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The Moral Assessment of Corporate Decision Making

In response to a number of widely criticized trends in American economic life—including corporate downsizing and factory relocations, widening income disparities, and changes in worker-management relations—there has been a resurgence of interest in the question of what constitutes responsible corporate behavior. Rejecting the view that business managers are accountable only to their stockholders, many people have argued that corporations also have obligations to their workers, to the communities where they are located, and to society in general. In order to carry out these obligations, managers must be prepared to make ethical judgments as they formulate and assess corporate policies.

There is, of course, no shortage of advice on how best to think about such policies. One source of advice is cognitive psychology. A prominent researcher in this field, Max Bazerman, has designed laboratory experiments to investigate managerial judgment; he has also written about practical problems for managers and business students. Bazerman finds that ethical judgment, including judgment of corporate behavior, is prone to irrationality and inconsistency. Even though he does not propose ethical policies for firms in the way that moral philosophers or ethicists might, he does give relevant advice to managers: his purpose in writing is to tell people how they may alter their judgments, including moral judgments, in order to avoid irrationality.

To make its research readily available to a broad audience, the Institute for Philosophy and Public Policy publishes this quarterly newsletter. Articles are intended to advance philosophically informed debate on current policy choices; the views presented are not necessarily those of the Institute or its sponsors.

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To his credit, Bazerman is aware of the difficulties that may attach to finding irrationality in moral judgment. "We are all entitled to our personal judgments about what we think is fair," he cautiously writes. "As a result, most research on fairness has avoided any evaluative statements about the irrationality of judgments of fairness." Nonetheless, Bazerman argues that certain ways of assessing fairness lead to "anger, jealousy, and inefficiency." If "we are to reduce or eliminate dysfunctional perceptions of fairness," he writes, "we need to confront the limits of rationality in these perceptions."

It turns out, however, that the conclusions Bazerman reaches about the irrationality of certain judgments imply a commitment to some implausible moral views. Furthermore, a careful reading of his examples suggests that people who make these "irrational" judgments may have plausible and coherent moral commitments that underlie their responses to corporate decisions. The purpose of this essay is to identify these commitments and consider their implications for understanding corporate responsibility.

Salary Change

Bazerman develops his position about the irrationality of moral judgment in business settings through discussion of a well-known set of experiments conducted by Daniel Kahneman and his colleagues. In these experiments (which we refer to as "Salary Change") each of two groups of subjects was presented with one of the following problems:

Problem A: A company is making a small profit. It is located in a community experiencing a recession with substantial unemployment but no inflation. Many workers are eager to work at the company. The company decides to decrease wages and salaries 7 percent this year.

Problem B: A company is making a small profit. It is located in a community experiencing a recession with substantial unemployment and inflation of 12 percent. Many workers are eager to work at the company. The company decides to increase wages and salaries 5 percent this year.

Among the respondents in the Kahneman experiment, 62 percent thought that the company's behavior in Problem A was unfair. In contrast, only 22 percent thought that the company's behavior in Problem B was unfair. For Bazerman, these findings provide an example of the irrationality he advises managers to avoid. In terms of inflation-adjusted dollars, he points out, the employees in Problem A and Problem B get approximately the same salary. Therefore, the companies in the two problems treat their employees in the same way, and it is irrational (or not "logical") to respond to the two cases differently. In Bazerman's

view, the research subjects should have thought only about how well-off the company's pay policy left employees in terms of real buying power. Since the outcomes for individual employees come out the same in Problem A and in Problem B, Bazerman thinks that attitudes toward the company should be the same in both cases.

We believe that the best way to understand Bazerman's charge of irrationality here is to suppose that he embraces the position philosophers call consequentialism, which holds that the moral rightness of an action must be measured solely in terms of the goodness of the action's consequences. Bazerman suggests that because the consequences for employees in Problem A and Problem B are the same, the two cases are morally on par and involve equally fair treatment of the employees. In judging the comparative moral status of two acts, then, all that matters are the consequences. Because the consequences of employer pay policy are the same in the two cases, it is irrational, Bazerman suggests, for people to see a moral difference between them.

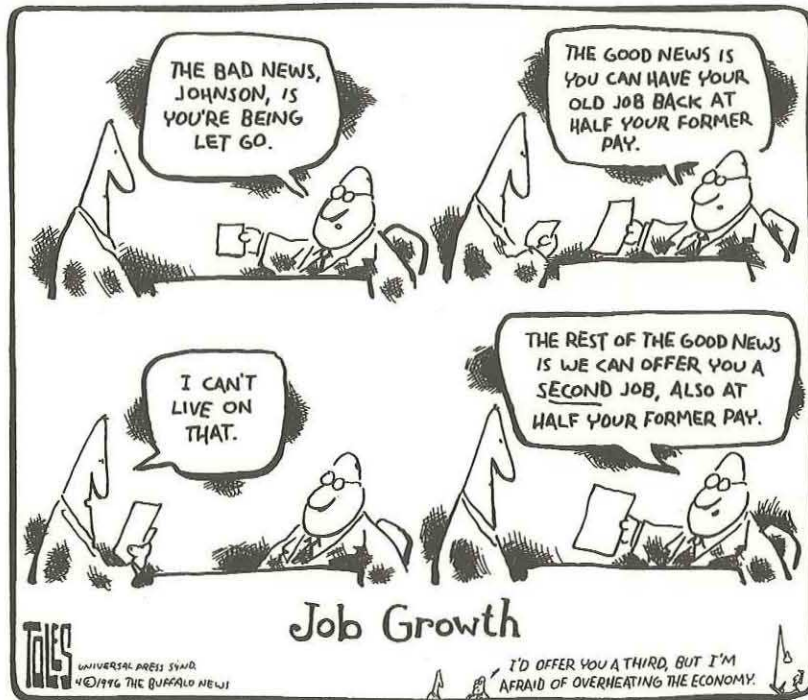
What happens, though, if one does not follow Bazerman in accepting consequentialism as a basis for assessing the rationality of the experimental subjects? In that case, it becomes much harder to justify the charge of irrationality. Once it is acknowledged that moral norms other than the consequentialist might plausibly be attributed to the subjects in Salary Change, the possible grounds for making and assessing corporate decisions without incurring the charge of irrationality prove to be broader than Bazerman's framework allows.

Alternative Norms

What other moral norms might be governing the responses of the subjects in the Kahneman study? One set of alternatives—usually described as deontological norms—have in common the idea that in assessing the moral rightness of an action, one cannot look simply, if at all, at the goodness of the consequences. The coherence and plausibility of deontological norms have been defended by respected moral philosophers, such as Alan Donagan and Thomas Nagel. And social psychologists, including Elaine Walster and Ronald Cohen, have argued that certain deontological norms concerning equity and justice exercise a powerful influence on the judgment and motivation of ordinary people.

Two deontological norms appear to have special potential significance for Salary Change: one concerns causal responsibility and the other concerns rights. Each of these norms suggests a distinctive interpretation of the Salary Change results.

Consider, first, the causal responsibility interpretation. While it is indisputable that neither employees in



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Problem A nor those in Problem B enjoy an increase in real income, the explanation as to why members of each group of employees lose out will differ. An employee in Problem B may explain his bad lot at least in part by saying that inflation is eating up the modest raise that his company gave him. A different explanation is available to an employee in Problem A, however: he may explain that the company took away some of his salary, perhaps at the same time complaining that the company should be helping him out. The nexus of causal responsibility identified in the two cases thus differs: in one case an employee explains his loss by appeal to the ailing economy, in the other case the employee explains the loss by appeal to the firm's action, which directly deprives him of money. Or one might say that in one case the company allows an economic harm to occur, but in the other case the company causes an economic harm.

Notions of causal responsibility are quite ancient, yet retain their credibility for contemporary philosophers working on problems in ethics. In a lucid review of these notions, Samuel Scheffler suggests that they include "the doctrine that individuals have a special responsibility for what they themselves do, as opposed to what they merely fail to prevent."

According to a second deontological idea of moral responsibility identified by Scheffler, one may have distinctive responsibilities (or "special obligations") toward those "to whom one stands in certain significant sorts of relationships." While Scheffler admits that there is no "consensus about the type of relationships that give rise to special obligations," it is clear, he argues, that such relationships play an important role in moral thought. Among these relationships, Scheffler includes friendship, membership in the same trade union, and the relationship of being coworkers. All these relationships seem to involve groups of people with shared interests and mutual dependence. The firm and its employees have this characteristic. So it is coherent to suppose that a firm's relation with its employees forms a basis of special obligations.

We might, then, characterize a deontological moral norm applying to firms as follows. The moral acceptability of a salary change must be measured in part by whether the change satisfies special responsibilities of the firm that would make the change. It counts against a salary change that it compromises special responsibilities that a firm owes, even if such a compromise would be comparatively favorable to the interests of the employees. If the experimental subjects in Salary

Change adopted their judgments of fairness in accordance with this norm, their responses reflected their belief that the nexus of causal responsibility matters morally, that it makes a difference morally whether the employee is economically harmed because the firm causes that harm or because the firm allows that harm to happen.

A similar point may be framed in terms of rights. Suppose that Problem A employees have developed certain salary rights which a pay decrease would infringe, while Problem B employees have no counterpart right to a raise that beats inflation. The existence of these two very different sets of rights will serve as a basis for certain responsibilities to Problem A employees but not to Problem B employees. To the deontological norm of causal responsibility, then, we may add a deontological norm of rights: the moral acceptability of a salary change must be measured in part by its impact on the rights of those affected by it; it counts against a salary change that it compromises individual rights, even if such a compromise would be comparatively favorable to the interests of the employees.

If experimental subjects believe that such rights exist, then consistency would require them to hold different attitudes about the fairness of the company's behavior in Problem A and Problem B. Contrary to Bazerman's suggestion, there would be nothing irrational in their attitudes about the fairness of company behavior.

Preferring the Status Quo

Results that psychologists obtain outside the realm of research into judgments of fairness may have encouraged Bazerman and others to find irrationality in experimental responses to Salary Change. In issues of valuation, for example, people attach importance to the status quo in ways that seem to defy rational explanation.

One intriguing example of this phenomenon, also investigated by Kahneman and his associates and discussed by Bazerman, is the endowment effect. Experimenters presented coffee mugs to a roomful of people, informing some of the people that they had just been given one of these mugs (and thus had just become mug owners) and the others that they were not being given the mugs. They then asked mug owners the price at which they would be willing to part with the mug, and asked the non-mug owners how much they would be willing to pay for the mug. Interestingly, the set of prices varied profoundly between owners and non-owners. Yet it hardly seems plausible that a mug's value varies so radically depending on whether one happens to own it or not.

Now plainly, whether you sell the mug and hence lose it, or whether you buy the mug and hence gain it,

there is some departure from the status quo. What psychologists claim to have discovered, however, is that as a general matter, people seem to regard it as more valuable to avoid going below the status quo than to improve over the status quo. One might suppose, then, that psychologists have discovered a broad-ranging pathology of human cognition: that subjects display irrationality in the way they tend to overvalue the status quo.

The difference in attitudes toward the company behavior in Problem A and Problem B might also be regarded as an instance of this pathology. Lowering income brings employees below the status quo; it causes a loss. Not giving a raise to keep income at pace with inflation, on the other hand, is merely not allowing one to make a nominal gain over the status quo. Because people irrationally see a loss, other things equal, as worse than failure to realize a gain, they will, researchers suggest, irrationally see the pay cut as worse than the failure to give a raise.

If the difference in attitude toward Problem A and Problem B is based on an irrational judgment regarding the status quo, it seems frivolous to defend it in terms of an entrenched and innocent preference for

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deontological as against consequentialist norms. But there is good reason to resist finding pathology here. Nobody has demonstrated that according special status to the status quo always signals error. Indeed, it seems quite plausible that sometimes the existence of a status quo is a source of special rights.

Consider the case of organ transplants. Suppose that society can take Fred's organs and give them to Tom, Dick and Harry. If it refuses to impose such a loss on Fred in order to achieve a gain for the others, it is not because society irrationally values avoiding loss over securing gain. It is instead because Fred has a right to his organs, and it is wrong to violate that right even if doing so might result in a rather sizable social gain. By protecting Fred's rights, society may be protecting the status quo, which involves saving fewer lives rather than many, but protecting the status quo seems a very different kind of activity here than in the case of valuing coffee mugs.

While not every status quo arrangement may be a source of rights, it seems inescapable that some of them are. The issue of rights presents a complication that is simply not at issue in the mug case. Even if, as Bazerman and his colleagues suggest, it is sometimes

irrational to attach more value to losses than to gains in simple market exchanges where nobody's rights are threatened, in cases where moral issues are at stake, the status quo may represent interests that society reasonably chooses to protect and which therefore form a basis of individual rights.

Corporate Responsibility and Philanthropy

Despite limitations on the analyses cognitive psychologists offer, it is important not to underestimate the significance of their experimental results. These results reveal much about the nature of the choices that managers confront. The relevance of the results can be demonstrated by reflecting on a typical problem for bank executives deliberating over issues of corporate responsibility.

Consider the social responsibility campaign of Chase Manhattan Bank. Like most large firms, Chase Manhattan is not shy about making the case that it scores high on the scale for responsible corporate conduct. For example, the bank publishes a *Chase Manhattan Corporate Responsibility Annual Report*, in which it lists activities intended to demonstrate its commitment to corporate responsibility. In 1993, the brochure documented about fifteen hundred charitable actions, mainly donations of money. These donations amounted to nearly \$10 million, roughly one percent of the bank's pretax income for the year.

The brochure is fascinating not only because of the large number of charitable actions it mentions, but also because of the enormous diversity of charitable activities it describes. In 1993, for example, these included \$500 for the purchase of bicycles for New York City Police to patrol a park; \$500 for the Connecticut Association for Mental Health; \$1,000 for the Chesapeake Bay Foundation; \$500 to People Against Sexual Abuse, Inc.; \$500 to the Chinatown Day Care Center, Inc.

One may infer from the brochure's title that the executives who approved it regard the brochure as an argument that the bank is a responsible corporation. Still, aside from some broadly aspirational remarks, the brochure contains little more than a very long list of charitable actions. This raises the question, How far does a heterogeneous list of good deeds go toward demonstrating corporate responsibility? Should we understand corporate responsibility as simply giving lots of money to lots of worthy causes? If so, then corporate responsibility might be viewed in terms of what we will call the "Lofty Strategy": if one gives lots of money to lots of really good causes, then, other things equal, one gets a high score on corporate responsibility.

What makes the Lofty Strategy appear lofty, no doubt, is that it exhibits an apparent commitment to impartial altruism: Chase Manhattan plainly purports

to be altruistic, at least in the weak sense that it engages in charitable acts aimed at advancing the interests of others. Chase Manhattan also seems to be impartial, because the interests it aims to advance are not those of people with whom it stands in some special relation, but instead people who are particularly needy. The rationale that underlies the Lofty Strategy should now be familiar. The Lofty Strategy seems to conform to a consequentialist moral norm, because it seems to identify the morally acceptable choices simply in terms of the amount of good done, and not in terms of satisfying obligations arising out of special relationships.

Despite the obvious appeal of the Lofty Strategy, some of the experimental evidence cited above raises doubt about its psychological and moral adequacy, and about its prospects for satisfying deeply entrenched social ideas of moral decency. The Salary Change results, for example, suggest that an executive deliberating about how to conceive of his bank's social responsibility must seriously consider an alternative to the Lofty Strategy—an alternative that we will call the "Involved Strategy." According to the Involved Strategy, a bank, in crafting its policy for corporate responsibility, should consider not merely how much good it does, but also whether it satisfies special obligations it incurs through its commercial activity.

How should we expect a bank which accepts the Involved Strategy to behave differently from a bank which accepts the Lofty Strategy? The key idea is to focus on the moral significance of the harm one causes or the rights one affects, even when these notions cannot be reduced to purely consequentialist considerations.

Suppose, for example, that Acme Bank's policy conforms to other bank policy in the community, which recognizes a presumption of financing only highly collateralized loan applicants. Also suppose that this policy, while not amounting to an illegal policy of redlining, has in fact led to a disproportionate number of loan denials to members of minority communities, and that economic development languishes in minority communities. As things stand now, one might plausibly explain the economic difficulties of minorities in these communities at least partially in terms of bank loan policy. It then becomes arguable, on deontological grounds, that Acme should recognize responsibility for this suffering and has a special obligation to help out.

Not all deontological arguments relevant to assessing bank responsibility bear on disadvantaged classes. Arguably when banks make people vulnerable to harm, they have a responsibility to protect them when the harm materializes, even if it is not strictly speaking the bank's fault that the harm occurs. Suppose that a bank engages in a robust policy of issuing credit cards