



Ethics: A Basic Framework

Markets are sometimes described as “amoral,” but market participants frequently make ethical judgments about the people and practices they encounter in the marketplace. Indeed, most market actors prefer doing business with companies and individuals they can trust, and few—at least in a free and open society—willingly submit to treatment they regard as unethical. Wronged, injured, slighted, or ignored, many will take their business elsewhere, and some will actively seek redress through the courts, media, legislature, or other channels. Some will even “reward” or “punish” companies for their conduct toward third parties—for example, investors who favor good corporate citizens or customers who shun human rights violators.

A growing body of research points to these and other links between ethics and performance. Researchers have found, for example, that greater creativity is associated with fair rewards, mutual helpfulness, and honest information;¹ that employees are more likely to share knowledge in an environment of trust;² that avoiding misconduct and practicing good corporate citizenship contribute to a positive reputation;³ and that firms convicted of wrongdoing often experience lower returns in succeeding years.⁴ Of course, these findings do not prove that ethics always “pays.” Indeed, such a conclusion would be mistaken. But this and other research does show that a company’s ethics has important implications for its functioning as an organization, its ability to manage risk, its reputation in the marketplace, and its standing in the community.⁵

Despite these findings, ethical analysis has not traditionally been a defined part of management decision making. In most well-run companies, financial, legal, and competitive analyses are explicit and routine. Ethics, by contrast, is often left to instinct or “gut feel” and managed on an *ad hoc* basis as problems arise. As social science research indicates, many people make ethical judgments on the basis of instinct and emotion.⁶ If they use reason and analysis at all, they do so after the fact—to justify their instinctual response rather than to formulate or test their judgment.

Instinct, of course, is an important guide to action and should rarely be ignored. But people’s instincts frequently differ, and few people have such well-honed instincts that they automatically see the ethical issues involved in, say, a complex financial restructuring, a new business model, or a technology breakthrough. While instinct alone may work well enough in relatively simple, familiar situations, a more structured approach to identifying and addressing ethical issues is essential for business leaders today. This note outlines one such approach.

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A Framework

Scholars have long debated the definition of ethics.⁷ It has been defined as narrowly as “the study of right and wrong” and as broadly as “the general inquiry into what is good.”⁸ Our framework draws from only a small part of this vast territory. It involves four fundamental questions that an actor—individual, company, or group—should consider when evaluating a possible course of action:

- Is the action consistent with the actor’s basic duties?
- Does it respect the rights and other legitimate claims of the affected parties?
- Does it reflect best practice?
- Is it compatible with the actor’s own deeply held commitments?

These questions elicit different types of ethical norms or standards. The first two questions bring out basic requirements—the ethical minimum that would be expected of anyone in the situation. The third and fourth raise considerations that are somewhat more discretionary though nonetheless important for companies and individuals who view themselves as leaders, given that leadership, almost by definition, means doing more than the minimum. Effective use of this framework requires an understanding of four concepts from ethical theory, each associated with one of the questions:

Duties A basic moral duty is a requirement to act—or not act—in a certain way. Duties are typically owed to *other parties*—the company, colleagues, customers, the general public—though duties to oneself are also important. A distinction is sometimes drawn between “perfect” duties, which involve specific obligations to particular parties (e.g., to keep a promise), and “imperfect” duties, which are more general and open-ended (e.g., a duty of charity). Although any competent actor is presumed to be capable of fulfilling basic duties, specialized knowledge and expertise are often required. Many basic moral duties have been written into law or otherwise codified. For example, duties to respect property, refrain from fraud, and avoid certain injuries to others are enforced by many legal systems, and similar provisions are found in many codes of business conduct. Basic duties are not always explicit; they may also reside in tacit understandings of what human beings owe to one another. Because basic duties reflect widely held expectations, actions that breach these duties may give rise to criticism or blame. They may also subject the actor to demands for an apology or compensation for injuries caused by the offending action.

Rights Moral duties go hand in hand with moral rights. A right is often the converse of a duty. For example, one party’s property right corresponds with other parties’ duty not to steal. Similarly, one party’s right to know typically corresponds with another party’s duty to inform. A right is thus an entitlement to certain behavior from other people.⁹ Rights are sometimes categorized as “positive” if they require others to commit resources or take affirmative action (e.g., the right to education) and “negative” if they require others to forbear from certain actions (e.g., the right to privacy). Even though rights and duties are correlated, it is sometimes useful to focus on the rights side of the equation as rights are sometimes better defined than the related duties. Like basic duties, basic rights are often written into law or formal codes such as the Universal Declaration of Human Rights. Like failure to fulfill basic duties, failure to respect basic rights may be cause for blame, and rights violators may be penalized or required to compensate for harm caused by their actions.

Best practice Beyond basic rights and duties, most ethical systems also posit certain principles or standards of excellence. In ethical theory, these are sometimes referred to as “ideals,” “values,” or “aspirations.” They might also be termed “best practice” standards since they represent conduct that is desirable but not necessarily obligatory. The distinction between behavior that is ethically required

(the “musts”) and behavior that is good but not mandatory (“shoulds” or “good-to-dos”) is not always clear. One test is how the behavior would be received. Conduct that exemplifies best practice will often elicit praise or admiration even though its absence would not merit criticism or blame. For instance, honoring an agreement that it is not binding may earn the actor “moral credit” even if failure to carry out the agreement would have been excused. Similarly, a company that provides information beyond the requirements of law and basic honesty may garner praise for its candor even though nondisclosure would not have been blameworthy.

Commitments Most individuals and organizations take on moral commitments that stand outside—or go beyond—the publicly defined rights, duties, and standards that apply to all. These self-chosen, or subjective, commitments may be rooted in an individual’s personal values and beliefs, the culture and practices of the organization, or the needs of the larger society. For example, a manager may believe deeply in honesty—telling it “straight” when most others would spin or shade the truth. Or a company may define itself around a commitment to the environment, employee development, or extraordinary service to the customer. Such commitments typically represent an important aspect of the actor’s identity. Thus, although falling short on these commitments may not generate external criticism, it can be quite damaging to the actor’s self-concept and may even lead to the actor’s impaired functioning.

Applying the Framework

This framework sounds simple, but applying it can be difficult. In using it to evaluate a possible course of action, challenges arise at each step in the process.

Understanding the facts A crucial first step is to understand the proposed course of action. This may seem obvious, but in many cases decision makers do not fully understand the nature or consequences of actions they are contemplating or even their own ultimate purpose in acting. Confident in their own good intentions and focused on their own narrow objectives, they often overlook collateral effects, alternative interpretations, and likely impacts on others. Yet, such considerations are integral to a reliable analysis. Without them, it is impossible to determine whether an action is harmful, fair, or even legal—or to predict its effectiveness in furthering the actor’s own aims. Understanding key aspects of the action—its intended purpose, its proper description, and its likely consequences—is thus an essential step in the analytic process.

A useful tool for this purpose is what is sometimes called “stakeholder analysis” or “stakeholder impact assessment.”¹⁰ Stakeholder analysis has two basic components: identifying the parties likely to be affected by the action (that is, those with a “stake” to consider); and, for each party, mapping the action’s likely consequences—both positive and negative, short term and long. With the likely outcomes for various stakeholders thus arrayed, the proposed action can be more thoroughly and systematically evaluated against the relevant ethical standards (duties, rights, best practices, and commitments). This process may also reveal opportunities to mitigate unnecessary harms or enhance the planned action’s benefits. The workbook provided in **Exhibit 1** can be used to guide this analysis.

Identifying relevant standards A second challenge is defining what ethical standards to apply. Because ethical norms are often tacit rather than explicit and because they derive from varied sources—reason, law, philosophy, religion, custom, and perhaps even biology—deciding on the appropriate standards in a given situation is not always straightforward.¹¹ One starting point will be the company’s own code and relevant industry standards. Another useful point of reference is the Global Business Standards Codex, a compilation of standards commonly found in leading codes of conduct for business around the world.¹² Although the codex does not differentiate between basic

duties and best practices, it provides a list of widely accepted standards to govern a company's dealings with its stakeholders, including precepts such as obey the law, forgo bribery and deception, disclose conflicts of interest, practice fair dealing, safeguard health, and protect the environment.¹³ The creators of the codex found that most of the commonly occurring standards were elaborations of just eight basic principles. A summary of the standards associated with each is found in **Exhibit 2**.

Fiduciary principle: Act in the best interests of the company and its investors.

Property principle: Respect property and the rights of those who own it.

Reliability principle: Keep promises, agreements, contracts, and other commitments.

Transparency principle: Conduct business in a truthful and open manner.

Dignity principle: Respect the dignity of all people.

Fairness principle: Deal fairly with all parties.

Citizenship principle: Act as responsible members of the community.

Responsiveness principle: Be responsive to the legitimate claims and concerns of others.

While many of these principles—and their associated standards—have roots in numerous ethical traditions, their significance and interpretation can vary enormously across different social and cultural contexts. So it would be simplistic to call them “universal values.” Still, given their widespread endorsement, they provide a useful point of reference.¹⁴

Maintaining objectivity All forms of analysis are vulnerable to the prejudices of their users. To correct for self-serving and other biases in ethical analysis, many “tests” of ethical judgment have been offered. Three of the best known and most useful are:

Visibility: Would I be comfortable if this action were described on the front page of a respected newspaper?

Generality: Would I be comfortable if everyone in a similar situation did this?

Legacy: Is this how I'd like my leadership to be remembered?

These tests evoke varied perspectives for evaluating our judgments.¹⁵ The “visibility” test—also called the “transparency,” “sunshine,” or “newspaper” test—reminds us to consider how our actions may be viewed by others. The “generality” test asks us to consider what would happen if our actions became the general practice.¹⁶ Would society benefit? Would we want to live in such a society? The legacy test appeals to the decision maker's own future self-evaluation. Although these tests are presented as hypothetical, their importance for leaders is often real—given that leaders' actions are frequently reported in the press, replicated by others, and even, in some cases, recorded in history.

As this discussion indicates, ethical analysis requires rigorous thought and careful deliberation. In many cases, it will also require research and information gathering—on law and regulation, codes of conduct, customary practice, expert opinion, stakeholder concerns, public opinion, and other matters. Of course, ethical analysis is, to some extent, situational across time and cultures. As with legal and economic analysis, reasonable people will disagree, and errors will be made. But the magnitude of the errors can be substantially lessened and better decisions made if the method is consistently and carefully applied.

Exhibit 1 Action Planning: Ethical Analysis Workbook

Proposed action:

Principal actor(s):

Other assumptions:

Main objectives:

Assumed time frame:

Key stakeholders (affected parties)	Likely consequences		Ethical standards			
	Positive (short and long term)	Negative (short and long term)	Duties to this party	Rights of this party	Best practice toward this party	Commitments to this party

Exhibit 2 Widely Endorsed Standards of Corporate Conduct

Principles	What they require	What they prohibit
Fiduciary	Diligence, candor, loyalty to company Disclosure of conflicts of interest Prudence, intelligence, best efforts	Unauthorized self-dealing Self-benefit at expense of company Negligence, carelessness, half-hearted effort Bribery, inducing breach of fiduciary duty
Dignity	Protect human health, safety, privacy, dignity Respect fundamental human rights Affirmative action to develop human capacities Special concern for the vulnerable	Coercion, humiliation, invasion of privacy Injury to health, safety Force, violence, harming the innocent Violations of basic human rights
Property	Respect for others' property Safeguarding own property Responsible use of own property	Theft, embezzlement Misappropriation of intellectual property Waste Infringement on others' property
Transparency	Accuracy, truthfulness, honesty Accurate presentation of information Disclosure of material information Correction of misinformation	Fraud, deceit Misrepresentation Materially misleading nondisclosures
Reliability	Fidelity to commitments, keeping promises Fulfilling contracts, carrying out agreements Care in making commitments—not more than can deliver	Breach of promise Breach of contract Going back on one's word Fraudulent promises
Fairness	Fair dealing (in exchange) Fair treatment (opportunity, pay) Due process (notice, opportunity to be heard) Fair competition (conduct among rivals)	Preferential or arbitrary treatment Unfair discrimination Unfair competitive advantage Suppressing competition
Citizenship	Respect for law and regulation Share in maintaining the commons Cooperation with public officials Civic contribution Recognizing government's jurisdiction	Illegality, indifference to the law Freeloading, free riding Injury, damage to society, the environment Improper involvement in politics or government
Responsiveness	Readiness to listen Responding to complaints and suggestions Addressing legitimate concerns of others	Indifference to legitimate claims and claimants Neglect of serious concerns

Source: Based on Lynn S. Paine, Rohit Deshpandé, Joshua D. Margolis, and Kim E. Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards?" *Harvard Business Review* (December 2005).

Endnotes

¹ Teresa M. Amabile, "How to Kill Creativity," *Harvard Business Review* (September–October 1998): 77–87; "Mobilizing Creativity in Organizations," *California Management Review*, vol. 40, no. 1 (Fall 1997): 39–58.

² Anil K. Gupta and Vijay Govindarajan, "Knowledge Management's Social Dimension: Lessons from Nucor Steel," *Sloan Management Review* (Fall 2000): 71–80.

³ See, for example, Charles J. Fombrun, *Reputation: Realizing Value from the Corporate Image* (Boston, Mass.: Harvard Business School Press, 1996), esp. p. 6; Grahame Dowling, *Creating Corporate Reputations: Identity, Image, and Performance* (Oxford, U.K.: Oxford University Press, 2001), pp. 49–63.

⁴ Melissa S. Baucus and David A. Baucus, "Paying the Piper: An Empirical Examination of Longer-Term Financial Consequences of Illegal Corporate Behavior," *Academy of Management Review*, vol. 40, no. 1 (1997): 129–151.

⁵ For a review of this research, see Lynn Sharp Paine, *Value Shift: Why Companies Must Merge Social and Financial Imperatives to Achieve Superior Performance* (New York, N.Y.: McGraw-Hill, 2003), Ch. 2.

⁶ Jon Haidt, "The emotional dog and its rational tail: A social intuitionist approach to moral judgment," *Psychological Review* 108 (2001): 814–834.

⁷ Although the terms "ethics" and "morality" are sometimes defined differently, they are frequently used as interchangeable synonyms. This note treats the terms as interchangeable.

⁸ G.E. Moore, *Principia Ethica*, orig. 1903 (Cambridge, U.K.: Cambridge University Press, 1968), p. 2. For an overview of definitions, see, for example, *The Definition of Morality*, eds. G. Wallace and A.D.M. Walker (London: Methuen & Co Ltd, 1970).

⁹ On rights as compared to interests, see Ronald Dworkin, *Taking Rights Seriously* (Cambridge, Mass.: Harvard University Press, 1978).

¹⁰ A 1964 document is often cited as the origin of the term "stakeholder," but use became widespread after the 1984 publication of R. Edward Freeman, *Strategic Planning: A Stakeholder Approach* (Boston, Mass.: Pitman Publishing, 1984). Interpretations and usages have since proliferated, and the term has even given rise to a theory of the firm. For a roundup, see Thomas Donaldson and Lee E. Preston, "The Stakeholder Theory of the Corporation: Concepts, Evidence, and Implications," *Academy of Management Review*, vol. 20, no. 1 (1995): 65–91. Although the stakeholder theory of the firm has been criticized on various grounds, most critics acknowledge that stakeholders' claims cannot be ignored. See, for example, Elaine Sternberg, "Stakeholder Theory Exposed," *Corporate Governance Quarterly*, vol. 2, no. 1 (March 1996).

¹¹ See, for example, the research of Frans B.M. de Waal, research professor in psychobiology, Yerkes Regional Primate Research Center, Emory University, Atlanta, Georgia.

¹² Lynn S. Paine, Rohit Deshpande, Joshua D. Margolis, and Kim E. Bettcher, "Up to Code: Does Your Company's Conduct Meet World-Class Standards," *Harvard Business Review* (December 2005).

¹³ Compare, for example, recently promulgated codes such as the OECD Guidelines for Multinational Enterprises, OECD Policy Brief (June 2001); Caux Round Table Principles for Business (1994); United Nations Global Compact (1999). See also Muel Kaptein, "Business Codes of Multinational Firms: What Do They Say," *Journal of Business Ethics*, vol. 50, no. 1 (March 2004).

¹⁴ Widespread endorsement of these principles should perhaps be unsurprising. Although the world's ethical traditions vary widely, scholars tell us that some themes appear repeatedly over time and across traditions. Calls for honesty, fairness, reciprocity, and mutual assistance can be found in virtually all traditions, as can injunctions against deception, betrayal, theft, injustice, violence, and indifference to others. The recurrence of these themes suggests that humans may be biologically programmed for morality (as for language) and that certain ethical norms may have survival value for groups that embrace them. See, for example, Sissela Bok,

Common Values (Columbia, Mo.: University of Missouri Press, 1995); H.L.A., Hart, *The Concept of Law* (Oxford, U.K.: Clarendon Press, 1961), pp. 187–191 (on basic standards of conduct necessary for any society's functioning).

¹⁵ Other frequently cited tests include the “golden rule,” the “mirror test,” and the “sleep test.” For different formulations of the “golden rule” in different cultures, see Sissela Bok's entry on this topic in *The Oxford Companion to Philosophy*, ed. Ted Honderich (Oxford, U.K.: Oxford University Press, 1995), p. 321. For different versions of the “mirror” test, see Wendy Fischman, Becca Solomon, Deborah Greenspan, and Howard Gardner, *Making Good: How Young People Cope with Moral Dilemmas at Work* (Cambridge, Mass.: Harvard University Press, 2004), pp. 178–179.

¹⁶ The generality test is closely related to the “universalizability” test. See, for example, R.M. Hare, “The Structure of Ethics and Morals,” in *Essays in Ethical Theory* (Oxford, U.K.: Clarendon Press, 1989); Marcus Singer, *Generalization in Ethics* (New York, N.Y.: Knopf, 1961).