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DECISION MAKING

Ethical Managers Make Their Own Rules

by Sir Adrian Cadbury

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The editors of *Harvard Business Review* are glad to announce that “Ethical Managers Make Their Own Rules” has won HBR’s 1986 Ethics in Business Prize for the best original article written and submitted by a corporate manager on the ethical problems business executives face.

In 1900 Queen Victoria sent a decorative tin with a bar of chocolate inside to all of her soldiers who were serving in South Africa. These tins still turn up today, often complete with their contents, a tribute to the collecting instinct. At the time, the order faced my grandfather with an ethical dilemma. He owned and ran the second-largest chocolate company in Britain, so he was trying harder and the order meant additional work for the factory. Yet he was deeply and publicly opposed to the Anglo-Boer War. He resolved the dilemma by accepting the order, but carrying it out at cost. He therefore made no profit out of what he saw as an unjust war, his employees benefited from the additional work, the soldiers received their royal present, and I am still sent the tins.

My grandfather was able to resolve the conflict between the decision best for his business and his personal code of ethics because he and his family owned the firm which bore their name. Certainly his dilemma would have been more acute if he had had to take into account the interests of outside shareholders, many of whom would no doubt have been in favor both of the war and of profiting from it. But even so, not all my grandfather’s ethical dilemmas could be as straightforwardly resolved.

So strongly did my grandfather feel about the South African War that he acquired and financed the only British newspaper which opposed it. He was also against gambling, however, and so he tried to run the paper without any references to horse racing. The effect on the newspaper's circulation was such that he had to choose between his ethical beliefs. He decided, in the end, that it was more important that the paper's voice be heard as widely as possible than that gambling should thereby receive some mild encouragement. The decision was doubtless a relief to those working on the paper and to its readers.

The way my grandfather settled these two clashes of principle brings out some practical points about ethics and business decisions. In the first place, the possibility that ethical and commercial considerations will conflict has always faced those who run companies. It is not a new problem. The difference now is that a more widespread and critical interest is being taken in our decisions and in the ethical judgments which lie behind them.

Secondly, as the newspaper example demonstrates, ethical signposts do not always point in the same direction. My grandfather had to choose between opposing a war and condoning gambling. The rule that it is best to tell the truth often runs up against the rule that we should not hurt people's feelings unnecessarily. There is no simple, universal formula for solving ethical problems. We have to choose from our own codes of conduct whichever rules are appropriate to the case in hand; the outcome of those choices makes us who we are.

Lastly, while it is hard enough to resolve dilemmas when our personal rules of conduct conflict, the real difficulties arise when we have to make decisions which affect the interests of others. We can work out what weighting to give to our own rules through trial and error. But business decisions require us to do the same for others by allocating weights to all the conflicting interests which may be involved. Frequently, for example, we must balance the interests of employees against those of shareholders. But even that sounds more straightforward than it really is, because there may well be differing views among the shareholders, and the interests of past, present, and future employees are unlikely to be identical.

Eliminating ethical considerations from business decisions would simplify the management task, and Milton Friedman has urged something of the kind in arguing that the interaction between business and society should be left to the political process. "Few trends could so thoroughly undermine the very foundation of our free society," he writes in *Capitalism and Freedom,* "as the acceptance by corporate officials of a social responsibility other than to make as much money for their shareholders as possible."

But the simplicity of this approach is deceptive. Business is part of the social system and we cannot isolate the economic elements of major decisions from their social consequences. So there are no simple rules. Those who make business decisions have to assess the economic and social consequences of their actions as best as they can and come to their conclusions on limited information and in a limited time.

As will already be apparent, I use the word ethics to mean the guidelines or rules of conduct by which we aim to live. It is, of course, foolhardy to write about ethics at all, because you lay yourself open to the charge of taking up a position of moral superiority, of failing to practice what you preach, or both. I am not in a position to preach nor am I promoting a specific code of conduct. I believe, however, that it is useful to all of us who are responsible for business decisions to acknowledge the part which ethics plays in those decisions and to encourage discussion of how best to combine commercial and ethical judgments. Most business decisions involve some degree of ethical judgment; few can be taken solely on the basis of arithmetic.

While we refer to a company as having a set of standards, that is a convenient shorthand. The people who make up the company are responsible for its conduct and it is their collective actions which determine the company's standards. The ethical standards of a company are judged by its actions, not by pious statements of intent put out in its name. This does not mean that those who head companies should not set down what they believe their companies stand for—hard though that is to do. The character of a company is a matter of importance to those in it, to those who do business with it, and to those who are considering joining it.

What matters most, however, is where we stand as individual managers and how we behave when faced with decisions which require us to combine ethical and commercial judgments. In approaching such decisions, I believe it is helpful to go through two steps. The first is to determine, as precisely as we can, what our personal rules of conduct are. This does not mean drawing up a list of virtuous notions, which will probably end up as a watered-down version of the Scriptures without their literary merit. It does mean looking back at decisions we have made and working out from there what our rules actually are. The aim is to avoid confusing ourselves and everyone else by declaring one set of principles and acting on another. Our ethics are expressed in our actions, which is why they are usually clearer to others than to ourselves.

Once we know where we stand personally we can move on to the second step, which is to think through who else will be affected by the decision and how we should weight their interest in it. Some interests will be represented by well-organized groups; others will have no one to put their case. If a factory manager is negotiating a wage claim with employee representatives, their remit is to look after the interests of those who are already employed. Yet the effect of the wage settlement on the factory's costs may well determine whether new employees are likely to be taken on. So the manager cannot ignore the interest of potential employees in the outcome of the negotiation, even though that interest is not represented at the bargaining table.

The rise of organized interest groups makes it doubly important that managers consider the arguments of everyone with a legitimate interest in a decision's outcome. Interest groups seek publicity to promote their causes and they have the advantage of being single-minded: they are against building an airport on a certain site, for example, but take no responsibility for finding a better alternative. This narrow focus gives pressure groups a debating advantage against managements, which cannot evade the responsibility for taking decisions in the same way.

In *The Hard Problems of Management,* Mark Pastin has perceptively referred to this phenomenon as the ethical superiority of the uninvolved, and there is a good deal of it about. Pressure groups are skilled at seizing the high moral ground and arguing that our judgment as managers is at best biased and at worst influenced solely by private gain because we have a direct commercial interest in the outcome of our decisions. But as managers we are also responsible for arriving at business decisions which take account of all the interests concerned; the uninvolved are not.

At times the campaign to persuade companies to divest themselves of their South African subsidiaries has exemplified this kind of ethical high-handedness. Apartheid is abhorrent politically, socially, and morally. Those who argue that they can exert some influence on the direction of change by staying put believe this as sincerely as those who favor divestment. Yet many anti-apartheid campaigners reject the proposition that both sides have the same end in view. From their perspective it is self-evident that the only ethical course of action is for companies to wash their hands of the problems of South Africa by selling out.

Managers cannot be so self-assured. In deciding what weight to give to the arguments for and against divestment, we must consider who has what at stake in the outcome of the decision. The employees of a South African subsidiary have the most direct stake, as the decision affects their future; they are also the group whose voice is least likely to be heard outside South Africa. The shareholders have at stake any loss on divestment, against which must be balanced any gain in the value of their shares through severing the South African connection. The divestment lobby is the one group for whom the decision is costless either way.

What is clear even from this limited analysis is that there is no general answer to the question of whether companies should sell their South African subsidiaries or not. Pressure to reduce complicated issues to straightforward alternatives, one of which is right and the other wrong, is a regrettable sign of the times. But boards are rarely presented with two clearly opposed alternatives. Companies faced with the same issues will therefore properly come to different conclusions and their decisions may alter over time.

A less contentious divestment decision faced my own company when we decided to sell our foods division. Because the division was mainly a U.K. business with regional brands, it did not fit the company's strategy, which called for concentrating resources behind our confectionery and soft drinks brands internationally. But it was an attractive business in its own right and the decision to sell prompted both a management bid and external offers.

Employees working in the division strongly supported the management bid and made their views felt. In this instance, they were the best organized interest group and they had more information available to them to back their case than any of the other parties involved. What they had at stake was also very clear.

From the shareholders' point of view, the premium over asset value offered by the various bidders was a key aspect of the decision. They also had an interest in seeing the deal completed without regulatory delays and without diverting too much management attention from the ongoing business. In addition, the way in which the successful bidder would guard the brand name had to be considered, since the division would take with it products carrying the parent company's name.

In weighing the advantages and disadvantages of the various offers, the board considered all the groups, consumers among them, who would be affected by the sale. But our main task was to reconcile the interests of the employees and of the shareholders. (The more, of course, we can encourage employees to become shareholders, the closer together the interests of these two stakeholders will be brought.) The division's management upped its bid in the face of outside competition, and after due deliberation we decided to sell to the management team, believing that this choice best balanced the diverse interests at stake.

Companies whose activities are international face an additional complication in taking their decisions. They aim to work to the same standards of business conduct wherever they are and to behave as good corporate citizens of the countries in which they trade. But the two aims are not always compatible: promotion on merit may be the rule of the company and promotion by seniority the custom of the country. In addition, while the financial arithmetic on which companies base their decisions is generally accepted, what is considered ethical varies among cultures.

If what would be considered corruption in the company's home territory is an accepted business practice elsewhere, how are local managers expected to act? Companies could do business only in countries in which they feel ethically at home, provided always that their shareholders take the same view. But this approach could prove unduly restrictive, and there is also a certain arrogance in dismissing foreign codes of conduct without considering why they may be different. If companies find, for example, that they have to pay customs officers in another country just to do their job, it may be that the state is simply transferring its responsibilities to the private sector as an alternative to using taxation less efficiently to the same end.

Nevertheless, this example brings us to one of the most common ethical issues companies face—how far to go in buying business? What payments are legitimate for companies to make to win orders and, the reverse side of that coin, when do gifts to employees become bribes? I use two rules of thumb to test whether a payment is acceptable from the company's point of view: Is the payment on the face of the invoice? Would it embarrass the recipient to have the gift mentioned in the company newspaper?

The first test ensures that all payments, however unusual they may seem, are recorded and go through the books. The second is aimed at distinguishing bribes from gifts, a definition which depends on the size of the gift and the influence it is likely to have on the recipient. The value of a case of whiskey to me would be limited, because I only take it as medicine. We know ourselves whether a gift is acceptable or not and we know that others will know if they are aware of the nature of the gift.

As for payment on the face of the invoice, I have found it a useful general rule precisely because codes of conduct do vary round the world. It has legitimized some otherwise unlikely company payments, to the police in one country, for example, and to the official planning authorities in another, but all went through the books and were audited. Listing a payment on the face of the invoice may not be a sufficient ethical test, but it is a necessary one; payments outside the company's system are corrupt and corrupting.

The logic behind these rules of thumb is that openness and ethics go together and that actions are unethical if they will not stand scrutiny. Openness in arriving at decisions reflects the same logic. It gives those with an interest in a particular decision the chance to make their views known and opens to argument the basis on which the decision is finally taken. This in turn enables the decision makers to learn from experience and to improve their powers of judgment.

Openness is also, I believe, the best way to disarm outside suspicion of companies' motives and actions. Disclosure is not a panacea for improving the relations between business and society, but the willingness to operate an open system is the foundation of those relations. Business needs to be open to the views of society and open in return about its own activities; this is essential for the establishment of trust.

For the same reasons, as managers we need to be candid when making decisions about other people. Dr. Johnson reminds us that when it comes to lapidary inscriptions, "no man is upon oath." But what should be disclosed in references, in fairness to those looking for work and to those who are considering employing them?

The simplest rule would seem to be that we should write the kind of reference we would wish to read. Yet "do as you would be done by" says nothing about ethics. The actions which result from applying it could be ethical or unethical, depending on the standards of the initiator. The rule could be adapted to help managers determine their ethical standards, however, by reframing it as a question: If you did business with yourself, how ethical would you think you were?

Anonymous letters accusing an employee of doing something discreditable create another context in which candor is the wisest course. Such letters cannot by definition be answered, but they convey a message to those who receive them, however warped or unfair the message may be. I normally destroy these letters, but tell the person concerned what has been said. This conveys the disregard I attach to nameless allegation, but preserves the rule of openness. From a practical point of view, it serves as a warning if there is anything in the allegations; from an ethical point of view, the degree to which my judgment of the person may now be prejudiced is known between us.

The last aspect of ethics in business decisions I want to discuss concerns our responsibility for the level of employment; what can or should companies do about the provision of jobs? This issue is of immediate concern to European managers because unemployment is higher in Europe than it is in the United States and the net number of new jobs created has been much lower. It comes to the fore whenever companies face decisions which require a trade-off between increasing efficiency and reducing numbers employed.

If you believe, as I do, that the primary purpose of a company is to satisfy the needs of its customers and to do so profitably, the creation of jobs cannot be the company's goal as well. Satisfying customers requires companies to compete in the marketplace, and so we cannot opt out of introducing new technology, for example, to preserve jobs. To do so would be to deny consumers the benefits of progress, to shortchange the shareholders, and in the longer run to put the jobs of everyone in the company at risk. What destroys jobs certainly and permanently is the failure to be competitive.

Experience says that the introduction of new technology creates more jobs than it eliminates, in ways which cannot be forecast. It may do so, however, only after a time lag, and those displaced may not, through lack of skills, be able to take advantage of the new opportunities when they arise. Nevertheless, the company's prime responsibility to everyone who has a stake in it is to retain its competitive edge, even if this means a loss of jobs in the short run.

Where companies do have a social responsibility, however, is in how we manage that situation, how we smooth the path of technological change. Companies are responsible for the timing of such changes and we are in a position to involve those who will be affected by the way in which those changes are introduced. We also have a vital resource in our capacity to provide training, so that continuing employees can take advantage of change and those who may lose their jobs can more readily find new ones.

In the United Kingdom, an organization called Business in the Community has been established to encourage the formation of new enterprises. Companies have backed it with cash and with secondments. The secondment of able managers to worthwhile institutions is a particularly effective expression of concern, because the ability to manage is such a scarce resource. Through Business in the Community we can create jobs collectively, even if we cannot do so individually, and it is clearly in our interest to improve the economic and social climate in this way.

Throughout, I have been writing about the responsibilities of those who head companies and my emphasis has been on taking decisions, because that is what directors and managers are appointed to do. What concerns me is that too often the public pressures which are put on companies in the name of ethics encourage their boards to put off decisions or to wash their hands of problems. There may well be commercial reasons for those choices, but there are rarely ethical ones. The ethical bases on which decisions are arrived at will vary among companies, but shelving those decisions is likely to be the least ethical course.

The company which takes drastic action in order to survive is more likely to be criticized publicly than the one which fails to grasp the nettle and gradually but inexorably declines. There is always a temptation to postpone difficult decisions, but it is not in society's interests that hard choices should be evaded because of public clamor or the possibility of legal action. Companies need to be encouraged to take the decisions which face them; the responsibility for providing that encouragement rests with society as a whole.

Society sets the ethical framework within which those who run companies have to work out their own codes of conduct. Responsibility for decisions, therefore, runs both ways. Business has to take account of its responsibilities to society in coming to its decisions, but society has to accept its responsibilities for setting the standards against which those decisions are made.

George Adrian Hayhurst Cadbury is chairman of Cadbury Schweppes PLC. Readers who would like to know more about Sir Adrian's views on management practice and ethics can read "Cadbury Schweppes: More Than Chocolate and Tonic," an interview with HBR that appeared in January–February 1983.

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