an inclination to apply the rules according to friendship and kinship relations. This has implications for recruitment and promotion policies in organizations in some Asian countries which may be at variance to practices in countries such as the United States and Britain. However, there are differences in European countries. Greece, Spain and France are seen as more particularist, and Sweden, former West Germany and Britain as more universalist. One of Trompenaars questionnaire items asks respondents to assume they are a passenger in a car which a friend is driving in an urban area above the speed limit. He hits a pedestrian. His lawyer says that it will help him considerably if you swear in court that he was driving below the legal speed limit. Helping your friend indicates particularism, not helping him indicates universalism. South American, African and Asian countries tend to be particularistic.
- *Achievement-Ascription*. Status is accorded to people on the basis of what they achieve in their jobs and their lives (achievement) or who they are and where they come from such as family background, their school or some other prior factor (ascription). Quite often more traditional societies accord status according to the latter precept. Again, this may influence recruitment and promotion policies which may be at variance to practices in some (but not all)

Western cultures. On some measures Austria, Belgium, Spain and Italy are more ascription oriented, and Denmark, Britain and Sweden more achievement oriented. Generally 'developing' countries tend to be more ascriptive.

- *Locus of control* (Trompenaars, 1993). People tend to believe that what happens to them in life is their own doing (internal locus of control), or they have no or little control over what happens to them (external locus of control), the causes of which are external to them. Generally 'developing' countries tend to have a higher external locus of control.

Both Trompenaars' and Hofstede's work focuses on organizations. The work of Inglehart and colleagues in the World Values Survey focuses on wider societal values. This work also identifies value dimensions.

The first dimension *Traditional vs. Secular-Rational* values is based on items that reflect an emphasis on obedience to traditional authority, often religious authority and adherence to family and communal obligations and norm sharing, versus items emphasising a secular worldview where authority is legitimized by rational-legal norms and an emphasis on economic accumulation and individual achievement. Hence items loading positively and representing the *Traditional* pole are: God is very important in respondent's life; it is more important for a child to learn obedience and religious faith than independence and determination; abortion is never justified; respondent has a strong sense of national pride; respondent favours more respect for authority. *Secular-rational* emphasizes the opposite values: that is, provide negative scores on the above items. The study also produce a list of a further 24 items that correlate with this values dimension. These are mainly concerning the importance of religion, respect for parents and family including the dominance of the husband's role, importance of work, and loyalty to country; with a positive correlation representing *traditional* values.

The second dimension *Survival vs. Self-Expression* values reflects 'the fact that in post-industrial society, historically unprecedented levels of wealth and the emergence of the welfare state have given rise to a shift from scarcity norms, emphasising hard work and self-denial, to postmodern values emphasising the quality of life, emancipation of women and sexual minorities and relatively postmaterialist priorities such as emphasis on self-expression'. Items loading on the factor *Survival* are: respondent gives priority to economic and physical security over self-expression and quality-of-life; respondent describes self as not very happy; respondent has not signed nor would not signed a petition; homosexuality is never justifiable; you have to be very careful about trusting people. *Self-Expression* emphasizes the opposite values: that is, provide negative scores on the above items. The study also produce a list of a further 31 items that correlate with this values dimension. These emphasize the different role of men and women, dissatisfaction with own situation, rejection of people who are different including foreigners, favouring of technology, lack of emphasis on preserving the environment, emphasis of material wellbeing and hard work, with a positive correlation representing *Survival* values.

Countries classified under 'Protestant European' (e.g. Scandinavian countries, two Germanys, Netherlands and Switzerland) score high on both the *Secular-Rational* (modernists) and *Self-Expression* (postmodernist) dimensions. They also represent countries with the highest GNP per capita. At the opposite extreme and representing countries with the lowest GNP per capita, those whose scores represent *Traditional* (pre-modern/pre-industrialized) and *Survival* (pre-postmodern) are the countries clustered in an 'Africa' group (South Africa, Nigeria, Ghana) and 'South Asia' group (Pakistan, Bangladesh, Philippines, Turkey and India).

Bordering the *Self-Expression* end of the *Survival/Self-Expression* dimension, but still representing *Traditional* values on the *Traditional/Secular-Rational* dimension, are countries clustered in a 'Latin America' group (Peru, Venezuela, Columbia, Brazil; and bordering on the Secular-Rational Mexico, Argentina, Uruguay). An 'Ex-Communist/Baltic' group (Estonia, Lithuania, Latvia, Czech) is clustered high on the *Secular-Rational* end of the *Traditional/Secular-Rational* dimension and at the *Survival* end of the *Survival/Self-Expression* dimension.

Bordering this group, towards the *Self-Expression* side of the dimension is a 'Confucian' group (China, S Korea, Taiwan and Japan), and towards the middle of the *Traditional/Secular-Rational* dimension, but still at the *Survival* side of the *Survival/Self-Expression* dimension an 'Orthodox' group (Russia, Ukraine, Bulgaria, and others).

An 'English Speaking' cluster (USA, Britain, Ireland, Australia, New Zealand, Canada) is grouped in the middle of the *Traditional/Secular-Rational* dimension, and high on *Self-Expression*. In the middle of both dimensions is a 'Catholic Europe' cluster that includes Belgium, France, Italy, Spain and Austria towards the *Self-Expression* side of the *Survival/Self-Expression* dimension, and overlapping with the 'Orthodox' group towards *Survival* is Slovenia, Croatia, Slovakia, Hungary.

America, contrary to what some modernist commentators suppose, is not the archetypal modern/postmodern or Secular-Rational and Self-Expression society that serves as the model for all other societies. Although high on *Self-Expression*, it is also high on *Traditional* values with high levels of religiosity and national pride comparable to 'developing' countries.

The WVS can be used to understand national differences regarding ethicality by drawing conclusions about correlations between Inglehart's general values dimensions with specific aspects of ethicality. For example, the relationship between traditional vs. secular-rational values and loyalty to ones' family, group, authority and nation. We could surmise that if a society has strong *traditional* values, being high on religiosity and deferential towards authority, then disloyalty to family, authority figures and nation could be regarded as unethical. Disloyalty to the corporation in the form of whistle blowing, for example could be frowned upon. Similarly, we might surmise a relationship between *survival* values and, say, corrupt practices. With an emphasis on economic survival people might be tempted to cut corners in business and be more pragmatic about paying bribes for example. Similarly, there may be a disregard for pollution controls as has been the case in many rapidly industrializing countries such as Eastern European countries and China.

At the other end of this dimension, *self-expression*, we could assume that lack of democracy, low concern for the environment and disregard of women's and minorities' rights are seen as unethical.

Another study that focuses on wider societal values is that of Schwartz. He argues that there are three basic issues that confront all societies. The first issue is the relation between the individual and the group; the second is the way it is possible to guarantee responsible behaviour to maintain the social fabric; the third is the relationship between humankind and the natural and social world within which they exist.

The way the first issue is addressed, he reminds us, is reflected in the large body of literature on individual-collectivism. Much of this literature is contained within management and organizational studies, and is reviewed later in this chapter. Schwartz also explains that this concept is reflected in a wider literature and described as individualism-communalism, independence-interdependence, autonomy-relatedness and separateness-interdependence. He suggests that inherent within this issue are two themes: the extent to which the individual's or the group's interests should take precedence; and, the extent to which persons are autonomous versus their embeddedness in their group. He believes that the latter is more fundamental as the extent to which a person is embedded in their group determines the extent to which conflicts of interests are unlikely to be experienced. One pole of this dimension reflects cultural values that see a person as being embedded in the collectivity, finding meaning in life mainly through social relationships and identifying with the group through participation in a shared way of life. This set of values is encompassed in Schwartz's empirical derived value type *Conservatism*, or 'a cultural emphasis on maintenance of the status quo, propriety, and restraint of actions or inclinations that might disrupt the solidary group or the traditional order (social order, respect for tradition, family security, wisdom)'. The other pole reflects individual autonomy. He distinguishes between two types of autonomy. These are *Intellectual Autonomy*: 'A cultural emphasis on the desirability of individuals independently pursuing their ideas and intellectual directions (curiosity, broadmindedness, creativity)'; and *Affective Autonomy*: 'A cultural emphasis on the desirability of individuals independently pursuing affectively positive experiences (pleasure, exciting life, varied life)'.

The second issue seeks to address the way it is possible to guarantee responsible behaviour to maintain the social fabric, and gives rise to two polar resolutions. From Schwartz's empirical work, one resolution involves using power differences, and the other involves voluntary responses to promoting the welfare of others. He terms the first *Hierarchy*: 'A cultural emphasis on the legitimacy of an unequal distribution of power, roles and resources (social power, authority, humility, wealth)'. The second Schwartz terms *Egalitarianism*: 'A cultural emphasis on transcendence of selfish interests in favour of voluntary commitment to promoting the welfare of others (equality, social justice, freedom, responsibility, honesty)'.

The third issue that addresses the relationship between humankind and the natural and social world is resolved again through two possible responses. The first seeks to



master, change and exploit the outside world out of personal or group interests; the second seeks to fit into the natural world and to accept it as it is. From his empirical study Schwartz defines these two value types as *Mastery*: ‘A cultural emphasis on getting ahead through active self-assertion (ambition, success, daring, competence); and *Harmony*: ‘A cultural emphasis on fitting harmoniously into the environment (unity with nature, protecting the environment, world of beauty).

So, for each of the three issues, there is a bipolar dimension that represents alternative resolutions of the issue that can be found in different cultural groups: 1. relation of individual and group (Conservatism versus Autonomy); 2. preservation of the social fabric (Hierarchy versus Egalitarianism); and, 3. relation to nature (Mastery versus Harmony).

Schwartz’s samples are from teachers and students. He argues that the former are good representatives of the cultures as they are custodians of cultures and it is they who pass this on to the next generation. The samples of university students generally corroborate results from school teachers. It is likely that because of the way the constructs and the variables comprising them have been tested among various cultural groups in some 44 countries, at both individual level and group level, that they may be claimed to be universally representative of values which may occur anywhere in the world. They also reflect societal values (rather than those in corporate settings) because of the populations from which Schwartz took his samples.

There also appears to be some overlap with Inglehart’s and colleagues theory concerning modernization/postmodernization trends and associated societal values. Hence, we could postulate that *Conservatism* and *Hierarchy* may prevail in Inglehart’s ‘traditional’ cultures (reflecting ‘developing’ countries) as well as in ‘secular-rational’/‘survival’ cultures (such as in rapidly industrialized or ‘emerging’ countries, e.g. Eastern European countries); *Autonomy* in ‘secular-rational’/‘self-expressive’ cultures (such as Western European and Anglo-Saxon countries); *Egalitarianism* in ‘secular-rational’/‘self-expression’ cultures; *Mastery* in ‘secular-rational’/‘survival’ cultures (such as the Eastern European and rapidly industrialized countries); and, *Harmony* in both ‘traditional’ and ‘self-expression’ cultures.

Previously noted has been the reluctance of those theorists that postulate about cultural values to extend their theories and empirical findings to a consideration of ethics values and decision making. Schwartz is almost there when he says:

“I postulate that cultural dimensions of values reflect the basic issues or problems that societies must confront in order to regulate human activity. Societal members, especially decision-makers, recognize and communicate about these problems, plan responses to them, and motivate one another to cope with them. Values (e.g. success, justice, freedom, social order, tradition) are the vocabulary of socially approved goals used to motivate action, and to express and justify the solutions chose.”

His view indicates a direct relationship between the types of cultural values he is investigating to what is believed in a society to constitute ethical decision making.

Yet he appears not to make this connection. The way that societies define the relationship between individual and group has implications for solidarity and loyalty issues, depending on the nature of the group: family, community, corporation, nation. Work on collectivism that is reviewed below suggests issues with out-group members and the difference in treatment of in-group and out-group members in the work place for example. This has implications for the ethicality of aspects such as nepotism, including recruitment, promotion and job security. It is more likely that in a *Conservatism* culture ‘nepotism’ is not an ethical issue, but in an *Autonomy* culture it is. Similarly, what is acceptable in terms of inequalities and autocratic or paternalistic management styles in a *Hierarchy* culture may not be acceptable in an *Egalitarianism* culture. Also the acceptability of ‘conquering nature’ would be far less in a culture that reflects *Harmony* values. Similarly in a *Mastery* culture socially assertive behaviour that could reflect an aggressive business style may be more acceptable.

Inglehart’s and Schwartz’s work together provide a view of cultural values across a number of countries. The values dimensions, as well as individual items from the WVS provide information from which conclusions may be drawn about the wider society within which corporations exist. Other modern cultural values studies are more specific to corporate life. Such is the case with the GLOBE project.

The GLOBE project (Global Leadership and Organizational Behavior Effectiveness Research Program) is a more recent cross-national study undertaken by Robert House and a team of 170 researchers across 62 societies. Its main focus is the relationship between culture and leadership characteristics. In some ways the study is disappointing because it did little to break out of the paradigm of cultural dimensions set by Hofstede in the early 1980s, and it mirrors many of Hofstede’s cultural dimensions. Yet this, for our current purpose is useful as it provides a more up to date view of these cultural dimensions, and like the other studies examined above, provides a basis for considering *how* ethicality may differ across nations. It also goes purports to investigate both ‘values’ (e.g. ‘Followers *should be* expected to obey their leaders without question’) and ‘practices’ (e.g. ‘Followers *are* expected to obey their leaders without question’).

The cultural value dimensions proffered by the GLOBE project are as follows:

- *Power Distance*: ‘The degree to which members of a collective expect power to be distribute equally’. This (‘practices’ only, not ‘values’) correlates positively with Hofstede’s Power Distance and Schwartz’s Hierarchy.
- *Uncertainty Avoidance*: ‘The extent to which a society, organization or group relies on social norms, rules, and procedures to alleviate unpredictability of future events’. Curiously ‘values’ correlates positively and ‘practices’ negatively with Hofstede’s Uncertainty Avoidance. It correlates positively with Schwartz’s ‘Embeddedness’ (this equates with Conservatism, and is Schwartz’s (1994) dimension at the individual level.

- *Humane Orientation*: ‘The degree to which a collective encourages and rewards individuals for being fair, altruistic, generous, caring and kind to others’. This does not appear to correlate with Hofstede’s or Schwartz’s dimensions.
- *Collectivism I (Institutional Collectivism)*: ‘The degree to which organizational and societal institutional practices encourage and reward collective distribution of resources and collective action’. ‘Values’ correlates negatively with Hofstede’s Individualism, but not with any of Schwartz’s dimensions.
- *Collectivism II (In-Group Collectivism)*: ‘The degree to which individuals express pride, loyalty, and cohesiveness in their organizations or families’. ‘Practices’ correlates negatively with Hofstede’s Individualism, but not with any of Schwartz’s dimensions.
- *Assertiveness*: ‘The degree to which individuals are assertive, confrontational, and aggressive in their relationships with others’. ‘Practices’ correlates positively with Hofstede’s Masculinity and negatively with Schwartz’s Egalitarianism.
- *Gender Egalitarianism*: ‘The degree to which a collective minimizes gender inequalities’. This does not correlate with any of Hofstede’s dimensions, but correlates positively with Schwartz’s Egalitarianism.
- *Future Orientation*: ‘The extent to which individuals engage in future-oriented behaviours such as delaying gratification, planning, and investing in the future’. This does not appear to correlate with any of Hofstede’s or Schwartz’s dimensions.
- *Performance Orientation*: ‘The degree to which a collective encourages and rewards group members for performance improvement and excellent’. Again this appears not to correlate with Hofstede’s or Schwartz’s dimensions.

The GLOBE project findings reflect many of the cultural dimensions proffered in earlier studies, and as such do not add conceptually to our descriptive understanding of ethical values across cultures. It does, however, provide current information that is perhaps more rigorously validated, and covers more countries than previous studies. For example it covers some six African countries and six post-communist countries.

## **Instrumentalism and Humanism**

Another important cultural dimension is *locus of human value* (Jackson 2002). Across cultures people are valued differently as human beings within work organizations as follows.

- An *instrumental* view of the utilitarian value of people in organizations (managing people as a resource), whereby people are seen as a means to an end: human resources are used to meet the executive objectives of the organization, and;
- A *humanistic* view of the intrinsic value of people in their own right (developing the potential of people in organizations as an end in itself), whereby people are seen as having a value for who they are, rather than what they can do for the organization.

This has been applied to South Africa and other emerging economies where at the macro levels, instrumental and humanist values vie for prominence: downsizing versus job creation, short-term versus long-term imperatives, status quo resourcing versus affirmative action, even monetarist versus interventionist policies. At the micro levels of management attitudes and practice, organizational orientation and people development, the differences between regarding people as a resource and means to an end, or as a value and end in themselves may be a cultural difference in management practice which needs to be reconciled in the context of emerging economies.

## The Link Between Culture, Values and Ethics

Explaining differences in the existence, or clarity of communication, of ethical policy (in terms of nationality, organization and sector variables) is an issue rarely addressed directly in the literature. Here we address the possible influences of cultural and other explanatory variables, and points to general cultural values discussed in the literature which may have a bearing on any explanation of such differences.

Perhaps the most relevant cultural value dimension is Hofstede's concept of 'individualism-collectivism' which suggests that societies which are more collectivist call for greater emotional dependencies of members on their organizations, and more moral involvement with the organization where collectivist values prevail, and more calculative involvement where individualistic values prevail. Collectivism may engender organizational loyalty, but collectivism may also be group-directed rather than organization-directed where little allegiance is given to the corporation.

Further explanation may be provided by Trompenaars' concepts of specific-diffuse relations (or low/high context communications) and universalism-particularism which bring together prior work in this area, and can be used to elaborate on the individualism-collectivism dimension. In individualist cultures low-context communication about such areas as the conduct of employees, business practices and expectations of the company towards its managers, is likely to be explicitly stated such as in the United States, and left implicit in high-context, diffuse and collectivistic societies such as Japan. In individualistic and universalis-

tic cultures people are more likely to adhere to a universal application of rules and laws, and in collectivistic and particularistic cultures are more likely to apply rules according to the relationship they have with the persons with whom they are dealing. As such this dimension may be a possible predictor of adherence to corporate policy on ethical behaviour.

Other possible influences on corporate attitudes which have been proposed in the literature as explanatory variables include size of company, and sector of industry. There is also evidence of the other influences such as national culture of parent company. Indeed evidence in the early 1990s suggested that the increasing prevalence of codes of ethics in Europe is probably a result of the influence of American companies, and that larger companies in Europe (which have the strongest American connections) are more likely to have codes of ethics. Other possible influences which are not developed as explanatory variables in the literature may include the extent and nature of the regulation of the economy. The Federal Sentencing Guidelines in the United States for example, clearly influence corporate attitudes, but so may the strong regulatory consultative provision in an economy such as Germany, and the state involvement in industry in countries such as France.

The extent to which certain ethical issues are seen as important, or a problem to the organization, may therefore be explained by the extent to which a culture is collectivistic, universalistic or to a lack of economic regulation, for example.

The relationship between corporate attitudes towards ethical issues and managers' attitudes towards ethical decision making is a complex one which would seem to be modified by manager's own perceptions of corporate policy, their perceptions of top managers' attitudes, and the way they perceive peer behaviour. These perceptions in turn may be influenced by national culture. In one study, American managers are least convinced (compared with British and Irish managers) that peer and top management influence others' ethical behaviour. This partly confirms another study which found that American managers are least likely to rely on the communication of codes of ethics by top management. Yet another study suggests that what Israeli managers believe their peers to do influences more their own (reported) behaviour than does perceived top managers' beliefs or the existence of a clear corporate policy. There is also a substantial literature on American managers' attitudes which supports the importance of peer influence on managers' own reported behaviour work in Asia-Pacific countries also suggests peer influence is important across cultures.

There is also some suggestion in the literature that personal factors such as age and managerial level may have a bearing. Other factors such as 'personality' are more difficult to define and research.

It is possible for organizations to make direct interventions into these processes, particularly by introducing and publicizing corporate codes of ethics, and by implementing training programmes. It is apparent from the discussion of the literature that the efficacy of these approaches may be influenced by cultural and other factors. Also the extent to which these interventions seek to change attitudes of

managers is an additional factor, and recently the differences in compliance-based and integrity-based approaches to corporate policy has been discussed in the literature. The former can be regarded as attempting to change behaviour (for example, to comply with the letter of the law) and the latter to change attitudes and implicit ethical decision processes (to inculcate a prevailing moral standard within the organization).

When investigating these links between culture and corporate codes of ethics in a study of France, Germany, Britain, Spain and USA, Jackson concluded that the most important finding of his study is that corporate policy would seem to have little influence on managers' ethical attitudes and decision making within organizations, with very little variation across cultures. It seems likely therefore that codes of ethics may only be useful as policy statements for external stakeholders, to enable corporations to comply with legislation, and possibly only in societies which have less well regulated economies such as the United States and Britain. Because corporate policy concerning intra- and extra-organizational relations may not be as clear in well regulated economies such as Germany and France, the perception of top managers' attitudes may be important in influencing managers' attitudes and decision making. Cynicism towards codes of ethics in less well regulated economies may lead to the disparaging also of top managers' attitudes so that they are not held in high regard when it comes to ethical questions. In this case, managers' perceptions of the way peers behave may therefore be more important in the way they are influenced in their own ethical attitudes and decision making. The latter may be in line with a more implicit approach to developing ethical standards in corporations, whereby ethical decision making is internalized, rather than is referenced to ethical criteria legislated for in codes of ethics. This is akin to the 'integrity' approach and distinct from the 'compliance' approach which may be more prevalent in less regulated economies.

The study suggests that formulating codes of ethics in order to influence managers' attitudes and decision making behaviour may be ineffective in less regulated economies and inappropriate in more regulated economies. In the latter it may be more appropriate and effective for top managers to directly communicate their feelings on ethical standards (for example, in France and Germany) down the line, although this may be less effective in less regulated economies. This is not to say that codes do not have a role, but this may simply be in portraying a public ethical image, or complying with legislation in the case of the United States, rather than being used alone to attempt to create an internal corporate ethical identity. Despite some evidence in the literature examined above that training is not very effective in this area, if this could be appropriately directed in order better to develop group dynamics as an influencer of managers' behaviour, this could have value. There may be difficulty in training people in a knowledge-based way for implicit ethical values such as 'compassion'. This may be more difficult where different implicit values prevail in different national cultures. It is perhaps only through more subtle social influences such as peer example that this may develop. In practical terms companies could usefully develop:

- Peer discussion groups to address issues such as pilfering, taking gifts and reporting others' violations of company policies, in order to gain some consensus and to make explicit commonly held views in these areas, particularly bearing in mind that attitudes and behaviours may differ between national cultures;
- Regular or ad hoc stakeholders' discussion groups including suppliers and key customers as well as internal stakeholders including top managers, and home-country and host-country managers, to gain valuable input and to take ownership of output;
- Appropriate information and decision making systems which facilitate decision making in line with the output of discussion groups;
- Training for managers in necessary ethical decision making competences including sensitivity to cross-cultural differences in these areas.

Used together, it is likely that these types of measures would be more effective in building an implicit corporate ethical identity, both within the parent organization and within national subsidiaries, which is more in line with the integrity approach discussed above and takes into consideration cultural difference in corporate attitudes and influences on managers' ethical attitudes and decision making.

## **The Problem: Cultural Relativism Versus Universalism**

The idea of cultural relativism in ethical decision making is common (perhaps more common in practice than in conceptualization). The idea goes something like this. All cultures are different and no culture is any better or worse than any other, they are simply different. It is therefore correct to accept a culture, and its values, for what they are, and not to be judgemental. Therefore, if the value system within one culture allows for corporate bribery, then this should be acceptable. Donaldson believes this position to be untenable, suggesting that people mistakenly endorse cultural relativism, confusing it with cultural tolerance. He argues:

“If a culture disagrees with the Shiite Moslem practice of having women wear veils, yet owing to its tolerance believes nonetheless that it should refrain from forcing its views on Shiite Moslems, then tolerance counts as a moral, not relativist, value ...were a cultural relativist asked whether culture A's belief in tolerance is any better than B's belief that values should be forced down people's throats, the relativist would be forced to deny it. The relativist would not endorse tolerance over intolerance.”

He also claims that cultural relativism requires an absence of any objective grounds for morality, such as a concept of evil and good, for example:

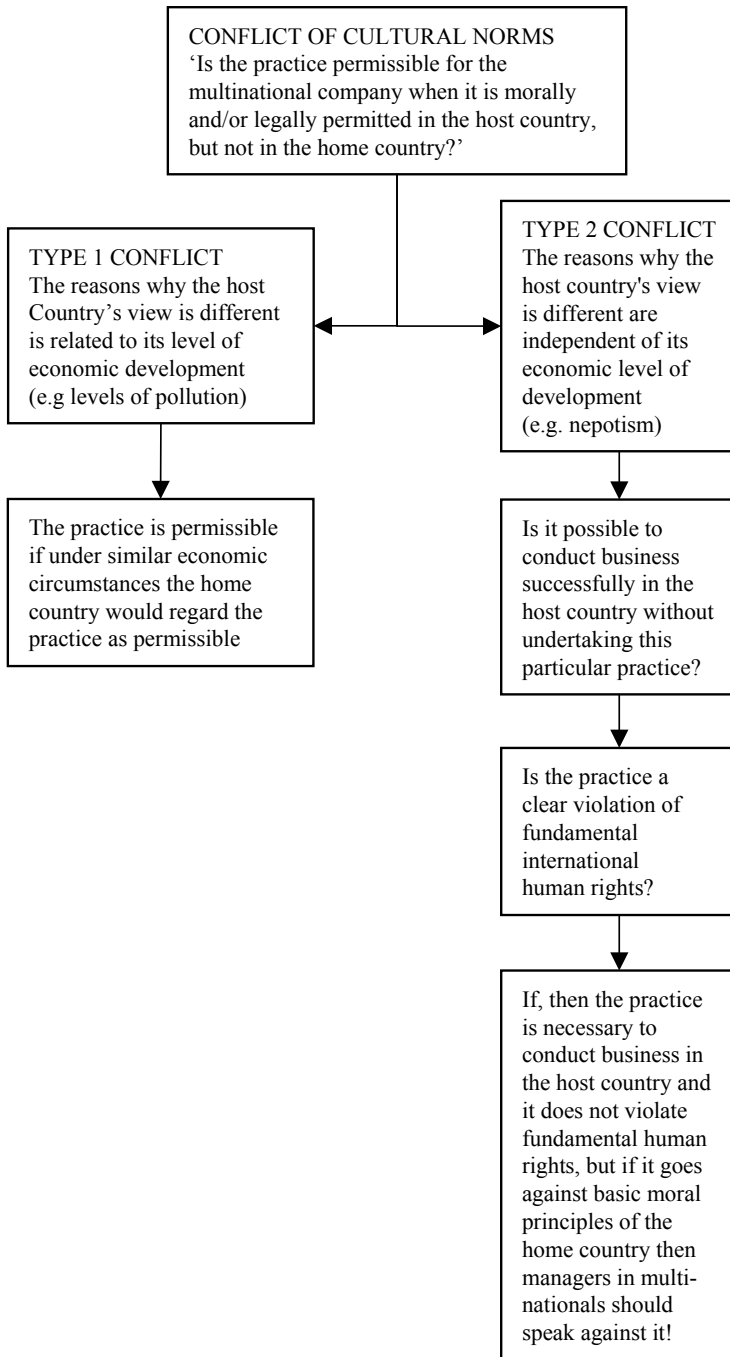


Fig. 1. An algorithm for international ethical decision making (adapted from Donaldson 1989)



„... consider the practice of Japanese Samurai warriors in earlier centuries. A new sword would be tested by murdering a complete stranger. When the sword had been forged, the Samurai would find a stranger in the road, confront him face to face, and without warning swing the sword down in a diagonal arc. If the sword cut neatly from the side of the neck to the waist on the opposite side, it was of adequate quality. If not, it was unfit for a warrior.”

Whilst rejecting a moral free-for-all, and the international arena as a moral ‘free zone’, Donaldson also does not accept the ethnocentric view of applying the moral values of one country (perhaps the United States) on another. It may therefore be difficult to establish a moral objectivity which can be applied in all countries of the world. Instead, he suggests an ‘ethical algorithm’ which provides a guide-line for those attempting to answer the question ‘Is the practice permissible for the multinational company when it is morally and/or legally permitted in the host country, but not in the home country?’

Donaldson separates these two types of dilemmas because practices which purely reflect the level of economic development are easier to empathize with, provided that the home country would do the same thing in similar circumstances (a current debate about the world’s rainforests may fit into this type of category, where the local economy is dependent on tree felling and reflects a level of economic development, but still the developed world is telling these countries to halt the level of tree felling).

An issue such as corporate bribery may not be dependent on the level of economic development of a country, although it may be a reflection of low salaries. This is particularly the case where bribery concerns petty officials in some developing countries. It is often the case that business cannot be done without bribery, and it does not seem to contradict any fundamental international human rights. However, managers from multinational companies doing business in such a country may feel that they have to speak out against such practices. From a purely pragmatic point of view, however, this may cause embarrassment to both the company and to the host country’s government.

## **Making Sense of Ethical Decision-Making Across Cultures**

We have seen from the discussion of cross-cultural differences above that cultural ‘values’ are important to decision making, and particularly so when we consider decisions which are made which cut across national cultures. For example, a Western European business person may do business in a West African country where corporate bribery may be the norm. This involves an interface between two sets of cultural values. The question of what is ethical in this situation? (and also, what is good business?) is raised.

From a cross-cultural perspective, it may be that the value content of the decision is fundamental to an understanding of decision making. To what extent do individual managers consider (consciously) their value system when making decisions? To what degree is their value system an unconscious influence on decision making? What principles (either consciously or not consciously) are applied when decisions are made? What principle should we follow when the other culture's principles or values are different to our own?

Brady distinguishes two basic ethical principles upon which decision making may be based: rules and results. This is based on two main schools of thought in ethics: the 'formalism' of Kant (a German) and the 'utilitarianism' of Bentham (an Englishman).

## Utilitarianism

The utilitarian approach is predominantly a North American one, and this is reflected in much of the management literature on ethical decision making. Here we find the premise that ethical decision making has a pay-off. If only companies are ethical then they will be prosperous. Ethics is good for business. This stems from the principles of utilitarianism which is based on the premise of results or outcomes of a decision. We judge a decision to be ethical on the basis of its perceived outcomes. Utilitarianism in its original form was based on the precept of the greatest good for the greatest number of people. Hence, governments could make policy on the basis that its outcome would benefit the greatest number of people (even at the expense of the minority). A business example could be a decision to make a minority of people redundant from a factory, in order for the factory to be run more cost-effectively and therefore benefit the majority who would remain in the job.

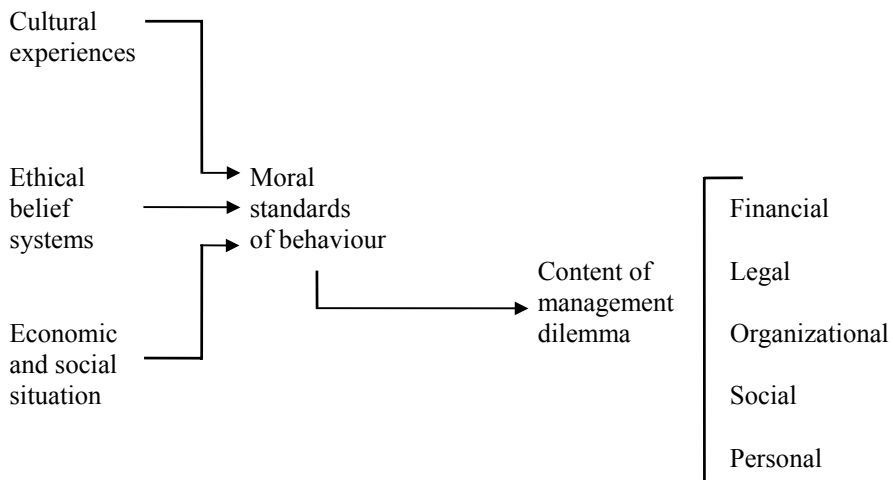
A modern day derivative of this theory is cost-benefit analysis which looks at decisions from the point of view of their total costs, both financial and social, and total benefits. Environmental decisions involving such issues as pollution may be decided on this basis, where the costs of pollution control may be weighed up against the potential benefits to the community.

Utilitarianism tends to be a forward looking philosophy. Decisions are made on the basis of looking into the future, to look at future gains and future costs. However, there are problems in this school of thought. The first is the question of justice. It is perfectly justifiable, using these principles, to persecute a minority in the interests of the majority. Democratic systems are often based on this principle in both the national arena and the organizational arena. There is also the question of subjective benefits, or the way people see the benefits which will accrue to them, and the possibility of 'preference manipulation': persuading people that they will enjoy more benefits from a decision than is possibly the case. So, in negotiations, a manager may 'sell' a decision to his or her opposite number by using manipulative persuasion techniques to convince the other negotiating team of the benefits available to them.

## Formalism

Formalism is independent of wants and needs, and is based on universal moral principles. Instead of anticipating the results of the decision, you ask the question, Is it right? based on certain established principles. Kant's principle is that of the 'categorical imperative' whereby everyone should act to ensure that similar decisions would be reached by others in similar circumstances. As such, formalism is established on the basis of a shared understanding. Everybody (at least within your organization, or within your country) understands the principles of right and wrong which you are applying. This type of decision making principles is backward-looking in perspective as it is based on historically formulated principles. As such it can lead to bureaucratic practice in the following of rules which govern decisions and actions, and can lead to dogmatism. It also tends to ignore individualism. It may be that individuals from different cultures have different preferences for one or the other decision principles.

Hosmer, discussing ethics in making decisions about human resources, develops a useful model of 'ethical analysis' of management decisions.



**Fig. 2.** Model of ethical analysis in management decisions (adapted from Hosmer, 1987)

Within Hosmer's model there is a consideration of moral standards of behaviour, prior to the consideration of the dilemmas facing the decision maker. He describes these as the criteria we use to judge our behaviour and that of others. He warns that they tend to be subjective, imprecise and variable between individuals, they also may vary from one situation to another (for example, our attitude towards lying). We can, and should, trace these moral standards back to our ethical sys-

tems of belief, which we can clarify as providing guiding principles for our decision making. He identifies five such systems of belief summarized in Figure 2.

These ethical belief systems contribute, with cultural experiences and with prevailing economic and social conditions, to moral standards of behaviour within Hosmer's model. It may be that different national cultures tend to have a preference for one of these belief systems in decision making. If systems of belief are different between different cultures (that is, incompatible) then a utilitarian approach (that is a more pragmatic approach) may need to be used when considering ethics issues in international decision making. Donaldson's algorithm discussed above may also provide a useful approach.

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PART V:

## **Global Corporate Ethics**

# Transnational Actors and World Politics<sup>1</sup>

Thomas Risse

## Introduction

The end of the Cold War and globalization processes have led to renewed interest in the study of transnational relations and the impact of non-state actors on world politics. Some authors praise the emergence of a global transnational civil society (Boli and Thomas, 1999; Florini, 2000; Held et al., 1999), while others denounce an increasing transnational capitalist hegemony (Gill, 1995). Both positions ascribe to non-state actors quite an extraordinary influence on outcomes in international politics. It is certainly true that transnational actors – from multinational corporations (MNCs) to International Non-Governmental Organizations (INGOs) – have left their mark on the international system and that we cannot even start theorizing about the contemporary world system without taking their influence into account. But there is little systematic evidence to sustain claims that the transnational ‘society world’ has somehow overtaken the ‘state world’ (see Czempiel, 1991, on these notions). Rather than analyzing transnational and interstate relations in zero-sum terms, it is more useful to study their interactions and inter-penetration. As Reinicke put it, ‘governing the global economy *without* governments is not an option. Yet for global governance to succeed, governments will also have to enlist the active cooperation of nonstate actors’ (Reinicke, 1998, 219). The following review of the literature tries to substantiate this point.

‘Transnational relations’ is a rather elusive concept. If we take the 1971 definition by Keohane and Nye referring to ‘regular interactions across national boundaries when at least one actor is a non-state agent...’ (Keohane and Nye, 1971b: xii-xvi), the concept encompasses anything as long as human agency is involved. Yet, cross-border capital flows, international trade, CNN media broadcasts, international migration, cross-border tourism, the diffusion of values and norms, transnational social movements, INGOs, and Multi-National Corporations are quite different phenomena. It is impossible to theorize about them in any systematic sense. This chapter does not deal with transnational relations in general, but more spe-

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cifically with transnational organizations and actors with a particular purpose. This refinement still comprises a wide range of regularized transnational relationships, from informal networks exchanging material and/or ideational resources to INGOs and large organizations such as MNCs. Some transnational actors operate globally (e.g., Catholic church, International Committee of the Red Cross [ICRC]; Amnesty International; Daimler-Chrysler), while others are confined to specific regions of the world (such as the European Environmental Bureau, Asia Watch, or the European Trade Union Confederation). Some transnational actors concentrate on a single issue (such as the transnational campaign to ban landmines), while others follow a multi-purpose mission such as churches and religious organizations.

This chapter distinguishes among transnational actors along two dimensions. The first dimension concerns their internal structure. Some TNAs are formal organizations (from multinational corporations to INGOs). Others are connected in a far more loose fashion for which I use the term 'network', defined as 'forms of organization characterized by voluntary, reciprocal, and horizontal patterns of communication' (Keck and Sikkink, 1998: 8).<sup>2</sup> Some networks simply consist of groups of individuals, others comprise formal organizations. 'Epistemic communities,' e.g., are networks of individuals and/or organizations based on authoritative claims to consensual knowledge (Haas, 1992b). Advocacy networks comprise actors who share specific values, principled beliefs, and a common discourse (Keck and Sikkink, 1998: 2).

The second dimension which is relevant for this chapter, differentiates between the motivations of various types of transnational actors. Some, such as MNCs or transnational special interest groups, are primarily motivated by *instrumental* goals and try to promote the well-being of the organization itself or the members of the group. Others, such as INGOs, epistemic communities, or advocacy networks are primarily motivated by promoting a perceived 'common good'. This differentiation roughly coincides with the distinction between the 'for profit' and the 'not for profit' sector as frequently found in the literature. However, it is useful to think of this distinction as a continuum rather than sharply divided classes of actors. The business-sponsored Global Climate Coalition certainly proclaims to promote the international public good, while some (I)NGOs seek to make a profit in the humanitarian action sector.

This review proceeds in the following steps. I begin with a brief intellectual history of theorizing about transnational relations in world politics. I conclude from this survey that constructing dichotomies between a society-centered and a state-dominated view of international relations is misleading and distracts from interesting research questions. The main parts of the chapter examine the mutual relationship and interaction between the inter-state world, on the one hand, and the transnational world, on the other. Section three deals with transnational actors and networks as 'dependent variables'. How do states, their institutional structures, as

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<sup>2</sup> Strictly speaking, of course, networks are not actors, but informal structures coordinating the activities of their members.

well as their international relations affect transnational actors, their characteristics and their strategies? The following section changes perspective and looks at the impact of transnational actors and networks on world politics. This is the realm where most empirical research has been carried out in recent years and where we can make some empirically informed theoretical statements. The chapter concludes with some remarks on emerging public-private governance structures comprising states, international organizations, and transnational actors.

## **International Relations and Transnational Actors: An Intellectual History**

Neither transnational relations nor theorizing about them started in the post-World War II era. Multinational corporations with dispersed investments and productions across several political jurisdictions date back at least to the medieval era. During the Renaissance era, ‘family businesses’ such as the Medicis in Florence or the Fuggers in Augsburg held huge investments and production facilities across Europe and had agents in India and China by the end of the sixteenth century (Krasner, 1999: 221). From the sixteenth century on, the trading companies of the imperial powers such as the British East India Company and the Hudson Bay Company operated across continents (Held et al., 1999: 238-239). Similar observations hold true for advocacy groups held together by principled ideas and values. Precursors to modern transnational networks in the human rights and women rights areas include the campaign to end slavery in the United States during the early to mid-1900s (Kaufmann and Pape, 1999), the international suffrage movement to secure the vote for women in the late nineteenth century, as well as the campaigns by Western missionaries and Chinese reformers to end the practice of footbinding in China during the same period (Keck and Sikkink, 1998: ch. 2). While these early transnational movements did not enjoy modern communications technologies such as the internet, their strategies were remarkably similar and sometimes no less effective than those of their modern successors. Krasner concludes, therefore, that rulers ‘have always operated in a transnational environment; autarky has rarely been an option; regulation and monitoring of transborder flows have always been problematic’ (Krasner, 1999: 223).

If the phenomenon of transnational actors is not particularly new, theorizing about them also has its precursors. Yet, scholarship on transnational relations during the eighteenth and nineteenth centuries was much more normative and prescriptive than analytical and descriptive. Take Immanuel Kant, for example. His 1795 ‘Perpetual Peace’ which has become the mantra of today’s literature on the democratic peace, contains ideas on transnational relations (Kant, 1795/1983). His statement that the ‘spirit of trade cannot coexist with war, and sooner or later this spirit dominates every people’ (Kant, 1795/1983: 125 [368]) has been among the first claims about the causal relationship between economic interdependence and



world peace. Long before modern human rights treaties proclaimed individuals as subjects of international law, Kant postulated a right to hospitality by foreigners against the government of their host state. Kant's cosmopolitanism was rather common among liberal intellectuals during the late 18<sup>th</sup> and 19<sup>th</sup> centuries. The modern literature on the democratic peace has largely lost this connection between a democratic society, transnationalism, and peace. Yet, liberals such as Tocqueville argued that transnational relations, i.e., links among democratic societies of different countries and its citizens, constituted a primary tool to prevent wars: 'As the spread of equality, taking place in several countries at once, simultaneously draws the inhabitants into trade and industry, not only do their tastes become to be alike, but their interests become so mixed and entangled that no nation can inflict on others ills which will not fall back on its own head' (Tocqueville, 1994: 660).

While these scholars related the democratic organizations of polities, transnationalism, and peace, liberal writers of the 19<sup>th</sup> century such as Adam Smith or John Stuart Mill took up Kant's ideas about free trade and peace. Yet, World War I which was fought among highly interdependent nations, discredited the idea that economic interdependence alone is a sufficient condition for peace in the absence of democracy. Schumpeter's 'Sociology of Imperialism' constitutes perhaps the most elaborate statement of the interwar period on the causal relationship between liberal capitalism, economic interdependence, and peace. He argued that the essence of capitalism is anti-imperialist, but recognized that capitalist states might pursue aggressive foreign policies if they are usurped by particular economic interests (Schumpeter, 1919/1953). Schumpeter reacted primarily to Marxist theories of imperialism, particularly Lenin's writings, who claimed exactly the opposite, namely that imperialist wars resulted from the externalization of the internal class struggles toward the outside world and the eternal capitalist strive for new markets and profit-making. Lenin argued that wars among capitalist states were inevitable in a stage of development 'in which the dominance of monopoly and finance capital has established himself' (Lenin, 1917/1939: 89). The controversy about the precise relationship between economic interests, capitalism, and economic interdependence, on the one hand, and aggressive/imperialist foreign policies as well as peace and war, on the other, continues until today.

With the emergence of international relations as a social science discipline, scholars increasingly employed analytical rather than purely normative arguments. Mitrany, the founder of modern functionalism and integration theories argued in 1943 that technology and technical issues confronting the industrialized democracies in the 20<sup>th</sup> century necessitated international cooperation along functional lines. Organizations for functional collaboration would eventually overcome the political institutions of the past including the nation-state (Mitrany, 1966/1943). After World War II, regional integration theory and, particularly, neofunctionalism (Haas, 1958) reformulated the argument claiming that rational economic behavior not only leads to transnational interdependence, but also to the creation of supranational institutions as stable peace orders such as the European Community.

It is important to note here that (neo-) functionalism never fell into the trap of later theorizing about transnational relations which created a dichotomy and adverse relationship between a 'society-centered' and 'state-dominated' perspective on world politics. Rather, the argument was about – in today's terms – the emergence of international institutions and supranational governance structures resulting from, responding to, and facilitating transnational interactions of private actors.

This also holds true for another version of integration theory, one of the most important predecessors of today's constructivism, the analysis of transnational and supranational community-building by Karl W. Deutsch and his colleagues (Deutsch, 1957). Deutsch argued that increasing transaction flows and crossborder communication as facilitated by trade, migration, tourism, educational exchanges, and the like, lead to a sense of community among people and to collective identification processes. 'Pluralistic security communities', while retaining the legal sovereignty of its member states, possess a 'compatibility of core values derived from common institutions, and mutual responsiveness – a matter of mutual identity and loyalty, a sense of 'we-ness', and are integrated to the point that they entertain 'dependable expectations of peaceful change' (Adler and Barnett, 1998b: 7, quoting Deutsch, 1957: 5). In line with the behaviorist orientation of the time, Deutsch and his colleagues measured transnational transactions quantitatively and compared them to the transaction flows inside the countries in order to determine the degree of international community-building. Deutsch's work in this area was largely ignored until recently when constructivist scholars picked up and reformulated his insights (see e.g., Adler and Barnett, 1998a).

In the meantime, the question of transnational relations was relegated to the sidelines of theorizing on either side of the Atlantic. Explicit analytical work on transnational actors and relations started during the late 1960s and early 1970s, both in the U.S. and in Europe (Cooper, 1968; Vernon, 1971). In 1969, the flagship journal of the German Political Science Association, *Politische Vierteljahresschrift*, published a special issue entitled '*Die anachronistische Souveränität*' (anachronistic sovereignty) which contained an essay on 'transnational politics' (Kaiser, 1969). Two years later, the journal *International Organization* followed suit with a special issue edited by Keohane and Nye on 'Transnational Relations and World Politics' (Keohane and Nye, 1971a; see also Huntington, 1973; Keohane and Nye, 1977; Rosenau, 1980). These and other works challenged the state-dominated view of world politics. Rosenau in particular attacked the state-centered paradigm of international relations theory promoting the 'transnationalization of world politics', a subject to which he came back ten years later (Rosenau, 1990).

This early literature was theoretically inspired by a broader critique of the concept of the state in political theory and in comparative politics. Liberal pluralist theories defined political systems functionally in terms of the authoritative allocation of values in a given society. Societal interest groups and organizations substantially constrained political actors and the political process was largely conceptualized by conflict and bargaining among these societal groups. The work on trans-

national relations of the late 1960s and early 1970s transposed pluralist theory to the level of international affairs. But this work did not produce a theory of transnational politics in the sense of testable propositions. It focussed on the international political economy, in particular the rise of multinational corporations in the post-World War II era. INGOs and other transnational actors were not yet subject of systematic inquiry (see, however, Huntington, 1973; Vallier, 1971). One of the first volumes explicitly dealing with INGOs used the term 'pressure groups' suggesting an analysis commensurate with the study of interest groups (Willetts, 1982).

The 1970s also saw a revival of critical political economy attacking transnational economic relations in general and the role of multinational corporations in particular with regard to the North-South relationship. Dependency theory argued against liberal free trade economists that under-development results from the structural dependency and the integration of the developing world in the world economy. MNCs in particular were seen as the main agents preventing the development of an endogenous industry in Southern countries, transferring their profits from the South to the North and exploiting cheap labor in the developing world (see, e.g. Amin, 1977; Emmanuel, 1972; Frank, 1967). Dependency theory constituted the first major contribution to the subject of transnational relations by Latin American, African, and Asian scholars, even though most of its propositions could not be confirmed empirically (see e.g. Caporaso, 1978; Menzel, 1992).

But liberal arguments about transnational relations of the 1960s and 1970s claiming an end of the state-centered view of world politics, did not survive the counter-attack of realism, either. In the 1971 'Transnational Relations and World Politics' volume, Gilpin had already argued against the liberal grain that MNCs were primarily an instrument of American foreign policy and power, not the other way round (Gilpin, 1971, 1975). The late 1970s and early 1980s then saw a revival of (neo) realist theory (Waltz, 1979). Hegemonic stability theory was the realist response to the liberal interdependence arguments.

The result was rather profound, particularly in the U.S. Ruggie, Keohane, and Nye had originally theorized about international regimes by arguing that economic interdependence led to increased interstate conflicts to be regulated by international institutions (Ruggie, 1975; Keohane and Nye, 1977). This connection between transnationalism and international institution-building was mostly lost during the early 1980s when regime analysis and neoliberal institutionalism took off. The main controversy between neorealism and neoliberal institutionalism concerned the prospects of 'cooperation under anarchy,' i.e., of cooperation among states (cf. Baldwin, 1993). In Europe, a state-of-the-art volume of the German-speaking international relations community did not bother to deal with transnational relations, except for a sharp critique of the disappointing accomplishments of the interdependence literature (Kohler-Koch, 1990).

Two developments of the late 1980s re-opened intellectual space for theorizing about the cross-border activities of non-state actors in the U.S. and Europe. First, the late 1980s saw the beginning of what would later be called constructivism or sociological institutionalism in international relations (Kratochwil and Ruggie, 1986;

Wendt, 1987; Kratochwil, 1989). Kratochwil, Ruggie, and Wendt drew attention to the social and ideational rather than simply material structure of international relations (for the most comprehensive statement see Wendt, 1999). Second, the end of the Cold War should not be underestimated in its impact on international relations theorizing. The failure of traditional international relations theory to at least recognize some underlying trends, pushed many scholars away from structuralist theories such as realism and state-centered institutionalism to a renewed appreciation of domestic politics, on the one hand, and of transnational relations, on the other.

As a result of these two developments, the 1990s saw a revival of theorizing about transnational actors, a trend which was further enhanced by the debate on 'globalization'. First, Rosenau's book on 'Turbulence in World Politics' constituted a sweeping statement on postinternational politics marked by a 'bifurcation in which the state-centric system now coexists with an equally powerful, though more decentralized, multi-centric system' characterized by transnational 'sovereignty-free actors' (Rosenau, 1990: 11; also Rosenau, 1997). Second, a 1992 special issue of *International Organization* elaborated the notion of transnational 'epistemic communities', defined as networks among professionals with an authoritative claim to policy-relevant knowledge (Haas, 1992c). The authors used constructivist work on socialization, cognitive evolution, and learning in order to theorize about the relationship between consensual knowledge and power (Adler and Haas, 1992). Third, a 1995 volume (Risse-Kappen, 1995b) argued that the impact of TNAs on outcomes depends on the domestic structures of the polity to be affected and the extent to which TNAs operate in an environment regulated by international institutions. Fourth, Keck and Sikkink elaborated the concept of transnational advocacy networks and explored their impact in the human rights and environmental spheres (Keck and Sikkink, 1998). Finally, Reinicke's book on 'global public policy' represents one of the first attempts to systematically analyze governance networks involving public and private actors on the international level (Reinicke, 1998).

Compared to the attempts of the 1970s, these latest moves at thinking about non-state actors in world politics share three characteristics:

1. While the empirical literature on transnational relations of the 1970s largely concentrated on MNCs, this focus on the international political economy is now taken over by the literature on globalization. The new transnationalism of the 1990s concentrates more thoroughly on the transnational non profit sector, such as 'epistemic communities', value-based advocacy networks, INGOs, and cross-border social movements.
2. The recent literature is much more about the *interaction* between states and transnational society than about *replacing* a state-centered view with a society-dominated perspective. One indicator of this trend is the increasing replacement of traditional regime analysis with its focus on inter-state institutions by a 'governance without government' perspective emphasizing non-hierarchical networks among public and transnational actors (see, e.g. Czempiel and Rosenau, 1992; Kaul et al., 1999; Kohler-Koch, 1998b; Cutler et al., 1999; O'Brien et al., 2000).

3. As mentioned above, constructivism and sociological institutionalism have influenced recent work on transnational relations. This has resulted in work focussing on transnational actors promoting and diffusing causal knowledge (epistemic communities) and norms (advocacy networks). As to critical theory, neo-Gramscianism and its contribution to the literature on the international political economy has to be mentioned (e.g. Cox and Sinclair, 1996; Gill, 1993).

In the following, I discuss the recent work on TNA in more detail. I begin with the impact of the ‘inter-state world’ on the ‘transnational society world.’

## The Impact of the Inter-State World on TNAs

The nation-state system and its structuration of the world along territorially defined boundaries has a profound impact on both the nature and the activities of transnational actors. The very concept of *transnational* relations implies an international system composed of nation-states as well as the distinction between state and societal actors within a given nation-state. It makes little sense to talk about transnational actors in a world of empires or in a medieval world of cross-cutting authority structures. However, most empirical work on transnational actors remains rather unidirectional by looking at the impact of TNAs on inter-state relations, international organizations, and international institutions in general. We know rather little about states and IOs enabling and/or constraining TNA activities.

### TNAs as Instruments of National Governments and IOs

On the one end of the theoretical spectrum are those (realists) for whom the growth of transnational relations in the contemporary international system essentially reflects the interests of the most powerful states. Gilpin developed this argument most eloquently, namely that it was U.S. post-war foreign policy and the U.S. hegemony in the international political economy that enabled the rise of MNCs and economic interdependence in the first place (Gilpin, 1971, 1975). To ask the counterfactual, would we still experience economic globalization if Adolf Hitler had won World War II?

Gilpin’s argument shows some similarities with the claims by critical theorists such as Cox, even though the causal mechanism is different. Cox argued that post-World War II American hegemony arose from a confluence of three factors, the hegemony of U.S. capitalism and its particular mode of production, the power of the U.S. state, and the consensual nature of Western liberal ideas (Cox, 1987; Cox and Sinclair, 1996). Cox concluded that U.S. hegemony enabled the rise of transnational (economic) relations in the post-war era in the first place. From a liberal perspective, Nye argued in a similar fashion that the days of American hegemony

in the world system are far from over, even though its economic preponderance has gone. U.S. 'soft' power and the hegemony of U.S. economic, political, and cultural ideas continue to secure the current world order (Nye, 1990).

One could develop this argument further and point out that the international free trade order – from the GATT to the World Trade Organization (WTO) – and other international institutions which are ultimately based on inter-state agreements both enable and constrain transnational interactions by regulating them. The legal framework provided by states and international institutions has, thus, constitutive effects on transnational actors and relations. The international refugee regime, for example, defines refugees and their rights in the first place.

While Gilpin's work focusses on the international political economy, a similar argument has emerged in security studies. Thomson argued in a historical study that state rulers in the thirteenth century Europe began authorizing the international use of force by private armies (privateers, mercenaries etc.) in order to accumulate power and wealth (Thomson, 1994). When the unintended consequences of this privatization of international violence became obvious, rulers of the eighteenth and nineteenth centuries struggled against pirates and mercenaries in order to (re)gain the monopoly of the international use of force. The modern state monopoly over the means of internal and external violence did not fall from heaven, but resulted from a sustained conflict between states and TNAs which the states ultimately won (see, however, the rise of global terrorism, of piracy in East Asia and of private armies in 'failed states').

In sum, these authors share the view that state power and state foreign policies gave rise to contemporary transnational relations (and globalization, one might add) where it suited their interests, but viciously fought these transnational forces when it did not. Realists would conclude that, when powerful states are pitched against transnational actors, even mighty ones, the former usually win over the latter (overview in Krasner, 1995b: 267-276). This latter assertion, however, does not follow from recognizing state power and international institutions as enabling transnational relations and has been challenged by the recent literature on TNAs.

The question concerning transnational actors as instruments of state power must also be asked with regard to the non-profit sector of INGOs and transnational advocacy networks. Unfortunately, there is little empirical work available in this area. Some preliminary observations can be made, though. First, INGOs by and large originated in the Western industrialized world and they are extremely unevenly spread across the world regions. 'The global stratification structure is clearly reproduced in INGO participation. Residents of resource-rich, technically developed, older, formally democratic Anglo-European countries participate the most; residents of poor, less developed, newer, less democratic countries participate the least' (Boli et al., 1999: 69). Does the INGO world then represent a 'global civil society' (Wapner, 1996) or does it merely reproduce *Western* enlightenment values such as universalism, individualism, progress, and cosmopolitanism? INGOs as part and parcel of a 'world culture' dominated by Western liberal hegemony?

Second, many INGOs are more directly dependent on the 'state world' than many of them would admit. Particularly in the issue-areas of international development and humanitarian aid, funding for the grassroot activities of INGOs originates to a large extent from public sources. According to the World Bank, public funding for development NGOs increased from 1.5 % of their total income in the early 1970s to 30 % in the mid-1990s. Some scholars estimate that the dependency of Southern NGOs on public funding by states or IOs reaches 80-90 % (according to Hulme and Edwards, 1997a: 6-7). The percentage of EU relief aid channeled through INGOs reached rose from 47 to 67% from 1990 to 1994. Even in the human rights area where one would expect most INGOs to be heavily critical of state policies, more than half of the organizations claimed to have received public funding (Smith et al., 1998). In the context of the European Union (EU), it has been frequently pointed out that the European Commission both created and funded many transnational organizations in order to be able to deal with societal interests on a European rather than on the various national levels (Kohler-Koch, 1994; Greenwood and Aspinwall, 1998).

TNA dependence on the resources of states and international organizations suggests that it would be preposterous to claim that the INGO world simply represents global civil society *against* the inter-state system. Transnational advocacy groups and epistemic communities often perform tasks which states and international organizations either cannot or do not want to carry out. In the issue-areas of foreign and humanitarian aid, states and IOs often subcontract (I)NGOs, because these groups are less bureaucratic, more flexible and can reach those in need of assistance more easily. The World Bank and other organizations have long recognized that strengthening civil society in the developing world through INGO networks contributes to political, economic, and social development. In the human rights and environmental areas, transnational actors provide monitoring capacities and supply information to states and international organizations which would otherwise not be available because of concerns about sovereignty rights. In the international economy, states have delegated regulatory authority to transnational private actors, e.g., in international standard setting, because they can carry out these tasks more efficiently (Cutler et al., 1999). Last not least, taking the concerns of INGOs on board also increases the legitimacy of international institutions such as the World Bank or the International Monetary Fund (O'Brien et al., 2000). As Forsythe argued already in the mid-1970s with regard to the International Committee of the Red Cross (ICRC), it cooperates with and, therefore, stabilizes the state system in war-making (see Forsythe, 1976).

In sum, transnational advocacy groups and INGOs should not be seen as necessarily in opposition to the inter-state system. Rather, their work often conforms to the interests of states and international organizations. But little is known how the increasing role of the INGO world in global governance affects these groups themselves in terms of their institutional structures, and strategies (see the contributions in Hulme and Edwards, 1997b; Edwards and Hulme, 1996). E.g., the growing involvement of INGOs in partnerships with IOs might alienate them from

their own social base in civil society (Finger, 1994). INGOs working with the World Bank, the IMF, or the WTO, for example, need to moderate their goals considerably, since they have to accept the principal goal of liberalization in order to promote human rights and environmental concerns effectively (O'Brien et al., 2000: 224). This might then lead to increasing tension between more radical transnational social movements and more 'professional' and moderate INGOs.

### Institutional Similarities Between TNAs and Structures of Governance

The works discussed so far adopt an actor-centered perspective to discuss the influence of state governments and international institutions on TNAs. The question was how state actors impact upon transnational actors and how the latter actually perform functions which states or international organizations cannot or are unwilling to carry out. A second, though even less-developed argument takes a more structural perspective and asks how institutional features of states or international regimes and organizations – i.e., domestic and international 'structures of governance' – impact upon institutional characteristics of transnational actors. Krasner, for example, took a sociological institutionalist perspective and argued that the 'institutional structures of transnational actors must reflect the institutional environment within which they function' (Krasner, 1995b: 260). Domestic laws, for example, constitute a strong tool forcing transnational actors to adjust their institutional structures to the country in which they operate. As a result, U.S. Honda looks different from its Japanese mother company, even though it is still institutionally different from General Motors or Ford. While the Catholic Church constitutes a quintessential transnational organization which preceded the modern state system, it still had to adjust to the domestic structure of the state in which it operates (see Vallier, 1971). Church-state relations in, say, Germany where the churches enjoy quasi-public status, differ profoundly from the U.S. where the Catholic church is treated like any private organization.

Doremus et al. have carried this line of argument further (Doremus et al., 1998) by investigating the internal structure and activities of MNCs operating out of Germany, Japan, and the U.S. (see also Pauly and Reich, 1997). They claim that the current talk of 'global corporations' and 'global players' constitutes an, albeit powerful, myth: 'Despite intensifying international competition, MNCs are not promoting the ineluctable convergence and integration of national systems of innovation, trade, and investment, nor are they forcing deep convergence in the national economies in which they are embedded. They cannot do so because they themselves are not converging toward global behavioral norms' (Doremus et al., 1998: 3). Globally operating MNCs do not at all look alike, but maintain distinct institutional features pertaining to their organizational structure and culture which originate from the national institutional environment in which the mother company operates.



If these claims hold true for private transnational actors such as MNCs which command powerful economic resources, similar arguments should be relevant for INGOs and the transnational non-profit sector. To begin with, states and national governments control access to a territory. Moreover, transnational actors operate in institutional environments which are largely determined by the domestic structures of nation-states. Amnesty International in the U.S. has to abide by different laws than, say, Amnesty International in Germany. As a result, their internal organizational structures are likely to diverge.

International institutions are also likely to shape organizational features of transnational actors. The EU, for example, represents an international governance structure which has given rise to particular forms of transnational interest organization. The European Commission has actively encouraged the formation of transnational organizations in Brussels, both traditional interest groups and not-for-profit INGOs. The result is a rather pluralist structure of interest organization at the EU level, in contrast to more corporatist structures with strong peak organizations in some member states (see, e.g., Kohler-Koch, 1994; Greenwood and Aspinwall, 1998).

Finally, international rule structures such as norms embedded in treaties and international regimes provide an enabling environment for transnational network activities. Take the human rights area, for example. The emerging legalization of the international human rights regime went hand in hand with an increasing professionalization and even bureaucratization of INGOs such as Amnesty International or Human Rights Watch. They changed their character from transnational social movements to professional organizations employing a large staff of lawyers, media experts, and country specialists. Yet, the empirical evidence on how institutional structures of the politics – both national and international – in which TNAs operate shapes the latter's organizational structures and cultures remains sketchy at best. Most of the empirical work so far has concentrated on the question how and under what conditions TNAs of various sorts have managed to affect the nation-state, international institutions, and IOs. The realist and state-centered legacy in international relations theory required that scholars first established that TNAs mattered before they could study how domestic and international institutions shaped the organizational structures of INGOs and the like. Such work could, for example, draw on the literature on 'political opportunity structures' which originated from scholarship on social movements, but has reached work on transnational actors rather recently (e.g. Thomas, 2001; on 'political opportunity structures' see Tarrow, 1996; Kitschelt, 1986).

## **The Impact of Transnational Actors on World Politics**

So far, I have discussed the literature with regard to how the 'state world' impacts upon the transnational 'society world'. As mentioned above, however, most of the

empirical work poses the question the other way around and asks what effects, if any, TNAs have on structures and processes of world politics. There is one important difference between scholarly controversies of the 1990s as opposed to the 1970s and 1980s. Most of the contemporary work in international affairs does no longer dispute that transnational actors influence decisions and outcomes (compare, e.g., Waltz, 1979 with Krasner, 1995b, 1999). Rather, current scholarship focusses on the *conditions* under which these effects are achieved and most of the controversies center around the significance of these intervening factors (e.g. Kaufmann and Pape, 1999; Moravcsik, 2000).

However, a body of literature mostly concerned with studying 'globalization' (see Zürn, 2002) goes much further and claims that the transnational 'society world' has not only profoundly changed the 'state world', but has made obsolete the current order of international relations as an inter-state system (see e.g. Strange, 1996; Gill, 1995; Amin, 1997). We do not live in a borderless world, but political, social, and economic boundaries cease to coincide and to be confined to the nation-state (e.g. Brock and Albert, 1995; Ferguson and Mansbach, 1996; Ruggie, 1993; Wolf, 2000). Even talking about transnational as opposed to state actors becomes problematic, the more we accept that the current 'Westphalian' system of nation-states is coming to an end and that political authority is increasingly structured along functional rather than territorial lines (Caporaso, 2000).

In the following, however, I bracket this discussion. I take a more 'pedestrian' and actor-centered approach and ask how and under which conditions specific TNAs such as multinational corporations and 'non-profit' INGOs affect outcomes in world politics. I put somewhat more emphasis on the non-profit sector.

## Globalization and MNCs: 'Global Players' as Sources of Policy Convergence?

As mentioned above, both the liberal and the critical-marxist literature on transnational relations of the 1970s focussed on the role of MNCs in world politics. At the time, the main controversies centered around the question of whether MNCs contributed to or hindered economic development (overview in Gilpin, 1987: ch. 6, 7; see also Maxfield, 2002). Realists argued that MNCs were irrelevant for developments, since national government remained largely in control of development policies, even in the less developed world (e.g., Krasner, 1978). Liberals and modernization theory claimed that MNCs had an overall positive effect on economic modernization by guaranteeing an open world economy based on free trade and by exporting capital, know-how, and modern values into less developed countries (for an early statement see Huntington, 1968). Critical theorists, particularly 'dependistas', maintained that, on the contrary, MNCs were among the main culprits of uneven development by essentially extracting

resources from developing countries which were desperately needed for economic development (e.g. Frank, 1967; Amin, 1977).

Twenty years later, this controversy has largely disappeared, for two reasons. First, as Menzel claimed, *the Third World has ceased to exist* (Menzel, 1992). The differentiation process among developing countries led to functionally equivalent paths to economic development (compare, e.g., the Latin American experience with South East Asia). As a result, it is impossible to sustain a unifying theory of MNC impact on economic development such as claimed by either modernization or dependency theorists. MNC impact on development varies enormously depending on social, political, and cultural structures in target countries (Clark and Chan, 1995).

Second, accounts ascribing an enormous influence of MNCs on less developed countries usually overstate their significance for the local economies. On a world-wide scale, overseas production of firms as a percentage of world GDP has risen from 4.5% in 1970 to 7.5% in 1995, while the sales of foreign affiliates of MNCs have doubled to ca. one quarter of world GDP in the meantime (according to Held et al., 1999: 246). These figures already challenge some exaggerated arguments about 'globalization', at least in production. Interestingly enough, the significance of MNCs and their local affiliates is even lower for the developing world, as concerns production as percentage of GDP (6.3 % in 1995). While the developing world and Eastern Europe since the end of the Cold War have taken part in the boom of Foreign Direct Investments (FDI) starting in the late 1980s, most FDIs still take place within the industrialized world. In fact, the proportion of FDI stocks in developing economies as compared to the OECD world has fallen from 32.3% in 1960 to 25.3% in 1994 (Held et al., 1999, 249). In sum, FDI and MNC activities are largely concentrated within the industrialized world, both intra- and inter-regional.

As a result of these patterns, the debate about MNC impact on world politics in the 1990s largely concentrated on the developed world in the context of discussions about 'globalization' and internationalization (for a useful overview see Held et al., 1999: ch. 5). This controversy is far from over, since the very notion of 'globalization' is heavily contested in the literature, let alone the impact of so-called 'global players' such as MNCs (see the excellent review in Beisheim and Walter, 1997; also Keohane and Milner, 1996; see also Zürn, 2002). The debate largely concentrates on the effects of MNCs and other transnational market forces on the nation-states, in particular the ability of industrialized countries to conduct their own 'autonomous' economic and monetary policies (see also Cohen, 2002).

The 'convergence hypothesis' holds that 'the authority of the governments of all states, large and small, strong and weak, has been weakened as a result of technological and financial change and of the accelerated integration of national economies into one single global market economy' (Strange, 1996: 13-14; see also Stopford and Strange, 1991). There is widespread agreement that the MNCs' ability to shift production elsewhere and their capacity as transnational

actors to allocate financial and other resources to places promising the highest profit rates severely circumscribe the autonomy of national governments to take economic decisions. The more a national economy is integrated into global markets, the higher the costs of a national economic policy which is not oriented toward liberalizing markets, but toward expansionary monetary and fiscal policies to create full employment. Since the latter policies are usually identified with center-left rather than center-right governments, the former should be more severely constrained in their policies than the latter (Milner and Keohane, 1996: 17-18). The result is a growing convergence of national economic policies toward neoliberalism and monetarism.

Critical theory in the neo-Gramscian tradition agrees with the overall description of recent trends, but explains it differently. Gill and others see an emerging transnational 'historic bloc' establishing the hegemony of transnationally mobile capital and relevant capitalist classes. The industrialized nation-states have not been passive by-standers of these trends, but have actively encouraged and contributed to it through, e.g., the liberalization of capital markets and the encouragement of FDIs. At the same time and with the demise of Keynesianism, neoliberalism became the dominant ideology of how to run a national economy shaping the worldviews of transnational elites, policy-makers, and other actors (Gill, 1995; Gill and Law, 1993). In the neo-Gramscian view, it is this confluence of modes of production (transnational), international and national institutions, and dominant ideas which constitute transnational global hegemony. What is less clear in this rather sweeping argument, is how it can be disconfirmed, i.e., how do we know transnational hegemony when we see it? Van Apeldoorn has recently applied the neo-Gramscian argument which takes constructivist work on the role of ideas into account, to the European Roundtable (ERT) of businesspeople and CEOs from major European MNCs (Van Apeldoorn, 1999). He claims that the ERT has successfully shaped the economic agenda of the EU toward the neoliberal paradigm, starting with the Single European Act and culminating in the Economic and Monetary Union (EMU). His point is not so much that the ERT lobbied for particular policies, but that it moved the dominant ideology toward an, albeit 'embedded,' neoliberal agenda.

The emerging literature on globalization, internationalization, and the role of MNCs in the international economy has only started to tackle these questions (see Zürn, 2002). The more empirical evidence becomes available about the domestic effects of the internationalization of production, the more it becomes clear that generalizations such as the 'convergence' hypothesis miss the mark. First, we can observe a transformation of national economic policies rather than a broad 'retreat of the state'. Second, the scholarly discussion moves toward specifying the conditions under which nation-states are more or less able to face the challenges of internationalization without giving up social and democratic values. Similar trends toward differentiated arguments can be observed when we look at the literature on the other type of transnational actors to be discussed here, advocacy networks and INGOs.

## The Power of Principles and Knowledge: Transnational Advocacy Networks and INGOs

There is a growing consensus in the literature that INGOs and other non profit TNAs make a difference in world politics. Scholars have collected evidence that advocacy networks, epistemic communities, and other TNAs can have a substantial impact on state policies, on the creation of international norms, and on the diffusion of these norms into domestic practices (e.g., Evangelista, 1999; Risse-Kappen, 1995a; Keck and Sikkink, 1998; Price, 1998; Florini, 2000; Princen and Finger, 1994; Litfin, 1994; Haas, 1992c; Willetts, 1996, Risse et al., 1999; Checkel, 1997; Klotz, 1995; Finnemore, 1996a; Smith et al., 1997; Boli and Thomas, 1999; O'Brien et al., 2000). While these and other works provide evidence that the power of knowledge and of principled beliefs matters in world politics, the more interesting question is why and under what conditions? But many studies do not lead to generalizable conclusions, since they suffer from methodological problems such as case selection on the dependent variable. There are many single-case studies of successful transnational campaigns, while we know much less about failed campaigns (see, however, Evangelista, 1999; Cortright and Pagnucco, 1997). The propositions emerging from the literature can be grouped under the following categories:

- International material and institutional conditions;
- Domestic conditions;
- Complex models linking the international and domestic levels;
- TNA strategies and socialization processes.

### International Conditions for TNA Impact

Realist-inspired authors essentially argue that the more transnational actors and coalitions succeed in changing the preferences and policies of the most powerful states, the greater their impact in international affairs becomes. Only great powers enjoy the ability and capacity of affecting outcomes in world politics as a result of which transnational actors need to influence their decisions and policies in order to make a difference (e.g. Krasner, 1993, 1995a). The proposition no longer claims to account for state preferences in the international system and, thus, does not explain why great powers sometimes promote INGO goals in international relations. A stronger version of the argument would have to maintain that great powers only promote 'soft norms' such as human rights or environmental concerns, if it suits their security and/or economic interests. In this latter formulation, TNA impact becomes more or less epiphenomenal.

Whether in its stronger or in its weaker form, a systematic evaluation of the argument in the human rights area has not shown much evidence for the proposition that transnational actors had first to convince great powers in order to influence

outcomes and decisions in international affairs (Risse et al., 1999). While it certainly helps if the governments of great powers start promoting the goals of transnational advocacy networks, this is neither a necessary nor a sufficient condition for TNA impact. This work on the impact of transnational networks on the domestic implementation of human rights norms in various regions of the world shows that great powers are rarely decisive in promoting these norms, because they rarely pursue consistent human rights policies. Realism might well explain that great powers do not promote human rights when it does not suit their strategic or economic interests, but precisely for this reason it cannot account for the substantial TNA influence on the implementation of human rights in domestic practices across the world regions.<sup>3</sup>

While the realist proposition has not yet been systematically tested in other issue-areas of world politics, there is circumstantial evidence to challenge it. INGO impact despite great power resistance has been amply documented in the environmental area (e.g. Keck and Sikkink, 1998: ch. 4; Lipschutz and Mayer, 1996; Princen and Finger, 1994), but also in international security. In the case of the international treaty banning landmines, for example, transnational advocacy networks succeeded, even though they were pitched against the fierce opposition of several great powers including the U.S. (Price, 1998).

But structure is not confined to the material realm. We need to take the social structure of international politics into account. I argued in my earlier work (Risse-Kappen, 1995a) that TNAs are expected to increase their political influence, the more they act in an international environment which is heavily structured by international institutions. International organizations, for example, provide arenas enabling regular interactions between TNAs and state actors. In some cases, they actively encourage (and even finance) INGOs and other transnational coalitions. The European Commission, the World Bank, and the developmental sector are cases in point (see, e.g., Imig and Tarrow, 2001 ; Chabbott, 1999). The more IOs and Western states realized that their developmental policies and foreign aid had to be targeted to the civil societies in Third World countries, the more they came to rely on the INGO world linking the local and the global. The strong collaboration between the World Bank and the INGO world did not result in a less contentious relationship between the two, even though sharp divisions among INGOs emerged concerning how far one should cooperate with the World Bank (O'Brien et al., 2000). The United Nations system provides another arena for INGO participation. The UN World Conferences in particular have served as important focal points for the activities of transnational advocacy networks (Clark et al., 1998; see also Weiss and Gordenker, 1996). Moreover, the UN and its various organizations increasingly serve as fora where transnational actors and state officials regularly meet and interact (see e.g. Willetts, 1996; Finger, 1994).

It is one thing to argue that international institutions provide arenas in which the activities of transnational actors are allowed to flourish. It is quite different to

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<sup>3</sup> I owe this thought to Anja Jetschke.

conclude that, therefore, they should have a policy impact on IOs, international regimes, and state policies. The above proposition probably needs refinement. International governance arenas such as the UN system or regional organizations such as the EU certainly provide TNA with regular *access* to policy-making. But access does not guarantee *impact*. As Clark et al. showed, NGO influence on policy outcomes of UN world conferences varied significantly according to subject area and countries involved (Clark et al., 1998).

We probably need to differentiate among various phases in the international policy cycle, such as agenda-setting, international norm creation, and norm implementation. It is safe to argue that *ceteris paribus* the influence of transnational advocacy networks has always been greatest during the agenda-setting or 'norm emergence' phase of a 'norm life cycle' (Finnemore and Sikkink, 1998). Since TNAs provide moral authority and knowledge about causal relationships, they are particularly crucial when it comes to paradigm shifts on the international agenda. One can probably go as far as to argue that there has rarely been a new normative issue on the international agenda which has not been advocated by transnational advocacy coalitions, INGOs, or epistemic communities. In the international political economy, for example, an epistemic community put Keynesian ideas of 'embedded liberalism' on the international agenda during the negotiations establishing the Bretton Woods system and the GATT (Ikenberry, 1993). In the environmental area, examples include the protection of the ozone layer, global warming, deforestation, wildlife conservation, and other questions (Haas, 1992a; Hurrell, 1992; Keck and Sikkink, 1998: ch. 4; Raustiala, 1997; Ringus, 1997; Princen, 1995; Litfin, 1994). Concerning human rights, the origins of almost every single post-World War II international human rights agreement can be found in the activities of transnational advocacy networks (Korey, 1998; Keck and Sikkink, 1998: ch. 2; see also Schmitz and Sikkink, 2002). Examples from international security include the Geneva conventions, the nuclear test ban debate, and – most recently – the treaty banning landmines (Finnemore, 1996b: ch. 3; Adler, 1992; Price, 1998).

Yet, agenda-setting does not equal norm creation. When it comes to international rule-creation and international treaty-making, national governments and IOs assume center-stage again. During this stage of the process, INGOs and transnational advocacy networks need to work through governments or international organizations. Moreover, while the agenda-setting phase might be dominated by well-organized transnational networks and INGOs, they are likely to counter considerable opposition when it comes to transforming principled beliefs or knowledge into concrete norms and rules prescribing appropriate behavior enshrined in treaties and other instruments of international governance and accepted by the international community. As a result, the requirements to build 'winning coalitions' with and among state actors usually become extensive and, thus, TNA impact appears to be less pronounced. There are few comparative case studies varying the conditions under which TNAs have an impact on treaty-making or regime creation. The available evidence points to three potential pathways by which TNAs influence multilateral negotiations:

- through lobbying activities in the domestic society of powerful states such as the U.S., thus exploiting ‘two level game’ mechanisms and changing state preferences;
- through coalitions with IOs thus pressuring states ‘from above’ and ‘from below;’ this particular pathway seems to be pronounced in the EU;
- through coalition-building with smaller states providing the latter with knowledge and ‘informational power’.

Once international rules and norms are created and international regimes have emerged, these normative commitments need to be implemented in the domestic practices of states and societies. This is by no means an automatic process as numerous studies about rule compliance (or lack of), and rule effectiveness reveal (see e.g. Keohane et al., 1993; Victor et al., 1998). While we still lack systematic comparative studies across issue-areas, the available evidence suggests that transnational advocacy networks and epistemic communities once again assume center-stage in the process by which states and their societies internalize international rules in their domestic practices. There are two reasons for this. First, the legalization process of international norms drastically increases the legitimacy of those actors who demand compliance with them. International institutions and the rules emanating from them empower both domestic and transnational actors in a differential way, thereby enhancing their moral and knowledge power.

Second, IOs and state agencies must often rely on the monitoring and information capacities of transnational networks and INGOs, because the former are bound by rules of sovereignty and of ‘non-interference in internal affairs’, while the latter can move more freely. This reliance on TNA expertise and information gathering capacities is particularly pronounced in issue-areas such as human rights and the environment (probably less so in international security and the international economy) and probably most relevant concerning international regimes that lack adequate, detailed, and intrusive verification procedures (see e.g. Haas, 1992c; Peterson, 1997; Korey, 1998; Smith, 1997).

## Domestic Conditions for TNA Impact

So far, I have concentrated on discussing effects of transnational activities mainly on the international level. Many transnational advocacy networks focus on influencing national policies and national governments in conjunction with international institutions and organizations. One proposition claims that differences in domestic structures explain the variation in TNA policy influence: ‘Domestic structures mediate, filter, and refract the efforts by transnational actors and alliances to influence policies in the various issue-areas. In order to affect policies, transnational actors have to overcome two hurdles. First, they have to gain access to the political system of their ‘target state’. Second, they must generate and/or contribute to ‘winning’ policy coalitions in order to change decisions in the de-



sired direction. ... Domestic structures are likely to determine both the availability of access points into the political systems and the size of and requirements for 'winning coalitions' (Risse-Kappen, 1995a: 25). This argument resembles to some extent the suggestions in the social movement literature that 'political opportunity structures' constitute an important factor in explaining the success of new social movements (Kitschelt, 1986; Tarrow, 1996). The domestic structure hypothesis has been evaluated empirically with regard to a variety of countries with diverging institutional setups (case studies in Risse-Kappen, 1995b).

This proposition posits a somewhat inverse relationship between TNA access and TNA impact on the domestic policy-making processes. The more open and the less centralized a political system, on the one hand, and the more pluralist the society, on the other, the easier it should be for transnational actors to gain access to decision-makers. The U.S. probably represents the best approximation of such a domestic structure. Yet, easy access does not equal policy impact. In fact, the coalition-building requirements in open political systems and societies such as the U.S. are quite formidable. On the other end of the spectrum are extremely centralized political systems such as the former Soviet Union which also dominate state-society relations. Evangelista's book on the impact of transnational networks on Soviet and Russian security and arms control policies (Evangelista, 1999) confirms the argument that TNA access to the Soviet policy-making structure was extremely difficult to achieve for transnational networks of advocacy and expert groups. Once Soviet leaders were prepared to listen, however, the transnational coalitions exercised an almost immediate policy impact. This explains the variation between the Khrushchev and Gorbachev eras, on the one hand, and the situation under Brezhnev and Andropov, on the other, when access to the top leadership was extremely limited. By contrasting Gorbachev's Soviet Union with Yeltsin's Russia, Evangelista also shows that the opening of the Soviet/Russian system multiplied the access points for transnational actors, but severely circumscribed their policy impact (Evangelista, 1995). This work constitutes one of the few examples whereby case selection on the independent variable (domestic structure) and keeping other factors constant allows for valid causal inferences on TNA impact.

But, as Keck and Sikkink point out, emphasizing domestic institutional arrangements does not tell the whole story of TNA impact: 'They cannot tell us why some transnational networks operating in the same context succeed and others do not' (Keck and Sikkink, 1998: 202). Human rights groups were more successful in changing U.S. policies under Presidents Carter and even Reagan than environmental groups. Their objection points to a weakness of the domestic structure argument. It has so far mainly emphasized formal aspects of political and social institutions rather than the substantive content of ideas and norms embedded in them. Constructivist insights might help to solve the puzzle why some TNAs successfully influence changes in state policies, while other fail, despite similar institutional conditions. A 'resonance' hypothesis has been developed by students of international norms trying to explain the differential diffusion in domestic practices (e.g. Ulbert, 1997; Checkel, 1997; Cortell and Davis, 2000): The more new ideas

promoted by transnational coalitions resonate or are compatible with pre-existing collective identities and beliefs of actors, the more policy influence they might have.

This proposition can be applied to efforts by transnational coalitions promoting international norms to affect domestic change. A comparison of human rights changes in the Philippines and Indonesia shows, for example, that the arguments by transnational networks resonated well with the Westernized political discourse in the Philippines under Marcos, while similar networks failed for quite a long time to pry open political space for human rights in Indonesia, since their arguments were not compatible with the prevailing nationalist discourse (Jetschke, 2000). In both cases, the domestic structure was strikingly similar during the 1970s (authoritarian rule). The 'resonance' argument would also explain the variation in transnational influence on Soviet security policy under Brezhnev as compared with Gorbachev (Evangelista, 1999). Litfin's critique of the 'epistemic community' literature and its application to the case of ozone depletion points in a similar direction (Litfin, 1994). She argues that Ernst and Peter Haas's conceptualization of consensual knowledge emphasizes too much a-political and 'objective' scientific knowledge. Rather, the claims by scientific communities must be framed in such a way that they are compatible with the prevailing political discourse. Otherwise, they fall by the wayside.

But the 'resonance hypothesis' is not unproblematic (see the discussion in Cortell and Davis, 2000). First, assessing the compatibility between transnationally diffused ideas and given domestic identities and collective beliefs must strictly concentrate on the discourses rather than on the behavioral practices of actors so as to avoid circular reasoning. Second, if there is a complete match between the new transnational norms and the ideas embedded in a given domestic culture, we do not need conscious efforts by transnational actors to make the norms stick. In other words, a certain degree of cultural misfit or incompatibility is necessary to ascribe causal weight to the activities of transnational actors. Most TNAs, INGOs and epistemic communities alike, are in the business of strategic construction (Finnemore and Sikkink, 1998: 269-275). In other words, they deliberately make new ideas and principled beliefs 'resonate' with pre-existing and embedded norms and collective understandings. It is very hard to predict beforehand which of these new ideas carry the day. The argument about ideational (in)compatibility is still underspecified in the literature.

## Toward Complex Models of TNA Impact

Most recently, scholars have advanced complex models of TNA impact integrating international and domestic levels. This work is particularly relevant for the study of TNA impact on norm implementation and compliance. Scholars have started specifying the conditions and causal mechanisms by which transnational advocacy networks manage to link the 'global' and the 'local' levels (on norms socialization in general see Checkel, 1999a). Keck and Sikkink have developed

the so-called ‘boomerang effect’ model to show how domestic and transnational social movements and networks unite to bring pressure ‘from above’ and ‘from below’ on authoritarian governments to accomplish human rights change (Keck and Sikkink, 1998: 12-13; see also Brysk, 1993; Klotz, 1995). A ‘boomerang’ pattern of influence exists when domestic groups in a repressive state bypass their government and directly search out international allies to bring pressure on their states from outside. National opposition groups and social movements link up with TNAs who then convince international human rights IOs and Western states to pressure norm-violating states. Transnational networks provide access, leverage, information, and often money to struggling domestic groups. International contacts can amplify the demands of domestic groups, pry open space for new issues, and then echo these demands back into the domestic arena.

Risse, Ropp, and Sikkink have developed a five-phase dynamic model of human rights change consisting of several ‘boomerang throws’ (Risse et al., 1999) and specifying the conditions under which links between domestic opposition groups and transnationally operating networks produce change toward domestic norm implementation and compliance. The ‘spiral model’ of human rights change claims that the mobilization activities of transnational advocacy networks are particularly significant in early stages of the process when domestic groups in the repressive state are too weak or too oppressed to constitute a serious challenge to the regime. At this stage, the information and monitoring capacities of transnational networks as agents of norms change are particularly relevant to mobilize the international community. The more the government is under pressure ‘from above’ and ‘from below’ and forced to make tactical concessions to its critics, the more the center of activities shifts from the transnational to the domestic level. During these later phases of the process, a major effect of transnational network activities is to empower and to strengthen domestic civil society. The spiral model has been successfully evaluated for the human rights area, but there is not yet systematic research for other issue-areas of international relations.

## TNA Strategies and Communicative Processes

Structural conditions need to be complemented by agency-centered approaches to account for TNA impact. Work focussing on INGOs and transnational advocacy networks which is largely inspired by moderate social constructivism and sociological institutionalism points to three relevant factors in this context:

1. TNA characteristics, particularly network density, material resources, and organizational capacities, but also ideational resources such as moral authority and legitimate knowledge;
2. Target characteristics, such as vulnerability to transnational pressures and uncertainty about cause-effect relationships;
3. Communication processes such as shaming, learning, and arguing.

As to the first factor, Keck and Sikkink point out that transnational advocacy networks 'operate best when they are dense, with many actors, strong connections among groups in the network, and reliable information flows' (Keck and Sikkink, 1998: 28, see also 206-207). One should add that material resources and organizational capacities of networks and INGOs also contribute to their effectiveness. But the example of Transparency International (TI), a tiny INGO with initially only few professional staff members, which almost single-handedly put corruption on the international agenda, indicates that ideational resources and knowledge might overcome a lack of material power and organizational capacities, at least initially (Galtung, 2000). Within a few years, TI acquired both moral and knowledge power in the area of corruption. The effectiveness of TI and other INGOs depends on ideational resources, particularly moral authority in terms of legitimate claims of representing some international 'common good' as well as informational capacities and knowledge. This ability to convert moral authority and excellent knowledge of the issue-area into ideational power explains to a large degree why transnational advocacy networks sometimes win against materially more powerful actors such as MNCs and national governments.

TNA impact not only depends on their own resources and capacities, but also on the vulnerability of their 'targets' – states, international organizations, or multinational corporations – to network pressures (Keck and Sikkink, 1998: 29, 208-209). Such sensitivity might concern vulnerability to material pressures such as economic sanctions or the cutoff of foreign aid in the cases of many Third World countries. But 'target vulnerability' might also imply reputational concerns and normative commitments. States or international organizations might be vulnerable to TNA pressures, because they want to be members of the international community 'in good standing'. In other words, the more these actors have committed themselves and their collective identities to the norms advocated by the networks, the more they should be vulnerable to TNA pressures in cases of norm violation.

Finally, 'target vulnerability' to network pressures might include uncertainty about the situation and about cause-effect relationships. This point has been particularly emphasized by the literature on epistemic communities (particularly Haas, 1992c). In many cases, policy-makers recognize a collective action problem in international life, but simply lack the knowledge to tackle it. Such uncertainty provides a window of opportunity for knowledge-based epistemic communities to exert influence.

Transnational networks as moral and knowledge entrepreneurs use various communication strategies to achieve their goals, the third group of factors to be mentioned here. INGOs rely on social mobilization, protest, and pressure. They use strategic constructions such as the re-framing of issues or shaming in order to mobilize people around new principled ideas and norms (Meyer and Tarrow, 1998). Shaming strategies remind actors such as national governments of their own standards of appropriateness and collective identities and demand that they live up to these norms (Liese, 1999; Keck and Sikkink, 1998: 23-24). Advocacy networks and epistemic communities also rely on the 'power of the better argu-

ment'. They need to justify their claims and to use various communication strategies in order to persuade their audience to change their interests and policies. Shaming and the re-framing of issues is usually not sufficient to convince others and overcome opposition. INGOs and other transnational actors must engage their audience in an argumentative process in order to achieve their goals. As 'teachers of norms' (Finnemore, 1993), they need to start a reasoned discourse justifying their claims in front of various public audiences.

Work on these micro-mechanisms and TNA strategies has just begun. It usually involves detailed process-tracing in (comparative) case studies research. Many case studies are methodologically problematic, however, since they focus on single cases and/or 'success stories' of transnational pressures without specifying the scope conditions of their arguments. As a result, we still lack testable propositions on the conditions under which such strategies succeed and when they fail (see, however, Checkel, 1999b). This area certainly deserves further scholarly exploration.

## **Conclusions: Toward Tripartite 'Global Governance'?**

This survey of more than thirty years of scholarship on transnational actors demonstrates that the significance of cross-border interactions involving non-state actors – Multinational Corporations, INGOs, epistemic communities, and advocacy networks – is no longer seriously contested in an age of globalization. But it would be premature to proclaim the end of the inter-state world as we knew it. The picture emerging from the literature reveals instead complex interactions between transnational actors, on the one hand, and corporate actors on all levels of supranational, international, national, regional, and local governance, on the other. Unfortunately, most of the literature is still primarily concerned with proving against a state-centered picture of world politics that transnational actors matter. As a result, the more interesting questions – when and under what conditions do they matter? – are rarely asked. Moreover, most research on TNA focusses on its direct policy impact rather than the structural implications of their activities on international society. This is particularly regrettable, since the goal of many transnational advocacy networks and INGOs is not so much geared to directly shape policies, but to engage in consciousness-raising and, thus, changing societies and building a transnational civil society (Wapner, 1996; Lipschutz and Mayer, 1996). While research on MNCs has always included the structural dimension in evaluating their impact, particularly in the developing world, this aspect is largely missing in studies concerning the non-profit sector.

There is no lack of propositions on TNA impact concentrating on institutional conditions (both domestic and international), coalition-building abilities, organizational capacities and resources, and actors' strategies. Research on transnational advocacy networks and epistemic communities appears to be a fruitful area for probing competing as well as complementary assumptions derived from rational choice liberalism and institutionalism, on the one hand, and sociological and con-

structivist approaches, on the other. But we are still in the early stages of a research program which concentrates more on hypothesis-generating than –testing through systematic and comparative case studies. Future research on transnational actors should evaluate competing explanations and specify the conditions of TNA impact on the various levels of governance. We also need more studies which turn the ‘dependent variable’ around and investigate the effects of increasing TNA influence in world politics on these non-state actors themselves.

Most important, future research on transnational actors needs to take into account that these actors – whether MNCs or principled INGOs – have lost their ‘innocence’ and have become part and parcel of international governance structures. Most previous scholarship has concentrated on the question how transnational actors affect national governments and international organizations through the various channels of exerting influence. Yet, international governance seems to be increasingly characterized by cooperative partnerships involving governmental as well as transnational actors, both MNCs and INGOs (see Reinicke, 1998; Reinicke and Deng, 2000; Kaul et al., 1999; O’Brien et al., 2000; Cutler et al., 1999). Examples include regulations in the financial services sector (Reinicke, 1998: ch. 4), private regimes in the insurance sector (Haufler, 1993), and the Transatlantic Business Dialogue (TABD) initiated by the European Commission and the U.S. government (Cowles, 2000). The UN system is replete with cooperative arrangements including international organizations, national agencies, and the NGO community, (e.g. Weiss and Gordenker, 1996; Willetts, 1996).

Empirical research on global (or regional) governance by tripartite networks including state actors, firms, and advocacy groups has just begun. The evidence is still sketchy and has not yet yielded testable propositions regarding the conditions under which such network structures emerge and how effective they are in international problem-solving. On the one hand, network governance might increase information capacities of both private and public actors as well as lead to new participation and learning possibilities. On the other hand, tripartite governance networks might lead to overly complex negotiation systems and to decision blockages.

Last not least, there is the problem of *democratic* and *legitimate* governance beyond the nation-state (see also Zürn, 2002). How can global governance by increasingly complex tripartite networks solve the dual problems of insuring ‘input legitimacy’ through participation of those concerned by the regulations and of ‘output legitimacy’ through effective and enhanced problem-solving (on these distinctions see Scharpf, 1999: 16-28; for general reviews see Wolf, 2000; Kohler-Koch, 1998a)? This debate has a long history starting with the first liberal thinkers on transnational relations for whom transborder interactions were an unproblematic ingredient of liberal democracy and a guarantee for peaceful international relations. But, as Kaiser pointed out already in 1971 (Kaiser, 1971), it constitutes a problem for democratic accountability if transnational governance structures include private actors – be it MNCs or INGOs – who are not elected by and, therefore, not accountable to anybody except, say, shareholders, and members of the transnational organizations. Claims by transnational advocacy networks to rep-

resent the international ‘common good’ and ‘global civil society’ have to be taken with a grain of salt when it comes to democratic accountability, representativity, and participation.

Two positions can essentially be distinguished in the emerging debate about the ‘democratic deficit’ of global governance. The first set of arguments is represented by Scharpf’s work on the EU (Scharpf, 1999) and is rather pessimistic about overcoming the democratic deficit of multilevel governance. Increasing democratic participation in international governance networks (‘input legitimacy’) faces the problem that there is no transnational ‘demos’, no transnational collective identity and no international public as we know them from the nation-states. Thus, ‘output legitimacy’ has to overcome the democracy problem in international governance. But there are limits to increasing the effectiveness and problem-solving capacity of international governance, since it requires positive collaboration among actors with diverging interests (‘positive integration’), while market liberalization (‘negative integration’) tends to be much easier.

The second position is more optimistic. Held’s concept of a ‘cosmopolitan democracy’ (Held, 1995) goes probably furthest in suggesting to strengthen parliamentary representation on the level of the United Nations and elsewhere and to systematically include transnational civil society and the INGO world into governance mechanisms. The concept of ‘deliberative democracy’ assumes center-stage among those who argue that the problems of democratic accountability in global governance and tripartite network structures can be overcome (see e.g. Wolf, 2000: 213-242; Schmalz-Bruns, 1999). It rests on the assumption that the legitimacy of the political process can be strengthened through public debate and deliberation and through the open exchange of arguments among citizens. The more tripartite networks of global governance are inclusive, their procedures and decisions transparent and subject to public deliberation, the more the democratic deficit of transnational governance can be tackled. Public deliberation might also increase the problem-solving capacity of multi-level governance, i.e. ‘output legitimacy’. At least, the concept of deliberative democracy offers a way out to tackle the legitimacy problems of global governance by networks, since it does not require a global ‘demos’ in terms of a strong supranational collective identity.

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# The UN Global Compact: The Challenge and the Promise<sup>1</sup>

*Oliver F. Williams*

The United Nations Global Compact is a new initiative intended to increase and to diffuse the benefits of global economic development through voluntary corporate policies and actions. Kofi Annan, secretary-general of the United Nations, addressing the Davos World Economic Forum in January 1999, challenged business leaders to join a “global compact of shared values and principles” and to provide globalization a human face. Annan argued that shared values provide a stable environment for a world market and that without these explicit values business could expect backlashes from protectionism, populism, fanaticism and terrorism.’ Following the 1999 Davos meeting, Annan and a group of business leaders formulated nine principles, which have come to be known as the UN Global Compact. After lengthy consultation, a tenth principle against corruption was added in June 2004.

The ten principles of the Global Compact focus on human rights, labor rights, concern for the environment and corruption and are taken directly from commitments made by governments at the UN: the Universal Declaration of Human Rights (1948); the Rio Declaration on Environment and Development (1992); the International Labor Organization’s Fundamental Principles and Rights at Work (1998); and the UN Convention Against Corruption (2003). The principles are:

## Human Rights

### *Principle 1*

Businesses should support and respect the protection of internationally proclaimed human rights within their sphere of influence; and

### *Principle 2*

make sure that they are not complicit in human rights abuses.

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## Labor

### *Principle 3*

Businesses should uphold the freedom of association and the effective recognition of the right to collective bargaining;

### *Principle 4*

the elimination of all forms of forced and compulsory labor;

### *Principle 5*

the effective abolition of child labor; and

### *Principle 6*

elimination of discrimination in respect of employment and occupation.

## Environment

### *Principle 7*

Businesses should support a precautionary approach to environmental challenges;

### *Principle 8*

*undertake initiatives to promote greater environmental responsibility, and*

### *Principle 9*

*encourage the development and diffusion of environmentally friendly technologies.*

## Corruption

### *Principle 10*

Business should work against corruption in all its forms, including extortion and bribery.

The Global Compact was designed as a voluntary initiative. A company subscribing to the Principles is invited to make a clear statement of support and must include some reference in its annual report or other public documents on the pro-

gress it is making on internalizing the Principles within its operations. The company must also submit a brief description of this report to the Global Compact website. Failure to submit such a description within two years of becoming a signatory to the Compact (and subsequently every two years) will result in being removed from the list of participants. The intention is that, through leading by the power of good example, member companies will set a high moral tone operating throughout the world. The overall thrust of the Global Compact is to accent the moral purpose of business and is summarized well by Kofi Annan in a quote that appears in the promotional brochure:

Let us choose to unite the power of markets with the authority of universal ideals. Let us choose to reconcile the creative forces of private entrepreneurship with the needs of the disadvantaged and the requirements of future generations. (Anan 1999, see also Tester/Kell 2000, p. 51)

One dimension of the Global Compact is to develop local networks, that is, groups of companies, NGOs and other key actors, in a region, a country or industrial sector. Through such networks – and there are over forty of them in operation in late 2004 – multinational companies and organizations involved in the Global Compact at the international level have the opportunity to engage and to discuss issues at the regional level. Having agreed to be guided by the ten principles, the companies have an opportunity to explore what these principles might mean in a specific context. For example, the local network in South Africa is planning projects on black economic empowerment and HIV/AIDS, crucial issues for that region.

While there has been an enthusiastic reception to the Compact, with over 1,100 companies signing throughout the world and many of the most influential companies from Europe joining, U.S. businesses, for the most part, have not signed on. (cf. [www.unglobalcompact.org](http://www.unglobalcompact.org)) In fact, only six of the major U.S. companies joined as of June 2004. Still, there are already some important signs of progress on the global level with the Compact. Two significant case studies have been produced, one on Novartis which shows how the company integrated the principles into its strategic planning process and another on Samarco's oil recycling program to reduce environmental damage from the fishing industry. Several global meetings have been held, one on Conflict Risk Assessment and Risk Management, and another on HIV/AIDS in the workplace. An important policy paper on Transparency has resulted from meetings as well as initiatives to increase sustainable business development in Least Developed Countries. Over 100 examples of good corporate practice are discussed on the Compact website as well as all the projects indicated above.

## Accountability: The Crucial Issue

U.S. company reluctance to join the Compact centers on the accountability issue. In an environment of increasing skepticism, without a traditional accountability structure or monitoring as part of the Global Compact, its legitimacy will be in question. There are two categories of critics and both need to be addressed. Some scholars who have contributed important research on codes of conduct see the Compact as another code without accountability, a public relations document without substance. How does one know that a business that claims to be following the principles of the Global Compact is actually doing so? Code scholars argue that an independent group of monitors with quantifiable and objective measures that translate general principles into operating standards is the way to assure that companies are accountable. Without this objectivity, precision and transparency, these “code critics” will find little that is helpful in the Compact. Prakash Sethi, perhaps the code scholar most critical of the Compact, makes these points as well. As discussed below (cf. *Accountability and Code Scholars*), I argue that such critics assume that the Compact is something that it is not, a code, and that they miss the role envisioned for the Compact by Kofi Annan.

More fundamental criticism comes from NGOs and others critical of the globalization of the economy. They view the Compact as a cover story, giving legitimacy to an idea which has yet to prove itself. This group argues for a mandatory legal framework as the only way to guarantee that companies are accountable to the least advantaged in the global economy.

Given this environment, many businesses ask whether signing the Compact will be more trouble than its worth. Further, should a comprehensive accountability structure be developed, will the loss of discretionary power, time and resources – what economists call transaction costs – be prohibitive?

An additional difficulty with the accountability issue, underscored by both schools of critics, is the elusive nature of the Global Compact’s principles on human rights. Can we develop a consensus that captures the legitimate expectations of society in this area? While the companies are in broad agreement with the human rights principles of the Global Compact, there is some apprehension that joining the Compact could lead to societal expectations that companies routinely have the obligation of correcting rights abuses. Where and how do we draw the line on obligations of business in the area of human rights? While at least some leading multinational companies understand that they must become proactive and meet societal expectations in a global economy, there is also a growing awareness that these expectations in the area of human rights are often unclear. In the litigious environment of the U.S., companies have been reluctant to sign the Compact without a clear idea of their responsibility and accountability. What follows is a clarification of the accountability issue drawing on literature in the business ethics field which may encourage companies to rethink their reluctance to join the Compact.

Before proceeding, however, it is interesting to note some of the reasons the European companies have not shared, for the most part, in the U.S. reluctance to

join the Compact. To have a sense of the problem here, in 2004, one hundred and ninety-two of the “Fortune Global 500” (which is the top five hundred corporations in the world in terms of revenues) are U.S. companies and only six (3.1 percent) have joined the Global Compact. One hundred and sixty-three of these companies are based in Europe and of these, sixty-four (40 percent) have joined the Compact. According to Georg Kell, the Executive Director of the UN Global Compact, European companies have not been deterred from joining either because their government regulatory environment has already mandated the substance of the Global Compact, or because they operate in a less litigious and adversarial context. A 2004 assessment of the impact of the Global Compact by McKinsey and Company, in addition to the point on fear of litigation, also cited two other concerns of U.S. companies: the implications of labor rights of the Compact; and the value of associating with a UN endeavor. European signatories are not overly concerned that corporate critics will use the Compact as a weapon in a struggle. This observation is similar to that of a study of various country codes of conduct employed during the apartheid era in South Africa where it was found that there was much less pressure on companies from NGOs and others for accountability in Europe than in the U.S. This was the case even when European companies were doing much less in the way of monitoring and verifying their attempts to dismantle apartheid than their U.S. counterparts who were participating in the Sullivan Principles and its accountability structure. (Fortune 2003, Sethi/Williams 2001)

## **Accountability and the Globalization Critics**

An important group of critics do not believe that economic globalization, as it is presently conceived, will ever bring authentic development to the poor, even if the principles of the Compact were implemented. Accountability for this sort of critic would involve carefully assessing whether the poor and developing nations are indeed better off with economic globalization. They are angry that Kofi Annan with his Global Compact and its voluntary nature has assumed the answer. In the final analysis, this school of thought sees the only answer to the plight of the poor as a radical change, “a binding legal framework for the transnational behavior of business in the human rights, environmental and labor realms.”(Letter to Kofi Anan 2000)

A July 20, 2000, letter from prominent scholars and NGO leaders to UN Secretary General Kofi Annan summarizes this objection.

We recognize that corporate-driven globalization has significant support among governments and business. However, that support is far from universal. Your support for this ideology, as official UN policy, has the effect of delegitimizing the work and aspirations of those sectors that believe that an unregulated market is incompatible with equity and environmental sustainability ... Many do not agree with the assumption of the Global Compact that globalization in its current form can be made sustainable and equitable, even if accom-

panied by the implementation of standards for human rights, labor, and the environment ... We are well aware that many corporations would like nothing better than to wrap themselves in the flag of the United Nations in order to "bluewash" their public image, while at the same time avoiding significant changes to their behavior ... Without monitoring, the public will be no better able to assess the behavior, as opposed to the rhetoric, of corporations. (Ibid.)

It is well beyond the bounds of this study to make some final judgment on the merits of the contemporary practice of economic globalization, but I do submit that there is a convergence in the vision of the globalization critics and the Compact. Both are trying to retrieve the notion that there is a moral purpose of business and not only in wealth creation but also in its distribution.

Perhaps the moral philosopher who has developed the intellectual underpinnings for the most demanding vision of the moral purpose of business is Alasdair MacIntyre. (MacIntyre 1994) Will the higher standards of living, if they ever come to poor countries, in fact, lead to a better quality of life? MacIntyre, in the face of a globalized economy he characterizes as marked by individualism and acquisitiveness, opts for an economic community where the virtues of character essential for the good life can flourish. He uses the example of two fishing communities, one characterized by a single-minded quest for profits and the other by a wider range of objectives including sustainability, community preservation, and promoting excellence in the task of fishing.<sup>2</sup> It is helpful to focus on the convergence in the views of MacIntyre and Annan in that both are trying to retrieve the notion of the moral purpose of business.

One way to view the Compact is as an attempt to revive the moral underpinnings of the economy that were assumed by Adam Smith. While many would characterize the world view of MacIntyre's first fishing village as that of Adam Smith (1723-1790), I join those who have another interpretation.<sup>3</sup> In *The Wealth of Nations*, Smith sought to understand why some nations were wealthier than others. Part of his answer was that nations that encouraged free competitive markets were wealthier. In a curious kind of way, in the context of the economy, when *each person pursues his or her self-interest the common good is enhanced* and all are

<sup>2</sup> While I find MacIntyre insightful and provocative, in the final analysis, I side with Andrew Wicks „I find enough coherence, hope, and possibility in both capitalism and 'modernity' to cast my lot with those who see the Enlightenment (and what followed) as something other than a disaster.“ (Wicks 1997)

<sup>3</sup> The 1991 encyclical letter of Pope John Paul II, *Centesimus Annus*, makes this central point: „The economy in fact is only one aspect and one dimension of the whole of human activity. If economic life is absolutized, if the production and consumption of goods become the center of social life and society's only value, not subject to any other value, the reason is to be found not so much in the economic system itself as in the fact that the entire socio-cultural system, by ignoring the ethical and religious dimension, has been weakened, and ends by limiting itself to the production of goods and services alone.“ (John Paul II 1991, p. 77)

wealthier. Given competition, the baker bakes the very best bread possible and sells it at the lowest price feasible so that he will have the resources to buy what he wants. Although motivated by self-interest, the result is that the community has good bread at a reasonable cost. Thus Smith showed how economic self-interest was beneficial for the community.

In my view, however, the crucial point in Smith's analysis is his assumption in *An Inquiry* that is quite explicit in his *The Theory of Moral Sentiments*: The "self-interest" of business people would be shaped by moral forces in the community so that self-interest would not always degenerate into greed and selfishness. Wealth creation enabled and sustained a humane community when it was practiced by virtuous people.

The Compact is not going to shape global business to be like MacIntyre's ideal fishing community any time soon. My argument is that Smith assumed that an acquisitive economy existed in the context of a moral community that would ensure that single-minded focus on making money would not perdure. Yet it is precisely this challenge of fostering the growth of humane values in the *global* society, a challenge heretofore managed by nation states for their own domestic situation, that marks the unique mission of the Global Compact. (Cassel 2001) The argument made by Global Compact officials is that unless the moral purpose of business is retrieved, economic globalization is doomed to failure.

It is precisely because a backlash to globalization would represent a historically unmatched threat to economic prosperity and peace that the Global Compact urges international business leaders to take reasonable steps to secure the emerging values of global civil society in exchange for a commitment on the part of the United Nations to market openness. (Tester/Kell 2000, p. 51)<sup>4</sup>

Globalization critics see little value in the Compact unless "the emerging values of global civil society" are somehow mandated by a world-wide legal framework. The Compact, seeing little prospect for world-wide legal statutes, advances a vision of the moral purpose of business that relies on transparency and the interest companies have in maintaining their good reputation as the ultimate sanction.

There is a growing awareness by multinational companies that global business is only possible in a world where basic ethical principles are assumed. Some evidence for this moral sensitivity of multinational companies is seen in the formation of the Caux Principles, a set of moral ideals not too unlike the Compact subscribed to by a number of prominent global companies. Founded in 1986, the Caux Principles do not have the visibility, global reach and convening power with many stakeholders that accrue under the umbrella of the United Nations, but they do rep-

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<sup>4</sup> The case for globalization and capitalism is made in the UN's 2002 edition of the Human Development Report but not without many caveats. For example: "The proportion of the world's people living in extreme poverty fell from 29% in 1990 to 23% in 1999", and „During the 1990's the number of people living in extreme poverty in Sub-Saharan Africa rose from 242 million to 300 million.“ (See [www.undp.org/hdr2002/](http://www.undp.org/hdr2002/)).



resent a significant attempt by companies to accent the moral purpose of business.<sup>5</sup> Largely because of the UN sponsorship, I argue that the Compact has the potential to be a more effective vehicle than Caux has been.

The moral context assumed by Adam Smith in his *Wealth of Nations* and made more explicit in *The Theory of Moral Sentiments* is retrieved with the notion of a Global Compact. Without the values embedded in the Compact, for example, trust, fairness, integrity and respect for people, global capitalism would neither be effective nor considered legitimate for long. In my view, Smith offers two sorts of justification for doing the right thing. In the *Wealth of Nations*, a utilitarian moral logic is the primary justification, whereas in *Moral Sentiments*, one does the right thing because it is the right thing to do. Both of these types of justifications are assumed by the Compact. Principles concerning the environment and safety in the workplace, for example, are justified by the first sort, while the Principles concerning human rights are largely matters justified by the second type. The Compact brings to the fore that business has a moral purpose and this is highlighted by the quote from Kofi Annan cited above where he refers to business's role concerning "the needs of the disadvantaged and the requirements of future generations."

To be sure, the Global Compact of today is a far cry from a force that might shape significant changes in the moral values of the global community. Yet one has to start somewhere and the authors of the Compact envision it as an incremental process of learning and improvement, rooted in local networks sharing the same universal values, that is now only at the starting gate. Not too unlike the Reverend Leon Sullivan's famous Sullivan Principles, the initial programs are only the seeds of the many flowers to bloom in the future. (Sethi/Williams 2001) One key difference of the Global Compact from the Sullivan Principles is that the moral leadership for moving the process along will not come from one charismatic leader (Sullivan) but rather from a coalition of major firms, NGOs and other members of civil society under the leadership of the UN Secretary-General which sees the value of the moral purpose of business.

Of course, one premise of the Compact is that there will always be NGOs, activists, social investors and others who will be on the scene to pressure firms and the Global Compact to be better corporate citizens.<sup>6</sup> There is a growing realization

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<sup>5</sup> Participants in the Caux Principles have been from twenty-seven countries and include such U.S. companies as 3M International, Chevron, Time Inc., The Prudential Insurance Company of America, The Procter and Gamble Co., The Chase Manhattan Bank, Medtronic Inc., Monsanto Company, Honeywell Inc., Cargill Inc., and the Bank of America. See the website [www.cauxroundtable.org](http://www.cauxroundtable.org). Accountability as discussed here is even less a requirement in the Caux Principles and this endeavor has much less visibility. For the text of the Caux Principles see Williams 2000, pp. 384-88. For two articles on the Caux Principles, see Cavanagh 2000, pp. 169-82; and Goodpaster 2000, pp. 183-95.

<sup>6</sup> For an example of this countervailing power of NGOs, see the letter by Louise Frechette, Deputy Secretary-General of the United Nations, of 3 June 2003, responding to the officers of Oxfam, Amnesty International, Lawyers Committee for Human Rights, and Human Rights Watch, who are pressuring for more accountability in the Compact. (See [www.globalpolicy.org/ngos/business/2003/0626secret.htm](http://www.globalpolicy.org/ngos/business/2003/0626secret.htm).)

that non-governmental organizations (NGOs) or organizations of civil society play an important role in such a dialogue, for their focus is properly the common good – the culture of civility, health, environmental protection, and so on. This is certainly not to say that NGOs are always above reproach for they too need accountability structures. In economic terms, NGOs focus on overcoming the negative externalities of business. Already major NGOs, including Amnesty International, Oxfam, Human Rights Watch, World Conservation Union, World Wildlife Fund, and Transparency International have joined and are participating in the deliberations of the Compact. The International Confederation of Free Trade Unions, Business Associations, and Academic and Public Policy Institutions have joined as well.

Thus while I understand that globalization critics, such as those who signed the letter cited above, ultimately believe that some sort of international law is the only way to hold firms accountable for their moral purpose, I have argued that, in this far from perfect world, a very good vehicle to retrieve the moral purpose of business is the Global Compact. For their part, multinational companies should view Compact deliberations with NGOs and others as potentially a significant contribution to the shaping of societal expectations for business. For this reason alone they should join the Compact.

## **Accountability and Code Scholars**

The great majority of scholars and activists in business related fields who have studied codes of conduct argue for accountability structures primarily to engender trust in an increasingly skeptical public. In an exhaustive study of what could be learned from the Sullivan Principles in South Africa for global codes today, one key finding was that “an independent oversight monitoring function is an absolute necessity.” (Sethi/Williams 2000, p. 187) This lack of an independent monitoring provision is the most significant criticism of the Compact. Given the current structure of the Compact, it is quite possible for a company with a poor record in labor or the environment to highlight another area of corporate citizenship in its annual report where its record is superlative. The general public will only have the knowledge about a company that the company chooses to report. Granted the Global Compact’s network structure is designed to enhance corporate learning through “best practices” and other measures, critics continue to call for some performance standards and verification procedures. Prakash Sethi writes: “The Global Compact...provides a venue for opportunistic companies to make grandiose statements of corporate citizenship without worrying about being called to account for their actions.” (Sethi 2003a, 2003b) Compact officials respond that this criticism misses the point. “The Global Compact is not designed as a code of conduct. Rather it is a means to serve as a (frame) of reference to stimulate best practices and to bring about convergence around universally shared values.” (Tester/Kell, p. 53) At this stage, the goal is to gain consensus on the moral purpose of business and to include the substance of the principles as a part of business strategy and operations. Since

companies will include a discussion of their Compact-related activities in their annual reports, the power of public transparency and the watchdog role of the media and NGOs serve as an accountability structure. What Compact advocates have in mind is that when actual business practice falls short of ethical standards, public criticism is a good corrective. For example, Lynn Sharp Paine, in an insightful study of the merging of social and financial imperatives, discusses how Royal Dutch/Shell made a major change in policy and practice after strident criticism of its activities in Nigeria. (Paine 2003), pp. 20-23) Although Shell has had serious problems in 2004 with top management overstating oil reserves, the company is still considered by many to be a leader in promoting and protecting the rights of workers and communities. Yet even with this role of the press and activist groups, while the Compact is a noble endeavor, unless the participating companies are involved in some sort of independent monitoring and verification system, corporate critics (even those in the moderate camp) may never acknowledge its legitimacy.

Some critics point out that the Compact may be the victim of “adverse selection”, that is, the companies most eager to join are those tainted by bad press and in need of a good public image. Needless to say, should this be a valid criticism, the most highly regarded companies may shun the Compact. Called “bluewash” by some, the critique argues that the UN is being used by companies to overcome a poor track record on social issues, for example, bad press because of sweatshops or low wage rates. Critics often cite Nike, a signer of the Compact, as an example of adverse selection. In all fairness, it must be said that after severe criticism by NGOs, Nike is now thought by many to be a model corporate citizen as far as assuming responsibility for working conditions in suppliers’ plants. The typical position in the past was that, since multinational companies did not own suppliers’ factories, they were not responsible for them. Aret van Heerden, the executive director of the Fair Labor Association (FLA), an NGO that monitors working conditions in the apparel industry, was recently quoted on Nike in the *Los Angeles Times*: “A company like Nike has moved way beyond that and has agreed that even though it doesn’t own the factories, it will be responsible for conditions in any supplier’s plant.(cf. Letter to Kofi Anan ...2000, see also [www.corpwatch.org](http://www.corpwatch.org))

Scanning the list of current signatories, adverse selection does not appear to be a problem at this time. For example, Compact member companies not based in the U.S. include five of the top ten Fortune Most Admired Companies (outside the U.S.): BMW, Nokia, Nestle, BP, and Royal Dutch/Shell Group. (Stein 2003)

Compact officials note that their endeavor is incremental and will evolve as the need arises and as the companies perceive the need for change.<sup>7</sup> As noted above, the requirement for some accountability structures is a need that almost all observers have identified. Just as accountability structures in quality management (ISO quality standards) have become a business imperative today, largely through

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<sup>7</sup> This point has been made repeatedly by Georg Kell in conversations with the author. For example, in light of complaints one current issue Compact officials are discussing is what business behaviors necessitate asking a company to sever its relationship with the Compact.

pressures from competitors, consumers and the media, so too can they in the area of corporate responsibility. (Waddock 2002)

Perhaps the best hope for transparency and accountability standards is the reporting mechanisms that would enable verification and monitoring being developed by the Global Reporting Initiative (GRI). The GRI grew out of the work of the Coalition for Environmentally Responsible Economics (CERES). Originally the CERES Principles were concerned only with environmental reporting and, in its early days in the late 1980s, only small firms with intense interest in the environment were willing to join and publicly report in standard metrics. In recent years, most major firms have published reports which disclose and measure their environmental record using the standard metrics of CERES. This led to a call to develop comparable reporting mechanisms for the economic and social areas and thus the founding of the GRI by CERES. Sometimes called the triple bottom line (economic, environmental and social), or sustainability reporting, the attempt to disclose and measure the full impact of a business is the ongoing project of the GRI. At present, the Global Compact encourages signatory companies to participate in the GRI but does not require it.

The most recent GRI Sustainability Reporting Guidelines (2002) presents a framework indicating what should be in a good company report. While the Guidelines are a good start, they are still far from adequate. For example, they include fifty core indicators of quality yet sixteen of these indicators focus on whether the company has a policy or process that deals with an issue and not on how the company is performing on that issue. A policy on child labor or downsizing tells little about how the company performed in that area. (cf. Baker 2002) Tracking a company on certain issues from year to year requires some performance metrics that all can understand. While the indicators in the environmental area are clear and useful to stakeholders, the social reporting indicators are only in their infant stages and much more dialogue and consensus building is required. That being said, it should be noted that the GRI has always had a social performance indicator on bribery and corruption, which, until June 2004, was a glaring omission in the Compact.

While the Global Compact has no required standard reporting provision at this time, it does encourage signatory companies to use the GRI. In fact, it will likely be increasingly clear that for the Global Compact to be a significant force, either the Global Reporting Initiative or something similar to it will be a necessary complement. Nevertheless, the independent monitoring and verification feature will probably never be a task of the Compact itself. Further, Compact officials do not believe such a role to be part of the UN mandate. Imagine a group like the Rotary Club that forms a community, promulgates moral ideals and encourages people to formulate a lifeplan based on such a vision. Although this organization may expel members who flagrantly and publicly violate core moral ideals, it does not itself police, enforce, or measure how well individuals do. This self-understanding is an approximation to that of the Global Compact; as prescribed in the „Global Compact Integrity Measures“ (see website), the Compact can expel members for egregious violations but it does not have a regular monitoring and verification feature.

## **Accountability and Gaining Consensus: The Two-Tier Pricing System**

There are a number of issues where there is little consensus on how to justify the apportioning of responsibility, particularly in the area of the environment and human rights. One example concerning the pharmaceutical industry meeting human rights may illustrate the role of ethical research in helping to gain consensus and shaping societal expectations. This example and the pages that follow are presented more to stimulate further thought and research rather than to provide a final answer, for the whole pricing structure of the pharmaceutical industry needs further understanding and analysis. Until this happens, there is little prospect that the Global Reporting Initiative will develop a comprehensive, standard metric responding to the right of health care and treatment built on societal consensus. Yet policies are being made in apportioning responsibility for health care, and normative theory can help in understanding them and formulating better ones.

One policy the pharmaceutical industry has produced to allow the poor in developing countries the possibility of affording life-saving drugs is a two-tier pricing system, that charges considerably more in affluent countries and thus covers the cost of current research for future products. This policy has caused no small controversy, particularly in the United States. There is considerable ethics research, however, which can provide a normative framework for this policy. For example, one might argue the case from a common good, a justice, or a rights perspective. (cf. Velasquez 1992, Bowie 1998, De George 1993)

One normative theory, which holds promise for clarifying and providing an ethical justification for a two-tier pricing system, is integrative social contract theory (ISCT). In ISCT, the most basic principles summarizing a broad consensus about behavioral norms are called “substantive hypemorms”, principles “so fundamental to human existence” that they are found in “a convergence of religious, political and philosophic thought.” (Donaldson/Dunfee 1992, 1993)

The case of apartheid in South Africa may be helpful to illustrate briefly the justificatory and explanatory role of ISCT. In South Africa up to the late 1980s, the rules that governed the society as well as individual firms (rules called social contracts or microsocal contracts in ISCT) assumed the black people should not have full political and civil rights. While social contracts do not have to be the same in all nations, companies, or groups – for there is a wide range of “moral free space” – all micronorms must be consistent with hypernorms in order to carry objective moral weight. Thus the apartheid laws and company policies, which denied people political and civil rights on the basic of skin color and race, were “illegitimate” micronorms. Although the apartheid policies were based on mutual consent of the voters (who were only of the white race), and reflected in both their attitudes and actions, since these micronorms violated basic human rights (hypernorms), the country as well as the companies participating in apartheid policies were considered immoral.(Sethi/Williams 2000)

In brief, ethical obligations are recognized where there is consent in the local community as well as consent by “all rational contractors to a theoretical macro-social contract”. While the local community of white Africaners saw no problem with a norm specifying racial hierarchy (apartheid) in South Africa, the world community saw that norm as “illegitimate”, a violation of basic human rights and universal truths (hypernorms). Finally, following much protest from around the world, the relevant ethical obligation was made operational. After 1984 human rights were factored into business decisions of multinationals in South Africa. And in 1994 statutory apartheid was dismantled with the first election where all could vote.

ISCT can provide a justification for the two-tier pricing system and for other policies that provide lower prices or commercial concessions for poor countries and the Global Compact can facilitate the process of developing appropriate norms. One way to understand the ten principles of the Global Compact, then, is as an expression of either norms and hypernorms (fairness, respect for other people and integrity) or principles derived from hypernorms (workplace safety and discrimination). With its emphasis on local networks, the Compact encourages regions, nations and individual firms to develop the norms appropriate to implement the nine principles as long as these norms do not violate a hypernorm. Thus, for example, the pharmaceutical industry’s pricing policy for life-saving drugs may be guided by a norm in developed countries which sanctions prices that include a significant amount that will be allocated for research costs for future products. While this norm will result in higher costs for patients, the assumption is that there is little prospect that a patient’s right to health care will suffer since there are government social safety nets and other measures to assist the poor in affluent countries. (To be sure, this assumption itself needs further study and action). In developing countries with weak governments and meager background institutions to assist, this same norm for a pricing policy would be illegitimate since it would likely mean no medicines for those in need and thus a violation of rights. While it is always difficult for consumers in affluent countries to understand how the same drug manufactured by the same pharmaceutical company can be sold much cheaper in poor countries, ISCT provides a helpful normative framework. (see Crouch 2002, “Africa’s cheap ...” 2003)<sup>8</sup>

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<sup>8</sup> Pharmaceutical companies were reluctant to approve the two-tiered pricing system because of the fear of „round-tripping“, fraudulently selling a deeply discounted drug meant for the poor in a developing country in an affluent country at the higher price. This would seriously erode the profit margin required for research for future drugs. After considering the options, most companies have moved to two-tier pricing although it has not been without problems.

## **Accountability as a Moving Target: For What Societal Expectations Are Multinationals Accountable?**

A recent article on the HIV/AIDS pandemic in sub-Saharan Africa spoke of an activist who “unleashed a verbal broadside against the pharmaceutical companies, and their refusal to provide drugs at cost or, even better, no cost at all”. Another article spoke of pharmaceutical companies being “threatened by the National Association of People Living with AIDS if the firms continued to refuse to provide antiretroviral drugs free of charge” (Lewis 2001, “Threatened” 2001). Needless to say, the multinationals are aghast at such proposals (there are thirty million people in the area with the disease and, for the most part, those persons have never seen a doctor or been in a clinic). In the face of weak and inadequate governments, NGOs and other civil society actors are increasingly pressuring multinational corporations to accept new social responsibilities to balance their newly acquired rights and power in the global community. In my view, what is going on in the pharmaceutical industry is only a dramatic, early warning signal of a rethinking and widening of the role of all of business in society and hence it is a helpful case study to consider. The question that comes to the fore is for what societal expectations are multinationals accountable?

The companies are in a difficult position summed up by one pharmaceutical company officer: “We take accountability for our obligations seriously.” What the companies want to know is how to gain a consensus in society of what these obligations are. “The Universal Declaration of Human Rights (UDHR) and article 12 of the International Covenant on Economic, Social and Cultural Rights (ICESCR) are interpreted by some as embodying a right to essential medicines. Are pharmaceuticals private goods to be obtained through the market, or public goods to which all citizens have a right?”<sup>9</sup> Do multinational pharmaceuticals have a moral obligation to satisfy this right for the poor in developing countries?

Drawing on research on human rights, including issues raised in Henry Shue’s work, the Economic and Social Council of the United Nations, in 2000, stated that “Health is a fundamental human right indispensable for the exercise of other human rights”. It based this right on the human dignity of the person. (General Comment No. 14 on Substantive Issues Arising from the Implementation of the International Covenant of Economic, Social and Cultural Rights (ICESCR)“, United Nations Economic and Social Council, 2000. See [www.unhchr.ch](http://www.unhchr.ch)., Shue 1981) The interdependent nature of basic rights is reflected in the fact that a cer-

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<sup>9</sup> In order to discuss the Compact with major U.S. multinationals and to increase U.S. membership, the United Nations Global Compact Office and the Center for Ethics and Religious Values in Business at the University of Notre Dame sponsored a conference at Notre Dame in April 2002. Several corporations that are already members of the Compact (Nike, Novartis, and Shell) and some considering joining (Freeport-McMoRan Copper and Gold, Hewlett-Packard, Merck, and Motorola) gave presentations. The statement summarizes the sense of some of the pharmaceutical company presentations at the Notre Dame-UN conference in April 2002.

tain minimum standard of health is required to enjoy other fundamental rights, such as freedom and equality. The right to health implies the right to access to what it takes to provide that health — care and treatment (since the right to *health* may imply that others have the obligation to see that one never gets ill, I use the right to *health care* and *treatment* to avoid any misunderstanding). This would likely include doctors, nurses, essential medicines, and facilities. Indirectly, good health also requires provision for basic conditions such as nutritional food, safe water, sanitation, preventative medicine and relevant education. While the document calls for “the highest attainable standard of health”, it recognizes that economic and social factors play a role in determining what is attainable in a particular society. Thus in the poorest countries extremely expensive medicines cannot be guaranteed by the government or multinationals although wealthy nations would have a duty to try to assist.

While there is a relatively good consensus about the right to health care and treatment, there is disagreement about how to fairly apportion these responsibilities, especially in developing countries. Where does one draw the line in assigning obligations to a multinational business? Is it the moral responsibility of the multinational to distribute society’s scarce resources, to feed the poor, to provide health care? If that be the current societal expectation, should it be honored? This is a concern to some of those U.S. companies which have not joined the Global Compact. In the U.S. context where litigiousness is a fact of life, the fear of some U.S. companies is that the Compact may well be considered a contract by some stakeholders and that they may be subject to law suits.

A recent California court decision allowed an activist to sue if a company falsely colors its social image. The California Supreme Court on May 2, 2002, in *Marc Kasky vs Nike*, held that claims about safe working conditions are “commercial speech” and must be defended in court if challenged. Nike asked the U.S. Supreme Court to review the ruling and, after hearing oral arguments, the high court refused and sent the matter back to California for a final determination. In September 2003, Kasky and Nike agreed to a settlement, Kasky withdrawing his lawsuit and Nike agreeing to pay \$1.5 million to the Fair Labor Association (FLA), a monitoring group that strives to improve factory conditions. While the settlement essentially means that the merits of the Kasky (and Nike) positions remain untested, the very fact that a similar suit may be brought forward in other cases may offer significant leverage to activists monitoring business theoretic and corporate actions. (For the court decision, see [www.courtinfo.ca.gov/opinions](http://www.courtinfo.ca.gov/opinions)). While for some companies this case may reinforce their reluctance to join the Global Compact, this is overly cautious. This is certainly the judgment of the American Bar Association which, in 2004, drafted a standard entry letter which companies joining the Compact can use to preclude subsequent litigious claims. I side with major companies like Hewlett Packard, Pfizer, Cisco Systems, Starbucks Coffee, and DuPont who have reviewed the issues and decided that signing the Compact is not only in the best interest of the company but also the global community. Their course of action is the one that others should follow.



Scholars have argued that, although multinational companies do have a responsibility to honor human rights, they do not have an obligation to aid those deprived of life-saving resources, i.e., to provide medicines for the sick or food for the hungry. They may want to do those things when feasible but, under normal circumstances, these activities should not be considered as a part of business. Donaldson, following Henry Shue, makes helpful distinctions in the classes of the rights honoring duties. Three classes of duties are:

1. Refraining from depriving people of the object of a right.
2. Protecting (in some instances) the right from being deprived.
3. Restoring to people whose rights have been violated the object of the right. (Donaldson 1989, 1994)

Thus while a company must never take medicines from the diseased (class number 1); and it may often protect people from being diseased (class number 2); it does not have an obligation to provide medicines to the diseased (class number 3).

There is clearly a compelling logic to this position which may be summarized as follows. While multinational corporations should and do assume extraordinary social responsibilities and corporate citizenship duties in developing countries, there is a limit to business's role in society. Individuals (especially wealthy individuals) and nations can and should help provide medicines to all who need them, limited only by their capability. For-profit corporations should see their primary duty as providing good products at a fair price in the context of listening to their many stakeholders. If a pharmaceutical company, for example, depleted its revenue in the process of providing antiretroviral medicines and developing medical clinics for the poor of sub-Saharan Africa, it could not generate the money necessary for research for a cure for HIV/AIDS. (Pear 2001, p.1) Consumers would ultimately pay either by much higher prices or by no new, innovative products or cures (assuming the company survived). To assign the pharmaceutical business the *obligation* of aiding those deprived of antiretroviral medicines and care would undermine the genius of the free enterprise system.

In spite of the compelling logic of the above position, there is growing realization that with the huge aggregates of money and power under the control of multinational businesses, these organizations *do have moral obligations* as corporate citizens in the global community to assume some responsibility for providing medicines. The very title of the UN program, the Global Compact, points us to the basis of these obligations. All organizations producing goods and services have an implied contract with society. Similar to the argument for the moral and political foundations of the state advanced by Locke, Rousseau, and Hobbes, this approach argues that companies have a duty to be social responsible and this involves honoring human rights. That being said, the theory does not spell out just what responsibilities are appropriate for multinationals.

Michael A. Santoro, in discussing the duties of multinational firms in the face of human rights violations in China, offers a conceptual framework to assist in the

analysis and clarification of the situation. Called a “fair share” theory of human rights, Santoro points us to four factors: “the diversity of actors, the diversity of duties; an allocation of duties among various actors; and principles for a fair allocation.” (Santoro 1998) In any human rights problem, there are a number of possible actors, for example, international institutions, nation-states, multinational firms, NGOs and individuals, and each should be allocated a fair share of the duties. The principles proposed for a fair allocation of duties are: relationship to those whose rights are violated; the likely effectiveness of the agent in remedying the problem; and the capacity of the agent. Santoro’s point is that while companies must do something, they should not be asked to do “more” than they are capable of doing effectively. (Ibid., p. 48)

Many of our best companies have formulated a philosophy of corporate citizenship and have taken steps to institutionalize this philosophy in their corporate culture. U.S. companies involved with producing antiretroviral medications include Abbott, Bristol-Myers Squibb, and Merck. Each of these have initiated programs to deliver better health care and treatment, in some limited way, to those suffering HIV/AIDS. I believe these companies correctly perceive that they must do these activities as a matter of moral obligation as corporate citizens and not merely as a matter of philanthropy or as a public relations gesture. From my discussions with some of the companies, I believe they are employing allocation principles similar to Santoro’s, largely effectiveness and capacity, and thus are trying to meet the morally required minimum.

The kind of moral leadership exemplified in Merck’s Botswana Comprehensive HIV/AIDS Partnership may set a standard of how corporate citizenship can contribute to solving the pandemic. Botswana, with a population of 1.6 million people, has an HIV prevalence rate of 38.5 percent among those in the 15-49 age group. While having the political will to solve the health crisis, the government felt overwhelmed, not only because of the cost involved but also because they lacked the expertise. A partnership was formed with the government of Botswana, Merck and the Bill and Milinda Gates Foundation with the overall objective of improving the care and treatment of HIV/AIDS patients. Merck is donating medicines and financial assistance. Gates and Merck are each contributing fifty million dollars over five years and the government will assist in training health care professionals to ensure that antiretrovirals are used safely and effectively. The program is led by the former CEO of the South African unit of Merck. A Harvard Business School case has been written about the partnership and this model may hold much promise for replication in other developing nations suffering from a health crisis. (Austin et al 2001, see also [www.achap.org/](http://www.achap.org/))

Some other examples of what the companies are doing may also offer models for the future. The UN/Industry Accelerating Access Initiative (AAI) is a cooperative endeavor among UNAIDS, WHO, the World Bank, UNICEF, the UN Population Fund and six pharmaceutical companies (Abbott, Boehringer Ingelheim, Bristol-Myers Squibb, GlaxoSmithKline, F. Hoffman-LaRoche, and Merck) to provide, among other things, antiretroviral medicines at more affordable prices. In addition

to the AAI program, three other initiatives designed to improve access to HIV/AIDS medicines in the developing world are worthy of note: 1. *Secure the Future* is a five-year program where Bristol-Myers Squibb is contributing \$115 million and working with South Africa, Botswana, Namibia, Lesotho and Swaziland to find ways managing HIV/AIDS among women and children; 2. *Diflucan Partnership Program* is a program where Pfizer pays for medical training, patient education and Diflucan for AIDS patients in 70 least developed countries; and 3. *Viramune Donation Program* involves Boehringer Ingelheim's donation to pregnant women with AIDS in developing countries of medicines to prevent mother-to-child transmission.

It is instructive to note that while these companies are striving to meet moral responsibility, only one (Pfizer) has joined the Compact. One explanation for this reluctance to join, as discussed above, is that given that there is not a clear consensus on what is the moral responsibility of a multinational pharmaceutical company in meeting the needs of the poor, joining the Compact would expose them to added criticism and perhaps even legal action from critics.

Research-based pharmaceutical companies' contributions and donations for HIV/AIDS and other diseases between 1998-2000 amounted to US \$1.9 billion. To be sure, critics of the pharmaceutical industry claim that companies relax intellectual property rights and "lower their prices only when threatened" (McNeil 2001, p. 6). Although the critics may have a point and further study in this area is surely warranted, the companies are, in fact, providing an answer to those societal expectations for which they believe they are capable of being held accountable.

Some companies active in sub-Saharan Africa, e.g., Coca-Cola, DeBeers, BP, and Anglo-American, have decided that they can provide antiretroviral medicines and care for their employees and their spouses with HIV/AIDS. (The Global Business Coalition on HTV/AIDS headed by Richard Holbrooke, former U.S. Ambassador to the UN, has enlisted many multinationals in the fight against AIDS. Some companies have gone well beyond the normal role of business in society. See the web site [www.businessfightsaids.org/](http://www.businessfightsaids.org/)) Pharmaceutical companies with antiretroviral medicines have initiated a whole series of programs to lower prices and deliver care for countries listed low or medium on the Human Development Index (HDI). (For example, GlaxoSmithKline cut the price of its AIDS and malaria treatments by 38 percent in the sixty-three poorest countries. „Glaxo Cuts Price ...” 2003) Again, the point of listing these company initiatives is not to foreclose criticism of the companies but rather to argue that companies with the resources can and must do something as a matter of moral obligation as good corporate citizens.

How much must they do? It is in the context of this question that companies are well advised to look to the Global Compact to help in the "recalibration going on of the public-private sector balance" (Ruggie, p. 29). As said earlier, because the Compact has the visibility, global reach and the convening power that accrue to it as an instrument of the UN, it is likely to be more effective than other global credos with similar missions. Since the Compact is based on principles that were ac-

cepted by most governments of the world, it offers a vision of the global community accepted by all nations. To be sure, the UN principles are ideals which are far from realized and may not even be honored in some places, but one has to start somewhere. The unique feature is that the private sector is now being asked to be the agency which closes the gap between vision and reality, to be the standard bearer for promoting community norms and to help shape the legitimate expectations of society. Even more than that, through the dynamic process of the Compact, new norms may be generated. Many U.S. companies have not joined the Compact because, given the litigious climate, they are apprehensive about growing societal expectations that companies routinely have the obligation of meeting basic human rights when nation-states cannot. Yet, as emphasized above, given the UN's role in the global community, it is in the forum of the Compact that this discussion can most effectively take place.

## Conclusion

While it is true that, at present, the Global Compact lacks adequate accountability structures, since it is a dynamic process open to incremental change, given intelligent and persistent criticism, there is bound to be progress in this area. The best hope for accountability without undue transaction costs is the effort currently underway by the Global Reporting Initiative. The Compact has supported this endeavor. If the Global Compact does not succeed in developing adequate reporting procedures and meeting the legitimate concern of giving globalization a human face, some other world-wide policy forum will have to rise to the challenge. U.S. companies would be well advised to join the Compact and help shape its future.

As to the potential obligations that trouble U.S. business, current issues in the pharmaceutical industry are a helpful case study. Most scholars argue that the right to medicines and care is a moral right but there is little consensus on how best to apportion the duties to meet this right. There is a growing consensus that with the large aggregates of money and power, multinationals have moral obligations as corporate citizens to assist the poor in the global community, but the extent of these obligations is unclear. The Global Compact offers a forum under the umbrella of the United Nations with its visibility, global reach and convening power where some of the best members of civil society – non-government organizations, academic and public policy institutions, individual companies, business associations and labor representatives – can come together to discuss the changing role of business and its moral purpose. U.S. companies as well as those throughout the world are well advised to join the Global Compact and contribute to the shaping of these new expectations of business in society.

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# Global Public Rules and Citizenship Rights: A New Responsibility of Private Business Firms?<sup>1</sup>

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Economic activities require the existence of rules and their enforcement as pre-conditions that the market cannot generate itself. Property rights, contractual rights and obligations are minimal conditions that in modern societies are provided and enforced by the state. Without such rules, the market cannot flourish. The *state* thus determines regulations and delineates the sphere of private freedom, within which individual citizens and private institutions are entitled to conclude contracts amongst each other but are as well forced to abide by the contracted rules. In line of the development of modern nation states, the state has not only been the guarantor of *civil rights*, e.g. the right to own property, to enter into private contracts, and to engage in market activity. In its role as a democratic constitutional state it has also been the guarantor of *political participation rights*, the right of the citizen to take part in the processes to determine public rules and issues of public concern. Finally, in its role as a welfare state it has provided *social rights* for citizens, such as the right to education, to healthcare and welfare (Marshall, 1965). The combination of state-guaranteed civil, political, and social rights provided modern society with welfare, legitimacy and solidarity, thereby contributing to peacefully stabilize the community of anonymous individuals (Habermas, 2001). Following Matten and Crane (2005) we refer to this triad of rights as *citizenship rights*.

In a globalized world, however, *global governance*, referring to rule making and rule implementation on a global scale, is no longer a task managed by the state alone (Braithwaite and Drahos, 2000; Zürn, 2002). Today, transnational corporations (TNCs) as well as civil society groups increasingly participate in the formulation and implementation of rules in policy areas that were once the sole responsibility of the state or international governmental organizations. These activities of

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TNCs and civil society groups include, e.g., involvement in peace-keeping (Dunfee and Fort, 2003; Fort and Schipani, 2002), protecting human rights (Kinley and Tadaki, 2004), or implementing social and environmental standards (Scherer and Smid, 2000; Young, 2004). This development indicates a shift in global business regulation from state-centric towards new multilateral non-territorial modes of regulation with private and non-governmental actors involved (Braithwaite and Drahos, 2000). Many TNCs have set up their own “codes of conduct” outlining the humanitarian and environmental standards of their business practices that are implemented in their area of influence including contractors and subcontractors (Sethi, 2002, 2003; Williams, 2000). TNCs also engage in rule making activities on the industry level. Within public-private-partnerships they cooperate with NGOs and state actors to identify and solve problems in various areas of public concern (Reinicke and Deng, 2000; Risse, 2002). Parker and Braithwaite (2003) therefore suggest that the concept of regulation needs to be enlarged to also include a complete self-regulation without the help of state agencies.

Given these developments, how shall TNCs react? – Management and economic theories deal with these concerns in an ambiguous manner. It is at issue whether business firms should support initiatives like the UN Global Compact or engage in other forms of political self-regulation (see Cavanagh, 2004). Some management scholars hold that business firms should give money to philanthropic projects (Porter and Kramer, 2002), others suggest that TNCs should reorganize their entire business processes according to human rights, social and environmental standards although this might cause higher costs or a loss of profits (Leisinger, 2003). However, many economists are very critical towards a social responsible engagement of business firms (e.g., Friedman, 1970; Hendersen, 2001) and many management students recommend CSR activities only if they contribute to the firm’s profit. The economic position is based on a liberal theory of society and its strict division of labor between the private and public domains: business firms should focus on profit seeking while it is considered the task of the state to take care of issues of public concern (e.g., Friedman, 1962).

We will argue that under the conditions of globalization nation state agencies come under pressure and are less able to overview the rights of their citizens and take care for the sufficient supply of public goods (Beck, 2000). As is argued by Matten and Crane (2005) and demonstrated by Young (2004) and Fung (2003) in their analysis of global labor justice TNCs are currently turning into political actors. They are held responsible for providing social rights (e.g., corporations manage health care issues); enabling civil rights (e.g., corporations protect the freedom of speech of workers and their associations in countries with repressive regimes), and channelling political rights (e.g., corporations engage in self-regulation). Through their political engagement some corporations set standards that permeate industries and change the rules for all players, thus going beyond legal standards or filling the gap of non existing regulation (Parker, 2002; Zadek, 2004).

These developments suggest to reconsider the separation thesis of economic theory and to propose an integrative concept of the firm as a private and a political

actor. However, in as much as business firms engage in political activity a *legitimation problem* arises as business firms and their managers are neither elected nor democratically controlled (see already Friedman, 1962). In the following we will explain the emerging problems, review various positions from economics and management theory, and attempt to develop possible answers to these concerns with the help of recent European approaches to business ethics and political theory. In particular, we will put emphasis on republican business ethics and Habermasian theory of democracy that promise to contribute to these issues.

## **Economic Theory and Free Trade**

Many economists do not support the UN Global Compact or other CSR-initiatives (see, e.g., Henderson, 2001; Krauss, 1997; Lal, 1998, 2003). Irwin (2002: 214), for instance, argues: “Still, the best and most direct way to raise wages and labor standards is to enhance the productivity of the workers through economic development. Trade and investment are important components of that development, and therefore efforts to limit international trade or to shut down the sweatshops are counterproductive”. In economic theory, the perception that only through free trade worldwide economic development and welfare becomes feasible is dominant (Bhagwati, 2002; Krauss, 1997; Norberg, 2003). A policy in favour of a worldwide harmonization of social and environmental standards would in comparison diminish this advantage of free trade. Standards are regarded as “non-tariff trade barriers” that only create obstacles for free trade. Out of this reason, developing countries have in multilateral meetings, like the WTO or the UNCTAD meetings, often voted against the introduction of social and environmental standards or the definition of a “social clause”. From the same background, Krauss (1997: 51) argues “The way to help poor people abroad is to open our markets to them not to force them to adopt ... human rights standards”. And even some economists from Third World Countries argue that “a lousy job is better than no job at all” (Martinez-Mont, 1996). Therefore, from the economic point of view democratization and social development may be seen as a result of economic development but not as its precondition.

## **Economic Theory and the Social Responsibility of the Corporation**

While the comments outlined above are directed towards state policy, some economists also criticize the social responsible behavior of TNCs (see, e.g., Henderson, 2001; Jensen, 2002; Sundaram and Inkpen, 2004), referring to the yardstick of Milton Friedman (1970) “the social responsibility of business is to increase its profits”. Friedman suggests that corporate social responsibility is a “fundamentally subversive doctrine” (1962: 133) and that socially responsible behavior exercised

by corporate managers will finally represent a threat to democratic power as these managers are not democratically controlled. Managers, as agents of the company owners, are obliged to act in the owner's interest which is usually to increase profits (Friedman, 1970, see also Jensen, 2002). Sundaram and Inkpen (2004: 355) claim that the "interests of stakeholders such as employees, suppliers, bondholders, communities, and customers are protected by contract law and by regulation". Therefore, the authors solely rely on the state apparatus to take care for societal issues while the managers of corporations should focus on value creation for shareholders. Only under these conditions managers take the effort to "increase the size of the pie for all constituencies" (354) and contribute to the well-being of society.

Profit-orientation, however, is not set unconditional. Economists stress that managers have to abide by national and local laws and by common decency. Friedman, e.g., refers to "basic rules of the society, both those embodied in law and those embodied in ethical custom" (Friedman, 1970: 218). This limitation of the pure profit-orientation has a good reason. Profit-orientation is *justified* by its expected contribution to societal growth and stability and the increase of public welfare that it generates from which all members of a society benefit (Jensen, 2002). This, however, only works under the precondition that the *state* sets the rules of the game and all members of the society can be forced to abide by these rules. Therefore, the coordination mechanism of the market only develops into the desired direction if the market is embedded in a *politically designed framework* of rules and regulations. This framework defines the rules that are necessary to achieve the optimal allocation of resources through market processes. In this model of the integration of society the design of the regulatory framework is the sole task of the state (Friedman, 1962; Sundaram and Inkpen, 2004). It is based on a division of labor between the public sphere (state) and the private sphere (economy). The state sets the rules of the game and the private firms pursue profits *within* these rules. Thus, in the economic model, firms are considered as *economic actors* only and an intrinsic political responsibility of the firm is rejected.

## **The Limits of the Liberal Model of Society**

It is debatable whether this liberal model of society still applies under the circumstances of *globalization* (Beck, 2000; Giddens, 1990; Habermas, 2001). Not only do economic activities cross the territory-bound validity of state regulation and bureaucracy. Due to technological progress it has also become possible for companies to split up their value-chain processes and distribute their production sites worldwide. Companies are no longer subject of the rules defined by the nation state. In their search for cost advantages they can arbitrate among alternative regulations (Ghemawat, 2003) choosing locations according to the firms' economic requirements. By doing so, economic actors undermine the internal sovereignty of the nation state, namely the ability of the state to independently set rules and limit or regulate any private activity on its territory (Reinicke and Witte, 2000; Habermas, 2001).

Interestingly, many economists do not regard the loss of regulatory capacity of the nation state as a problem of the liberal model of society. Instead, they take the competition between locations and regulations (competition of systems) as an opportunity to limit the influence of the state, to cut back on overregulation, and to stress market forces. They assume that such a competition of systems results in an optimal level of regulation (see, e.g., Marciano and Josselin, 2003). However, what is overlooked with these expectations is that a functioning competition requires “rules of the game” that are enforceable of an arbitrator. For the competition on markets of goods and services this role has been assigned to the state and its anti-trust regulations and authorities. For the competition of systems there is no comparable institution on a global level. To attract foreign capital developed countries tend to cut taxes or loosen the social safety net as a consequence (Avi-Yonah, 2000). Many developing countries do not protect human rights, tend to suppress unions, and have lax environmental regulation thereby increasing the pressure on other states to do likewise (Scherer and Smid, 2000). Obviously, we need institutions that determine which measures are regarded as “fairplay” in this competition of systems and which are not (see, e.g., Avi-Yonah, 2003). However, “neoliberalism cannot explain how the deficits in steering competencies and legitimation that emerge at the national level can be compensated at the supranational level without new forms of political regulation” (Habermas, 2001: 81).

## The Instrumentalization of Corporate Responsibility

Many scholars in business management deal with these developments in an ambiguous manner. This is particularly true for the research in the fields of “business and society”, “stakeholder theory” and “corporate social responsibility” that have gained wide attention. While these approaches address the problematic social and environmental consequences of business activities, many of them have in common the tacit acknowledgment of a dominance of the economic role of the firm. Therefore, these schools of thought do not create an adequate basis for an extended understanding of the role of the TNC in a world society (see critically Margolis and Walsh, 2003; Walsh, Weber, and Margolis, 2003). The *stakeholder approach* has been developed by Freeman in the 80s (Freeman, 1984). Freeman pointed out that managers not only have to satisfy the expectations of the shareholders or the contractors of the company but also need to recognize various stakeholder interests. Depending on the amount of pressure a single stakeholder can exert on the company in case of conflict, the stakeholder’s interests have to be taken into consideration. Despite the various calls for a normative theory (Donaldson and Preston, 1995) the stakeholder orientation often has been *instrumentalized* for profit maximization (Jones, 1995; McWilliams and Siegel, 2001; see critically Whetten, Rands, and Godfrey, 2002). The consequence is that only the stakes of groups that are either useful or able to harm the company economically will be recognized (see also Phillips, 2003). Consequently, as long as the norm of profit maximiza-

tion remains the final point of reference, “business and society” research engages in false labelling if it claims to deal with “corporate social responsibility” (see, critically, Whetten et al., 2002: 384). It rather feeds Milton Friedman’s doctrine “the social responsibility of business is to increase its profits”, because any CSR-activity in the end has to pay off (McWilliams and Siegel, 2001). As a result, its contribution to the governance challenges in a globalized world and the related discussion on the role and responsibilities of TNCs does not go far beyond the criticized pure economic reasoning.

There is, of course also an important body of literature in normative international business ethics (e.g., DeGeorge, 1993; Donaldson, 1989). These normative theories are based on philosophical conceptions such as Aristotelian virtues, Kantian duties, or social contracts (Hobbes, Rousseau) (e.g., Goodpaster, 1998; Trevino and Weaver, 1994). However, due to their focus on the link between management theory and moral theory they normally lack a critical analysis of the underlying concept of society and its democratic institutions and mechanisms.

## **Towards a New Concept of the Firm as a Responsible Political Actor**

In Europe there have been several attempts to start anew and create a more suited foundation for a theory of the firm as a socially responsible *political actor in society*. For instance, authors like Steinmann and his fellows of the republican approach to business ethics (Steinmann and Löhr, 1996; Steinmann and Scherer, 1998, 2000) as well as the “Integrative Economic Ethics” of Ulrich (2000, 2002) and recently the “extended view” of corporate citizenship presented by Matten and Crane point into a new direction (Matten and Crane, 2005; Matten, Crane, and Chapple, 2003). Matten and Crane (2005) suggest that the corporation holds a “catalyst function” of citizenship rights. In their conception “corporate citizenship” refers not so much to a citizen-like role of the corporation but defines corporate citizenship as the “role of the corporation in administering citizenship rights for individuals” (Matten and Crane, 2005: 173). Liberal models of society assume a private role of business and thus consider the business firm as a part of the private sphere whose boundaries are circumscribed by state regulation, i.e., by laws and their enforcement through administration (Parker and Braithwaite, 2003). In comparison, with regards to its corporate citizenship behavior Matten and Crane put the corporation in the *public sphere* and assume a *state-like role* of the corporation. With this “extended view” Matten and Crane take account of the observation that in times of globalization companies already fulfil the function of protecting, enabling and implementing citizenship rights, a function that in the liberal model is assumed to be exclusively under the authority of the state and its agencies. This is particularly true when (1) the state withdraws, (2) the state has not yet im-

plemented basic citizenship rights and when (3) the state is principally unable to do so (Matten and Crane, 2005).

Matten and Crane (2005) examine the possible channels of influence for corporations within the framework of “corporate citizenship”, namely the assistance of corporations in the implementation of private, social and political rights. They suggest that many TNCs by their activities already contribute to the administration of citizenship rights. This new conception of corporate citizenship provides a major contribution to the discussion because it highlights the role of the private corporation in the process of designing global rules and implementing citizenship rights. In addition, such a conceptualization of the role of the TNCs also touches upon a realm which in liberal theory has been in the sole responsibility of the state. However, both the authors do not address the *legitimacy issue* of whether and how the state-like role of the corporation can be controlled democratically. Instead, Matten and Crane explicitly confine their extended view to a descriptive approach of corporate social responsibility. Here, republican business ethics can be of help and deliver a way towards a resolution of the legitimacy issue.

Republican business ethics suggests a “supplementing function” of ethics in respect to positive law (Steinmann and Löhr, 1996; Steinmann and Scherer, 2000). That means that ethics in the sense of a self-organizing socially responsible activity is required whenever there is no other general rule available, from, e.g., state laws and regulations, or international regimes, or whenever these rules fail to resolve emerging problems of business. The supplementing function exerted by the private firm results from a *republican model of politics*. In contrast to the liberal model of society in the republican model the citizen has a double role as a private citizen (“bourgeois”) and as a citizen of a state or a community (“citoyen”) (Habermas, 1998). In the republican business ethics model it is assumed that the role of the corporation resembles this *double role of a citizen* in a state (Steinmann and Scherer, 2000; see also Moon, Crane and Matten, 2005; Ulrich, 2002: 30). In addition to the economic responsibility of the private business firm republican business ethics recognize “a *republican co-responsibility* of the business company” (Ulrich, 2000: 51).

This *political responsibility of the business firm* can be explained with the help of the political philosophy of Habermas (1996, 1998). As “citoyens”, private firms help to design rules that are of public interest and contribute to the peaceful stabilization of society. The “public interest” is not like in the liberal model of politics the result of the aggregation of individual interests but the result of a *communication process* through which individuals form or change their preferences over time (Elster, 1986). The aim of such an interactive process is to come up with a common understanding of which goals shall be pursued and what rules are required. Only within this collectively defined political order, a domain of freedom is defined where citizens as well as corporations pursue their individual interests as “private citizens”, i.e. as “bourgeois”. Individual freedom thus requires social rules as a *precondition*. In the *republican view* these rules are defined collectively by the citizens and business firms as much as NGOs and other actors of civil society

taking part in this process (Steinmann and Scherer, 2000; Ulrich, 2002). “In this way the republican citizen is credited with more than an exclusive concern with his or her private interests.” (Habermas, 1998: 241) In comparison, *liberal philosophy* only recognizes citizens as “private citizens” who always pursue their individual interests, in the market as well as in politics (see Elster, 1986; Habermas, 1998). Citizens’ choices in the market and in politics are an expression of their egoistic motives and therefore politics in the liberal conception is only *power politics*.

The perspective of the corporation as a *political actor* and as the *guarantor* of rights, puts its finger again on the problem of *legitimacy*. Namely, if corporations, as in Matten and Crane’s conception (2005), assume responsibility of state functions and generate global rules then it becomes obvious that it is necessary to *control* corporations like the democratic state needs to be controlled by its citizens. Therefore, the extended view of corporate citizenship provides arguments for the civic duties corporations have in the emerging global polity and thus has far-reaching consequences for a transnational concept of corporate governance. In particular, inasmuch as corporations engage in global governance their internal structures and processes have to become more democratic (see, e.g., Driver and Thompson, 2002; Parker, 2002). However, the *legitimacy issue of global governance* is not taken seriously enough in the extended view of Matten and Crane (2005). Even the republican business ethics of Steinmann et al. or Ulrich which was originally confined to the situation of a single nation state with a more or less properly working legislation and administration needs to be developed much further in order to cover the legitimacy issue in global business.

## The Changing Landscape of Corporate Citizenship Behavior

Due to globalization, established mechanisms of democratic governance erode. Processes of political decision-making transcend the borders of the political system and involve new actors such as TNCs and NGOs (Risse, 2002; Zürn, 2002). Based on the republican conception of business ethics as introduced by Steinmann et al. and Ulrich the transnational vacuum of legal regulation and moral orientation has to be filled by acts of *corporate self-regulation*. Additionally, as shown by Matten and Crane (2005), the *promotion of citizenship rights* is ascribed to the corporate actor. Especially TNCs, have already started to operate with such an enlarged understanding of social responsibility (Windsor, 2004). The murder of Ken Saro Wiwa in Nigeria has for instance changed Shell’s self-understanding from being an apolitical to a politicized actor, especially in their worldwide collaborations with repressive regimes (cf. Hollender and Fenichell, 2004: 58). Coca Cola is contributing to the worldwide fight against AIDS by using its globally spanned network of franchisees for distributing information and offering education (cf. Hollender and Fenichell, 2004: 35).

However, proponents of the traditional division of labor between the state and economy argue that those corporate activities might erode the power of the state apparatus even further (Reich, 1998) and surrender key aspects of a stable democratic regime to the arbitrariness of the corporate actors whose commitment remains fragile. In his analysis of the current research on stakeholder theory, Walsh (2005) comes to the conclusion that the argumentations of the different stakeholder approaches lead to the same results as neoclassical theory. The fight against AIDS, illiteracy, starvation or diseases is a political challenge for which the governments have to provide solutions. Comparable arguments have been advanced against corporate self-regulation (Henderson, 2001). Despite this mainstream consensus on the division of labor between corporations and governments, TNCs in some industries have, since the early 90s and due to public pressure, started to deal with the challenge of self-regulation. This in order to define the environmental and social standards of their operations in the global governance vacuum (Scherer and Smid, 2000). The discussion on the labor conditions in the globally expanded supply chains of the apparel industry shows that especially industries under NGO pressure took up the challenge (Zadek, 2004). Those acts of self-regulation are facing growing suspicion. They have been criticized for deception (Lantos, 1999) and window-dressing (Frenkel and Scott, 2002) since the self-imposed standards are often not the result of a broader and inclusive discourse with civil society and they are often implemented without any form of neutral third party control. It is sometimes “business as usual” that takes place behind the veil of well-formulated ethical rules (Rondinelli, 2002). King and Lenox (2000) have for instance shown in their analysis of the chemical industry’s *Responsible Care Program* that self-regulation without sanctions leads to opportunism. On average, members showed no different behavior to non-members.

As we have seen, some corporations have started to operate with a politically enlarged understanding of societal responsibility. The current research on CSR with its focus on the interface of management theory and moral philosophy is prepared to deal with the normative challenges that arise from the observation of corporate opportunism. Systematically expanding corporate activities (or outsourcing them) to countries with the lowest human rights and environmental standards poses problems that can be discussed against Donaldson and Dunfee’s hypernorms (1999) or within normative stakeholder concepts (Donaldson and Preston, 1995). Much more difficult to analyse in these theoretical settings are the normative consequences that arise at the interface of management theory and political theory (Walsh, 2005). Against the background of political theory, corporate acts of self-regulation, here described as political activities, do not only solve urgent problems but also provoke new normative questions. Corporations that fill the regulatory vacuum through acts of self-regulation obviously lack democratic legitimacy.



## The Democratic Deficit of Global Corporate Citizenship Behavior

The current dilemma of the debate on corporate responsibility is based on the widening gap between the decreasing efficiency of traditional mechanisms of national governance and the lacking legitimacy of emerging transnational mechanisms of governance. With the TNCs and NGOs moving centre stage, political processes are often dominated by actors that lack any form of traditional democratic legitimacy (Edwards and Zadek, 2003; Orts, 1995). This argument was also put forward by economists to criticize NGO and CSR initiatives (see, e.g., Lal, 2003; Rugman, 2000). However, in the role model of the TNC that we have sketched out in this paper, corporations decide on the further development of a global framework and influence its general conditions without being authorized or controlled democratically. As argued, their acts of self-regulation unfold a binding character upon legally unregulated aspects of global corporate activities. One could critically argue that, for instance, the Global Compact of the United Nations is based on paternalism that blindly trusts on the “good” corporation, without providing sufficient control mechanisms. Is corporate citizenship in the end not the solution but the problem itself when corporations exert their power to define global rules in a way that serves their economic interest best (see, e.g., Shell, 2004; Siedel, 2002) as recommendations for political lobbying? How can the democratic deficit in global governance be balanced (Edwards and Zadek, 2003, Orts, 1995)? Doesn’t the new role of the corporation have consequences for the internal constitution of the corporation, the corporate governance? Would it not be appropriate to argue that to the extent corporations act politically they also have to open up their internal structures and processes for public control, thereby enabling democratic legitimacy (Driver and Thompson, 2002; Parker, 2002)?

In his *deliberative model of democracy*, Habermas outlines an alternative approach to the mainstream liberal model and unfolds a de-centered concept of democratic governance (1996, 1998, 2001). While originally, governance activities were linked to nationally contained processes of public will-formation, on the global playing field, this understanding of legitimacy has to be *reframed* in all its dimensions. Globalization is changing the object of legitimacy questions (from state actors to private actors), the output of legitimacy (from hard national to “soft” transnational law), and the input (from national polity to transnational civil society). In the global context, with eroding state power and the emerging political authority of corporations and civil society associations, the legitimacy question rather addresses these new political actors instead of the traditional state actors.

The legitimacy of corporate acts of self-regulation and civic participation depends on the *political embeddedness* of the described CSR activities in the above mentioned Habermasian sense. We would argue that corporate political legitimacy refers to the link between corporate decision-making and discursive processes of public will-formation that express the democratic sovereignty of the transnationally

expanding civil society. Only the democratization of corporate activities through continuous discourse participation and enlarged mechanisms of transparency, monitoring and reporting can close the legitimacy gap of the corporation as a political actor in a globalized economy (Fung, 2003).

The idea of political embeddedness might be illustrated by a comparison between the Forest Stewardship Council (FSC) (see Hollenhorst and Johnson, 2005) and the Responsible Care Program (see King and Lenox, 2000). While the latter was developed by corporations as a voluntary set of rules and standards without the participation of civil society actors and without enforceable sanctions, the FSC has been developed in a broad and participatory process with corporations, NGOs and representatives of indigenous people involved. There are clear monitoring and labelling procedures applied and sanctions enforced (Hollenhorst & Johnson, 2005). Political embeddedness thus describes the application of standards of democratic deliberation outside the governmental institutions. This might provide a solution to the legitimacy problem that is provoked by the rising tide of corporate political activities. Self-regulation takes place in a broad process of democratic will-formation and control in collaboration with civil society actors. The FSC as an organization is designed around deliberative criteria such as broad participation, the attempt to exclude corporate power as a decision criterion, and a constant process of improvement based on critical feedback about the council's performance or form of organization.

In a global context one has to operate of course with a modified concept of legitimacy. On the one hand, political legitimacy in a global sense is *weaker* than in the traditional understanding since it refers to processes of self-regulation and production of transnational "soft law" instead of national hard law (Shelton, 2000). It is also weaker because it refers to the discourses of a globalizing civil society as the source of legitimacy instead of a nationally defined community. As argued by Teegen, Doh and Vachani (2004: 471) NGOs have started to organize their activities around "cosmopolitan" and "higher-order interests" that transcend national contexts. Self-regulation has started to emerge from the cooperation of TNC with transnational social movements that are able to mobilize civil society activities on a global scale (Smith, 2002). While on a national level, legitimacy has been weakened by the replacement of direct democracy through representative democracy, the link between political power and civic deliberation gets even more stretched on the global playing field. On the other hand, legitimacy in a global sense is *broader* because it includes non-state actors as objects of legitimacy claims and expands the understanding of responsibility beyond the common liability concept of responsibility (Young, 2004). A liability concept of responsibility is lead by the assumption that actors can be held responsible for "an action that caused a harm even if they did not intend the outcome" (Young, 2004: 368). Such a concept of responsibility is looking backward since it tries to judge past behavior. Young unfolds an alternative forward-looking approach to political responsibility that is displayed in an actor's engagement in collective processes of solving structural problems, e.g., the sweatshop conditions in globally expanded supply chains (Young, 2004).

## Conclusion: The Emerging Responsibility of Private Business Firms

The international debate on the corporations' role in the realization of global labor justice might serve as an illustration of the conditions of the political legitimacy of corporate acts of self-regulation and citizenship rights promotion, since those acts of self-regulation via codes of conduct play a crucial role especially in the process of "upholding labor standards in third world countries" (Frenkel and Scott, 2002: 30). In his recent contribution, Zadek describes the responsibility learning curve of Nike as a process of "civil learning" (Zadek, 2004: 126). As a pioneer in global outsourcing, the company has already been entangled in the debate on global labor standards since the early 90s. As most of the accused corporations, for several years it reacted with an outright rejection of any responsibility for the working conditions at its suppliers (Young, 2004). Facing a rising pressure, Nike started to accept responsibility and to develop solutions for the human rights problems at its suppliers. However, Nike did not involve the critics in its CSR implementation and communicated defensively on the issue. The problems remained and so did the pressure. Today, according to Zadek (2004), Nike has opened its decision-making process to civil society critics. They have launched multi-stakeholder initiatives with which they try to find solutions for emerging problems in collaboration with NGOs, labor organizations and public bodies.

This growing political embeddedness of their CSR activities is accompanied by growing transparency as well as stricter monitoring and reporting. What Zadek calls civil learning describes the *move towards a strengthened political legitimacy* of Nike's global activity: self-regulation is no longer an enforced act, which is sorted out by the corporation in splendid and patriarchal isolation. If anything, "Nike's metamorphosis from the poster child for irresponsibility to a leader in progressive practices" (Zadek, 2004: 125) describes a *democratic move* that implies proactive sensitivity for ethical challenges. It also describes an intensive networking of corporate and public discourses, a responsibility concept beyond liability, and an increased credibility due to transparency and accountability. It seems at least *possible* to close the legitimacy gap in global governance. However, as demanded by Young (2004), the assumption of political responsibility can not be reduced to the activities of the TNCs. It more likely has to include a broad set of actors who are involved in the human rights violations, or social and environmental issues, qua structural connectedness. It covers a set of actors that ranges from the sweatshop workers to national and transnational political bodies to the TNCs and even the consumers (Young, 2004). Problems such as global labor standards should not be solved by expert discourses but by processes of deliberation that are as broad as possible (Fung, 2003). The new role of the state according to Fung would be the arena management of those discourses. Public authorities facilitate discourses, guarantee the required transparency and the monitoring, they ensure the comparability of information and ensure the access of less powerful stake-

holders to the discourses (Fung, 2003). A similar role can be suggested for international institutions such as the UN, the ILO or the WTO (Kinley and Tadaki, 2004).

As we have seen, economic theory is reluctant to accept an intrinsic social responsibility of business firms. It is still based on a division of labor between economic and political domains and assumes a state system that is able to direct business activities via law and administration towards the common good. Only under this premise is it appropriate to confine business activities to a purely economic role. However, in a modern society with complex and dynamic conditions, this premise does not hold any more. It becomes even more problematic in a globalized world we observe today. Business firms have already reacted to the regulation deficits at the global level and responded to the growing expectations of society. They engage in activities to support human rights or define labor and environmental standards. In addition, business firms in many cases offer global public goods where the state is unable or unwilling to do so. It seems, as if on the global playing field, the traditional division of labor between business and politics can no longer be upheld.

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