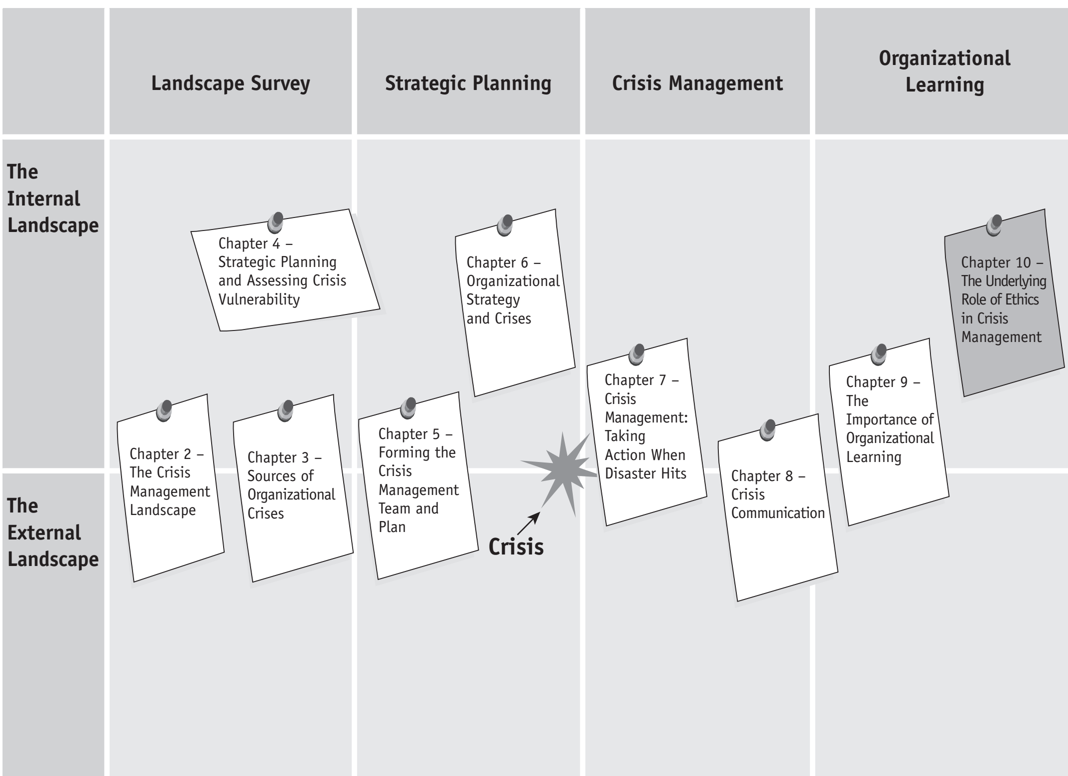
CHAPTER 10

The Underlying Role of Ethics in Crisis Management



Hawks Nest

In southern West Virginia, there is an engineering feat that few people know about except for the locals and the tourists who happen to stop by the small roadside park overlooking the project. It is an underground tunnel, about 3 miles long, that carries water from a dam to a small hydroelectric plant perched securely on the side of a mountain. The purpose of the project was to supply electricity to the Union Carbide plant, then located in Alloy, West Virginia, about 6 miles away. The tunnel was built during the Great Depression, mostly by poor workers who migrated to the area seeking employment (Cherniak, 1986).

The project itself was somewhat ingenious because it solved a problem faced by Union Carbide. Additional electricity was needed to power its new plant, but the prospects of supplying it with hydroelectric power seemed bleak because the New River—one of only a few rivers in the United States that flow north—was (and still is) a slow-moving, narrow band of water that does not have enough force to power a hydroelectric plant in that location. The engineers came up with a clever solution: Construct a dam to build up water volume and then pitch it in a downward direction to give it force (Cherniak, 1986). A small hydroelectric building with four turbines was positioned where the water emerged with great force from the tunnel. The result was a facility that still makes electricity to this day (Crandall & Crandall, 2002).

But there is a darker side to this project. The tunnel contractor, Virginia engineering firm Rinehart and Dennis, drastically cut corners to save on project time and expenses. Workers were forced to go inside the dusty tunnel shortly after explosives had been detonated to begin clearing out the debris. Although engineers were supplied with respirators, those doing the manual labor were not. When silica rock was encountered, the resulting fine dust that the explosion had created was inhaled by the workers as they removed debris from the tunnel shaft. As a result, many of these laborers developed silicosis, a debilitating lung disease that eventually causes death. This disease is avoidable if respirators are worn.

Rinehart and Dennis also used another cost-cutting measure: dry drilling. Wet drilling should have been used to minimize dust levels. The downside is that wet drilling slows the extraction process, unlike dry drilling, which is faster but also creates more dust (Orr & Dragan, 1981; Rowh, 1981). The additional dust associated with the dry drilling, coupled with the lack of respirators, was another factor that led to sickness in these workers.

The number of deaths attributed to the Hawks Nest Tunnel can only be estimated because Social Security records did not exist at the time (Cherniak, 1986). The estimates vary depending on the source of information. Rinehart and Dennis submitted a figure of 65 total deaths, whereas Union Carbide, the ultimate user of the Hawks Nest tunnel, counted 109 fatalities. In his account of the Hawks Nest incident, Martin Cherniak estimates a total of 764 deaths. Regardless of the exact number, the figures are high relative to today's standards of industrial safety. As one might expect, the death estimates become more conservative as the source of information moves closer to the tunnel contractor (Crandall & Crandall, 2002).

Background

There is an underlying problem in many of the crisis events discussed in this book. This problem does not manifest itself in every crisis, but it is substantial nonetheless. Why do seemingly preventable crises happen again and again? The answer can be found with a firm's employees, particularly managers and top-level business executives and their desire to gain unfairly at the expense of another party. This problem appears in many forms, but the results are usually the same: an organizational crisis of some type, stakeholders that have been hurt, and prevention that would have cost pennies when compared to the damage done.

The Hawks Nest Tunnel incident was one of the first major industrial crises in the United States. Although the tunnel was a remarkable success, the human resource tragedy was enormous. The deaths of these workers were entirely preventable, but tunnel contractor Rinehart and Dennis seemed to decide that breathing protection and other safety measures be abandoned in order to maximize profits. The contractor did not escape unscathed, however. Within 5 years of the project, its assets were liquidated, a victim of bad publicity, lawsuits, and loss of revenue.

In an age when Enron, Arthur Andersen, WorldCom, Tyco, and Adelphia are more commonly known scandal-ridden companies, why focus on a human tragedy that occurred more than half a century ago? The Hawks Nest Tunnel incident clearly illustrates the fact that some crises have human roots that can be traced back to unethical or irresponsible behavior by key decision makers. In addition, such behaviors are not confined to any specific time period in history. Human-induced crises have always occurred and will continue to occur, an inescapable reality. However, we also know that some organizations seem to do better than others at avoiding these types of crises because they put an emphasis on promoting ethical behavior throughout their organizations. This fact also is inescapable, and a cause for hope.

In this chapter we examine human-induced crises more closely, specifically those linked to unethical behavior. We examine these types of crises through the crisis management framework presented in this book. The chapter begins with a brief review of the concept of business ethics. Next, we survey the landscape in which unethical behaviors reside. The discussion proceeds to the strategic planning phase where we will consider how organizations, industries, and ultimately government regulations seek to prevent unethical behavior. The crisis management phase involves the management of internal and external stakeholders during this acute segment of the crisis. We examine what works and does not work, using an ethical perspective. We conclude by considering the organizational learning phase and what should occur at the micro and macro levels when stakeholders seek to learn lessons from experiencing scandal-ridden crises.

What Is Business Ethics?

Business ethics looks at issues of right and wrong in a business context (Carroll & Buchholtz, 2003). A related but distinct concept is corporate social

TABLE 10.1 The Components of Corporate Social Responsibility (CSR)

Component of CSR	*Key Thought to Understanding*	*Manifestations*
Economic	Be profitable	Maximize revenues Cut expenses Maximize profits Increase shareholder wealth
Legal	Obey the law	Abide by all legal regulations Stay within industry standards Maintain all contract and warranty obligations
Ethical	Avoid questionable practices	Go beyond just obeying the law, abide by the spirit of the law as well Avoid practices that may appear to be suspicious, even if they are legal Do the right thing, and be just and fair
Philanthropic	Be a good corporate citizen	Make financial contributions to stakeholders in the community Seek to be a good neighbor in the community by making it a better place to live Look for ways to support education, health/human services, and the arts

Source: Adapted from Carroll, A., & Buchholtz, A. (2003). *Business & Society: Ethics and Stakeholder Management* (5th ed.). Cincinnati, OH: Thompson South-Western, pp. 39–40.

responsibility (CSR), which maintains that businesses should seek social benefits for society as well as economic benefits for the business (Post, Lawrence, & Weber, 2002). A popular framework for looking at the two concepts of business ethics and CSR is shown in Table 10.1. In this framework, proposed by Carroll & Buchholtz, (2003), CSR is made up of our four parts: economic, legal, ethical, and philanthropic responsibilities. Above all, businesses must meet their economic responsibility by being profitable while operating within the confines of the law.

There is also a realm of business behavior that goes beyond obeying the law. Ethical responsibility seeks to avoid behaviors that are questionable though not necessarily illegal. Practically speaking, it is not possible to develop laws to prohibit every unethical business activity. Consider also that many companies sell products or services that are legal, but are considered by many to be unethical in some contexts. Hartley (1993) documents the now infamous PowerMaster Beer controversy in which malt liquor, a legal product, was heavily marketed to poor urban areas, markets where crime and youth despair were prevalent. This combination created an unethical situation in the eyes of many community stakeholders who saw this product contributing to even higher crime problems in urban neighborhoods. More recently, the mortgage crisis of the early 2000s that adversely affected an entire industry could have been avoided if individual lenders had simply refused to issue loans with terms that were likely to create a substantial repayment hardship down the road for borrowers. To their credit, several lenders—including BB&T, a regional banking company based in North Carolina—refused to issue such profitable loans on ethical grounds, a high road not taken by most in the industry (Parnell & Dent, in press).

Finally, it can be argued that companies have a philanthropic responsibility: the obligation to be a good corporate citizen. Some seek to fulfill this responsibility by contributing time and money to the communities in which they operate. Many businesses make financial contributions to school systems as well as colleges and universities. Others encourage their employees to volunteer in their communities and will often compensate these employees for their time invested in a civic cause.

Carroll and Buchholtz (2003) maintain that three CSR components—economic, legal, and ethical—are also the most closely tied in with business ethics. Considering organizational crises, it is clear that many are comprised of one or more of these components. In Table 10.2 we provide examples based on the assumption that business ethics crises are motivated by a desire to gain financially at the expense of another stakeholder. For example, at the heart of the economic component is the need to make a profit for the business. But doing so without regard to morality can result in breaking the law (the legal component) or taking part in questionable ethical practices (the ethical component), both of which can result in an organizational crisis.

Business Ethics and the Crisis Management Framework

Many of the ethically oriented crises that are discussed in this section are examples of what have been labeled "smoldering crises." The Institute for Crisis Management (ICM) notes that these crises start out small and can be fixed early on, but instead are allowed to fester until they become full-blown crises and known to the public (Institute for Crisis Management, 2007). What makes some smoldering crises ethically induced is that they do not have to occur in the first place. If such a crisis does occur, it can be mitigated through ethical decision making, although not all executives will proceed in that manner. Instead, some escalate the crisis by making additional unethical decisions, until the crisis spins out of control.

The Beech-Nut apple juice case (see Chapter 6) illustrates a smoldering crisis that should have been stopped early on. During the late 1970s, Beech-Nut Nutrition Corporation found out that it was the victim of a scam when it discovered its apple juice concentrate supplier was providing bogus apple juice. This discovery was especially troublesome because Beech-Nut advertised its apple juice as "100% fruit juice, no sugar added," a claim that was, in fact, not true, given the fraudulent supplier. At that point, Beech-Nut could have reported the incident, pleaded ignorance, and most likely escaped any prosecution since it was an innocent victim ("Bad Apples," 1989; Hartley, 1993). However, this particular supplier was providing its product at 25 percent below the market

TABLE 10.2 Ethical Crises Components

The Basis for an Ethical Crisis	*Ethical Crisis Component*	*Examples of Crises* *Note*: Some of these company crises events may not be familiar to you. These will be examined in more detail in the chapter exercise.
Economic: The basic motive is a desire to gain financially, sometimes at the expense of another stakeholder.	**Legal**: These cases involve behavior on the part of company employees that violates the law.	Company misrepresents its accounting statements by hiding debt or overstating profits. Examples: Adelphia Communications Corporation (2002); Enron (2002); HealthSouth (2002); Qwest Communications International (2005) Company knowingly sells a defective product. Examples: the A. H. Robins Dalkon Shield (1984); Dow Corning silicone breast implants (1992) Company falsely advertises its product. Example: Beech-Nut apple juice (1982) Company violates safety standards in the workplace. Examples: BP Texas City Explosion (2005); Film Recovery Services, Inc. (1985); Warner-Lambert Company (1976)
	Ethical: These cases involve behavior on the part of company employees that is questionable, but does not necessarily violate the law.	Company sells a product that is legal but not necessarily beneficial to society. Examples: PowerMaster Beer (1991); the tobacco industry; Nestlé Infant Formula (1970s) Company is aware of safety changes it could make to its product, but decides to not to do so because of cost factors. Examples: Ford Pinto (1970s); GM Corvair (1960s) Company uses questionable means to obtain phone information. Example: HP (2006) Company compensates auto shop managers based on sales commission, resulting in higher customer bills for repairs not necessarily needed. Example: Sears Auto Centers (1992)

Sources: Carroll A., & Buchholtz, A. (2003). *Business & Society: Ethics and Stakeholder Management* (5th ed.). Cincinnati, OH: Thompson South-Western; Coombs, W. (2006). *Code Red in the Boardroom: Crisis Management as Organizational DNA*. Westport, CT: Praeger; Coombs, W. (2007). *Ongoing Crisis Communication: Planning, Managing, and Responding* (2nd ed.). Thousand Oaks, CA: Sage; Hartley, R. (1993). *Business Ethics: Violations of the Public Trust*. New York: John Wiley; Sethi, S., & Steidlmeier, P. (1997). *Up Against the Corporate Wall: Cases in Business and Society* (6th ed). Upper Saddle River, NJ: Prentice Hall.

rate, and the cost savings was too attractive for Beech-Nut executives to pass up. The incident escalated to a smoldering crisis where Beech-Nut top executives concocted an elaborate coverup scheme and continued using the supplier. From 1977 to 1983, Beech-Nut sold its juice as 100% pure when, in fact, it was nothing more than a "100% fraudulent chemical cocktail," according to an

TABLE 10.3 Crisis Management Framework

	Landscape Survey	Strategic Planning	Crisis Management	Organizational Learning
The Internal Landscape	❑ The ethical environment and the board of directors ❑ The safety policies of the organization ❑ The extent of greed present among top executives and management	❑ The enthusiasm for crisis management planning and training ❑ The focus on the prevention of ethical breaches	❑ The management of internal stakeholders ○ Owners ○ Employees **Crisis**	❑ The evaluation of the ethical management process ❑ The commitment to organizational learning
The External Landscape	❑ The degree of industry vulnerability ❑ The vulnerability of the organization in the global environment	❑ The fulfillment of existing government regulations ❑ The fulfillment of current industry standards	❑ The management of external stakeholders ○ Customers ○ Suppliers ○ Government parties ○ Local community	❑ The benefits of industry renewal ❑ The inevitability of new government regulations ❑ The anticipation of new stakeholder outlooks

investigator close to the case (Welles, 1988, p. 124). What should have been a decision to change suppliers became an ethical misconduct crisis. Beech-Nut president Neils Hoyvald, and John Lavery, vice president for operations, were the main parties who instigated the coverup. When the crisis was finally over, both men were found guilty of violating federal food and drug laws. Hartley (1993) estimates the crisis that never should have happened cost Beech-Nut $25 million in fines, legal costs, and lost sales.

Table 10.3 depicts the crisis management framework in relation to business ethics issues. The next sections develop the four areas of the crisis management process.

Landscape Survey: Uncovering the Ethical Boulders

The landscape survey looks for clues in the organization's internal and external environments that may indicate the presence of an unethical event brewing. Potential crisis indicators include the ethical environment of the Board of Directors, the safety policies of the organization, the economic motives among top executives and management, the degree of industry vulnerability, and the vulnerability of the organization in the global environment. These indicators are discussed next.

The Ethical Environment and the Board of Directors

The ethical environment of the organization is an indicator of the potential for a future crisis. The founder of the company holds a considerable amount of influence in forming this ethical environment. For example, Enron, WorldCom, Adelphia, HealthSouth, and Tyco have all faced ethical scandals. What these firms had in common was that their founders, all hardworking entrepreneurs, were at the helm when the crises hit (Colvin, 2003). Furthermore, those in charge of these companies had at least three characteristics in common that led to the scandals. First, these companies had not learned to question the founder/CEO when necessary. Rather, their CEOs were powerful individuals who seemed to answer to no one. Second, the characteristic of greed was apparent at the top levels of these companies. It was as if an entitlement mentality prevailed, with those running the company receiving extraordinary amounts of compensation because they felt they deserved it. Finally, all of these companies had leaders who seemed to focus on short-term gains through increasing stock price, without regard to the sustainability of the company. The link between CEO compensation and stock price is an underlying factor in many of the scandals that hit these big corporations (Colvin, 2003).

This factor presents the corporation with a dilemma. On one hand, CEO compensation should be linked to firm performance; on the other hand, this linkage can be abused in favor of short-term performance versus long-term survival and growth. In response to this quandary, some firms have favored the balanced scorecard approach (Kaplan & Norton, 2001), an approach that has pushed the practice of accounting to track long-term as well as short-term performance results. Thousands of companies have now adopted this approach in the United States and abroad (Parnell & Jusoh, 2008; Post et al., 2002).

More scrutiny of corporate boards has also occurred, with boards facing more accountability and disclosure mandates (Thorne, Ferrell, & Ferrell, 2003). The situation at WorldCom is an example of a board that continually gave in to the desires of then-CEO Bernard Ebbers: "As CEO, Ebbers was allowed nearly imperial reign over the affairs of the company with little influence from the board of directors, even though he did not appear to possess the experience or training to be qualified for his position" (Breeden, 2003, p. 1). Two areas of questionable freedom were requested by Ebbers and approved by the board. The first involved the approval of the collection of $400 million in loans, and the second a rubber-stamping of his request to compensate favored executives to the tune of $238 million. The arrangement was made without standards or supervision and allowed Ebbers to compensate whomever he wanted and in whatever amount he wished (Breeden, 2003). Ultimately, these schemes, along with others, culminated in a crisis that resulted in the largest accounting fraud case in the United States.

Crisis cases like WorldCom illustrate why boards have to be more than just a rubber stamp for the CEO. In response, some boards are taking a more aggressive approach to holding the CEO accountable for ethical behavior. Case in point: Boeing's former CEO, Harry Stonecipher, lost his job after it was revealed he was having an affair with another Boeing executive (Benjamin, Lim, & Streisand, 2005). The relationship violated company policy. Ironically, Stonecipher, who agreed to come out of retirement to serve as CEO, was brought in to lead the scandal-ridden company out of its ethical quagmires (Levenson, 2005).

The Safety Policies of the Organization

Safety policies, or the lack of them, have a direct link to the ethical climate of the organization. Ultimately, the adherence to such policies can determine whether or not a major crisis occurs. An ethical stance on the part of management promotes an environment where all stakeholders (particularly employees) are safe from bodily and emotional harm. However, as every manager and top executive knows, safety costs money and can detract from the bottom line in the short run. In the long run, though, these expenditures can save the company millions and maybe even the company itself.

In looking back at industrial accidents, organizational researchers have never reached a conclusion that indicated too much money was spent on safety (Crandall & Crandall, 2002). Executives who have experienced a safety issue such as an industrial accident resulting in injuries or deaths probably wish they had spent more on safety. For example, in the 1983 Bhopal, India gas leak incident, Union Carbide and local government officials in India should have focused more on correcting safety problems that had already been widely documented at the plant prior to the accident (Sethi & Steidlmeier, 1997; Steiner & Steiner, 2000).

Safety measures involve short-term expenses but usually produce long-term savings by avoiding accidents. Hence, safety remedies need not always be viewed as "expensive." Money spent to prevent employee injury and death is not money wasted; it may well save the company millions in lawsuits, as well as the company's reputation, not to mention human lives. The Hawks Nest Tunnel contractor, Rinehart and Dennis, could have implemented at least three relatively low-cost measures to make working conditions safer and thereby prevent their workers from developing silicosis: better ventilation of the tunnel shaft, wet drilling, and providing respirators for workers. While it is difficult to determine the exact cost of these measures, it is clear that such measures might have saved many lives as well as the downfall the company experienced within 5 years of completing the tunnel.

The Economic Motives Among Top Executives and Management

Economic motives are often linked to unethical and illegal behaviors. As Table 10.2 indicates, the economic motive can be pushed to the point of greed becoming part of the process. The reason for this is actually easy to see. Management competence is measured by key performance indicators such as sales, profits, and market share, which can ultimately drive the price of the company's stock. Boards of directors typically reward the CEO when stock valuations increase, because this represents an increase in wealth for the shareholders. At first, this sounds like a win-win situation, but as many recent business crises indicate, abuses can occur that ultimately are not in the best interest of the corporation or its stakeholders. Two such abuses are hiding debt and counterproductive cost cutting.

Hiding debt creates the illusion that the firm is performing better than it actually is, which encourages a false sense of optimism and confidence in the stock. The result is that stock prices rise in the short term, and shareholder values increase. The CEO is also rewarded, because "on paper" the firm is doing well. This whole process is motivated by an attempt at excessive financial gain at the expense of other stakeholders. In the short run, this unethical strategy can actually produce financial benefits for the CEO and the shareholders. In the long run, however, it is a prescription for a major crisis. Enron will remain the poster child for this abuse as the company spiraled downward after its elaborate schemes for hiding debt became known. Technically, the mechanism for hiding its debt, a provision called special-purpose entities (SPEs), was legal, but such SPEs have trigger mechanisms that require repayment of the debt under certain circumstances (Henry, Timmons, Rosenbush, & Arndt, 2002). It was these trigger mechanisms that began the "visible" crisis at Enron even though the invisible part of the crisis, the part not known to stakeholders, actually took place well before, when the SPEs were originally developed.

Counterproductive cost cutting is the other abuse that can arise from unethical motives. Such cost cutting is actually the profit motive at work, and will cause some managers to do just about anything. Cutting costs delivers dollars to the bottom line, but doing so without regard for worker safety has resulted in many examples of industrial tragedies. In 1976, when Warner-Lambert was introducing a new line of chewing gum, it took shortcuts in the manufacturing area by allowing high levels of dust near the machinery. The company could have installed a dust collection system, a move that would have reduced dust levels significantly. The cost was seen as prohibitive, however, so the opportunity to buy the system was ignored. The result was a dust explosion that killed six employees and injured 54 others (Sethi & Steidlmeier, 1997).

Although cost cutting is a normal and necessary business activity, it was the major factor in the many deaths that resulted from building the Hawks Nest Tunnel. The use of dry drilling to expedite the project time was discussed earlier. Shortening the project time reduces expenses and increases the bottom line. The decision not to provide tunnel workers with respirators is especially troubling. The only explanation for this seems to be the additional cost that would have been incurred.

The Hawks Nest incident illustrates the connection between ethical decision making—doing what is just and fair for employees—and protecting worker safety. Perhaps the most famous abuse of worker safety in the United States was the 1911 Triangle Shirtwaist Company fire that occurred on the 10th floor of a factory in New York City. The fire spread rapidly due to the large amounts of linen and other combustible materials close by. One hundred forty-six employees died, most of them immigrant women, who were either burned in the blaze or jumped to their deaths. Sadly, the fire escape routes for these employees had been locked by management in order to prevent theft (Greer, 2001; Vernon, 1998). Some may argue that revisiting cases like Hawks Nest and the Triangle Shirtwaist fire is not necessary today. After all, labor unions, labor laws, safety inspectors, and various watchdog groups discourage this kind of behavior (Shanker, 1992). Unfortunately, history has a way of repeating itself.

On September 3, 1991, a fire erupted at the Imperial Food Products poultry plant in Hamlet, North Carolina. Before the day was over, 25 employees, most of them single mothers, would perish. "The plant had no sprinkler or fire alarm system, and workers who got to the unmarked fire exits found some of them locked from the outside. Imperial's management was using the same 'loss control' technique as the bosses at Triangle—and with the same results" (Shanker, 1992, p. 27). An $800,000 labor code fine was levied against the company. Fourteen months after the fire, a $16 million settlement was reached between the insurers and the claimants. Plant owner Emmet Roe was sentenced to 20 years in prison after pleading guilty to manslaughter (Jefferson, 1993). Eventually, Imperial went bankrupt. As these examples illustrate, unchecked greed comes in various forms and can hurt other stakeholders in the process.

The Degree of Industry Vulnerability

Certain industries are more vulnerable to crisis events. The airline industry remains the most crisis prone, according to the Institute for Crisis Management (ICM). This is due to the potential for terrorist attacks and aviation accidents, which are risk factors when operating in that industry. However, a crisis-prone industry does not mean that unethical decision making prevails. Some industries are just more susceptible to accidents, such as natural gas and petroleum refining, which ranked fifth and sixth, respectively in the top crisis-prone industries (Institute for Crisis Management, 2007).

Looking through the lens of ethical rationality (Snyder, Hall, Robertson, Jasinski, & Miller, 2006), the challenge is to determine if an industry is more vulnerable to a crisis because of a higher degree of unethical occurrences. The link between industry-specific factors and unethical behaviors has not been as widely addressed, although some attention has been focused on aircraft manufacturers. Both Lockheed and Northrop were found to have made improper cash payments to overseas sales agents in the 1970s in order to secure contracts to sell aircraft (Securities and Exchange Commission, 1976). More recently, Boeing has been plagued by a number of ethical problems, perpetuated by what has been called a "culture of silence" by Boeing general counsel Douglas Bain. The culture stems from a lack of speaking up on ethical issues, a problem that has plagued the company for a considerable amount of time (Holmes, 2006).

The Vulnerability of the Organization in the Global Environment

As a firm expands its international presence, its vulnerability to crisis may also increase. There is a greater potential for an ethical breach to occur as well. Three reasons for potential ethical problems include the temptation to make illegal cash payments, the possibility that a foreign contractor will supply a defective product, and the potential to be linked with sweatshop manufacturing.

The Temptation to Make Illegal Cash Payments

Major scandals often result in new legislation. As a result of the Lockheed bribery scandal, the Foreign Corrupt Practices Act was passed in 1977 (Hartley, 1993). The act prohibits offering cash payments to foreign government officials for the purpose of obtaining business (Carroll & Buchholtz, 2003). Critics often complain, however, that the act places American firms at a disadvantage when competing for foreign contracts where legal infrastructure requiring that all companies play by the same rules does not exist. In many parts of the world, offering bribes is an accepted way to conduct business. To further complicate the matter, the act does allow some cash payments, called grease payments—smaller amounts of cash used to encourage foreign officials to do what they are supposed to do anyway (Carrol & Buchholtz, 2003). A bribe, on the other hand, is a large cash payment used to entice a foreign official or agent to do something not normally done in the course of business, such as buying from a particular vendor.

As companies expand globally, the temptation to use illegal cash payments such as bribes increases. Recent enforcement by the U.S. Securities and Exchange Commission (SEC) and the U.S. Department of Justice (DOJ) indicates that the act is being violated to some degree. The year 2006 was a busy year for its enforcement, with charges leveled at four high-profile companies and a number of individuals. The DOJ promises that future enforcement of the Foreign Corrupt Practices Act will be carried out with "increased vigilance" (Warin, Blume, Bell, & McConkie, 2007, p. 2).

The Possibility That a Foreign Contractor Will Supply a Defective Product

Defective products originate from foreign contractors just like they do from domestic companies. However, the perception of citizens in the home country may be that the foreign contractor has acted unethically in some way, possibly by cutting corners in the manufacturing process. Furthermore, if jobs have been lost due to outsourcing, the home company is likely to experience a public relations problem.

The Potential of Being Linked With Sweatshop Manufacturing

Companies that outsource processes to overseas vendors may face potential association with sweatshops. This crisis can lead critics of outsourcing to be diligent in identifying companies that are using sweatshops for the manufacturing of their products. Sweatshops are manufacturing facilities that pay low wages, employ child labor, have poor working conditions, require long work hours, and use abusive supervision of workers. Their use has increased as companies seek to lower costs (Carroll & Buccholtz, 2003). Their use can also cause companies to be hit with a public relations crisis. Wal-Mart, Nike, Liz Claiborne, Disney, and McDonald's are large, high-profile companies that have been linked with sweatshops in the past (Post et al., 2002).

Sweatshops are the ultimate "guilt by association" crisis. Although some progress has been made in recent years to improve working conditions in developing countries, the issue will not go away anytime soon. Although a company can "require" its subcontractors to abide by certain working condition standards, the enforcement of these standards can be difficult. Typically, independent monitors are sent to investigate working conditions in plants that are supposed to be compliant with certain standards. Even companies with reputations for good ethics face such problems. The 2007 discovery tracing some of the clothing sold in Gap stores to sweatshops in India where children as young as 10 years of age work 16 hours a day is one such example (Hansen & Harkin, 2008).

Strategic Planning: Confronting the Ethical Boulders

The strategic planning process can generate efforts to improve the ethical climate of the organization. Improving this climate can reduce the company's vulnerability to an ethics-related crisis. Specific efforts should be directed to generating enthusiasm for crisis management and training, focusing on the prevention of ethical breaches, and abiding by both government regulations and industry standards.

The Enthusiasm for Crisis Management and Training

Neglecting to prepare for a crisis is in itself an ethical problem. Unfortunate events can eventually happen to an organization, and having a plan to meet these crises is expected by the company's stakeholders. The lack of a crisis management plan and the subsequent training that goes with it will only draw negative perceptions from employees, suppliers, customers, government agencies, and the general public when a crisis does occur.

Simply forming a crisis management team and generating a crisis plan is not sufficient. Enthusiasm for the crisis management process and the accompanying training must also be present. For this reason, the organization should seek a crisis management champion from within who will spearhead the process toward an ongoing crisis management program. If the organization is new to crisis planning, an outside consultant should also be retained to assist the crisis management team in writing its first plan.

The Focus on the Prevention of Ethics Breaches

The best approach to dealing with an ethical crisis is to prevent it from happening in the first place. An ethical rationality approach seeks to address events in the life of the organization from a morally driven response perspective (Snyder et al., 2006). However, to a great extent the organizational culture dictates how ethical or unethical decision making will be in the company (Heineman, 2007; Vallario, 2007). For this reason, a cultural change in the organization is also necessary to improve ethical decision making.

Changing the culture of an organization is a large undertaking; culture is, after all, the prevailing belief system within the organization. Some cultures simply look the other way when an ethical breach occurs, whereas others are committed to ethical standards in any business decision. All cultures look to

TABLE 10.4 Measures Organizations Take to Change Their Ethical Culture

Measure Taken	*Description*
Code of ethics	Organization-wide ethical principles and behaviors are outlined in a pamphlet or manual. Managers and employees review the code on a regular basis and sign it, indicating their willingness to abide by the code.
Ethics training	Short classes and workshops that highlight ethical issues and how to respond to them are offered to employees.
Ethics hotline	Employees have a person or department they can report ethical violations to within their organization. A hotline can also offer guidance on specific ethical issues that an employee may be facing.
Top management sets the example	Executives in top positions in the company—the CEO, president, and vice presidents—need to realize that lower-level managers get their cues on ethical matters by watching those higher up. Thus, top managers are encouraged to set the right example.
Realistic goal setting	Goals set for managers are well conceived and realistic. Unrealistic goals encourage unethical decision making since managers feel they must cut corners to attain the goal.
Discipline for ethical violations	When an ethical violation is discovered, the company works quickly to correct the situation and punish the person responsible.
Ethics audits	As in a financial audit, the company periodically checks itself in a systematic manner to see if it is following proper ethical guidelines in its business processes.

Sources: Carroll, A., & Buchholtz, A. (2003). *Business & Society: Ethics and Stakeholder Management* (5th ed.). Cincinnati, OH: Thompson South-Western; Post, J., Lawrence, A., & Weber, J. (2002). *Business and Society: Corporate Strategy, Public Policy, Ethics*. New York: McGraw-Hill Irwin.

upper-level management for cues to right and wrong behavior in the organization (Trevino, Hartman, & Brown, 2000). Table 10.4 overviews other measures companies take to change their ethical cultures.

Abiding by Existing Government Regulations

Government regulations exist to protect employees, consumers, and the local community. Unfortunately, such regulations can sometimes be sidestepped by businesses, which can lead to catastrophic outcomes in the future. It is an ethical decision to abide by government regulations. The converse of this statement is also true: Ignoring regulations is also a decision, one that is conscious and deliberate. Many organizations find themselves in trouble with government regulations because of unethical/illegal decisions made by management or other key employees.

In 1997, the Andrew & Williamson Sales Company sold strawberries grown in Mexico to the U.S. Department of Agriculture (USDA). There was one problem with the deal. The USDA distributes food to public schools, and government regulations require that strawberries sold to school systems be grown in the United States. As part of a coverup, the San Diego–based firm submitted falsified certificates of origin that indicated the strawberries were grown domestically (Salkin, 1997). While the company thought its deed would go unnoticed, a major crisis soon erupted. A number of public school students in Michigan were stricken with hepatitis A, and the ailment was linked to the strawberries sold by Andrew & Williamson. Eventually outbreaks of the hepatitis A strain originating from the strawberries resulted in 213 cases in Michigan, 29 in Maine, and 7 in Wisconsin (Entis, 2007). What started out as an illegal scheme to move excess inventory out of the warehouse culminated in a major crisis across a number of states. When the ordeal ended, Frederick Williamson resigned as president and was sentenced to 5 months in prison, followed by 5 months of home detention. The company was also forced to pay $1.3 million in civil damages, as well as $200,000 in criminal penalties (Entis, 2007).

In the Hawks Nest incident, existing regulations were ignored in certain circumstances. For example, standard operating procedures required that wet drilling be utilized to keep dust levels to a minimum (Cherniak, 1986; Tyler, 1975). Testimony before the U.S. Congress revealed that employees were posted to watch for incoming mine inspectors (Comstock, 1973). With these arrivals "announced," wet drilling would begin until the inspectors had left the area, when dry drilling would resume to speed up the extraction process. Such sidestepping of regulations would provide short-term relief for the contractor, but in the long run it would come back to haunt them.

Abiding by Current Industry Standards

Industry standards are often set by associations for their members to follow. The intent is to set guidelines concerning a particular item, such as quality or safety, that can be viewed by member companies as a minimally acceptable standard (Vernon, 1998). Such efforts have also been referred to as self-policing (Becker, 2006) or self-regulation (Hemphill, 2006). Certain professions also have standards for their members; these professions include physicians, attorneys, college and university professors, engineers, pharmacists, and accountants.

Guidelines for ethical conduct can be proposed by industry associations. In 2001, an industry group of 14 Wall Street firms established ethical conduct standards governing compensation and stock ownership for analysts. This move was prompted by some of the industry leaders, including Goldman Sachs, Merrill Lynch, and Morgan Stanley Dean Witter, to address emerging ethical problems (Carroll & Buchholtz, 2003). In another example, Financial Executives International (FEI) requires all of its members to review and sign a code of ethics. They also recommend that the financial executive deliver the signed copy to the company board of directors. FEI has become a model for companies seeking to comply with Sarbanes-Oxley and New York Stock Exchange mandates (Vallario, 2007).

Several caveats should be offered concerning industry standards. First, requiring that member companies have a code of ethics is a step in the right direction, but it does not ensure all companies will have leaders who always make ethical decisions. Even Enron had a 62-page code of ethical conduct;

unfortunately, it was not an ingrained part of the Enron culture (Becker, 2006). Second, larger companies within associations attract more attention than smaller ones and thus are easier targets for critics. Case in point: A Google search on the company names Wal-Mart or Starbucks will inevitably reveal Web sites that are critical of these companies. Some of these sites even trump up false claims about the companies. Why? Large, successful companies are also seen as vulnerable targets by issue-oriented groups.

Crisis Management: Further Considerations During an Ethical Crisis

A crisis should be managed in an ethical manner. "Decision-makers who understand the needs of a wide range of stakeholders as part of their strategic decision-making will make more ethical decisions during a time of crisis" (Snyder et al., 2006, p. 376). Thus, ethical rationality is a habit that must be ingrained in the culture and daily operations of the organization (Fritzsche, 2005). This ethical rationality involves the careful management of the organization's internal and external stakeholders throughout the duration of the crisis.

The Management of Internal Stakeholders

Employees and owners are the internal stakeholders that must be managed with ethical integrity when a crisis occurs. Typically, it is the crisis communication function that must be approached in an honest, straightforward manner. Employees are often the forgotten stakeholder in the ordeal. It is important they receive truthful and expedient information updates as the crisis progresses.

On the other hand, the owners may suffer a direct consequence from a crisis in the form of financial loss. If the shareholders are geographically dispersed, the impact of the loss may not be felt until quarterly reports are distributed months after the crisis commences. If the company is a corporation with many stockholders, then they, too, like the employees, may be left in the dark on the details of the crisis at hand. This is not an ethical approach to informing these groups.

The organization's Web site is a strategic tool that can be used to communicate with these stakeholders. Updates on the state of the crisis should be made on a regular basis. Chapter 8 addressed the importance of maintaining a special "dark site," a link used to answer frequently asked questions (FAQs) on the nature of the crisis (Snellen, 2003). Both employees and stockholders should have ready access to these sites. In addition, the organization should use its managers and supervisors to communicate the details of the crisis to employees. To supplement this type of communication, an organization-wide memo or letter should be circulated to all employees. This is an excellent way to clarify misunderstandings or rumors that may be circulating about the crisis.

The Management of External Stakeholders

External stakeholders include customers, suppliers, the local community, the media, and affected government agencies. As with internal stakeholders, the ethical approach is to make sure that communication to these groups is honest and timely. For example, if the crisis is an untrue rumor, it should be addressed quickly and stated that it is untrue (Coombs, 2007; Gross, 1990). Again, the organization's Web site can be an excellent vehicle for updated information on the latest developments of the crisis.

Organizational Learning: Lessons From the Ethical Crisis

Lessons learned from an ethical crisis tend to be somber. Recovering from these types of crisis requires a commitment to pursue better behavior in the future. But not all individuals involved will take responsibility for their actions, and some of them will pay for their actions with prison time. Collectively, the organization must also speak with one voice and make it plain that it proposes to remedy the problems that led to the ethical incident to begin with, and to continue with aboveboard behavior in the future.

Evaluating the Ethical Management Process

Organizations guilty of a moral lapse are usually caught in the process. Unlike a crisis where the organization is an obvious victim (e.g., earthquake, torrential weather, or some other act of nature), an ethical crisis generates little public sympathy. Furthermore, sentiments often run against the company, even if it is not to blame for the actual crisis. For example, if damaging weather hits a company warehouse and knocks out its storage and operations, some critics will still question why the company was not more prepared.

Ethical decision making will anticipate not only how to handle the crisis, but what to do about the organization's critics. This is why Bertrand and Lajtha (2002) noted that every crisis can be interpreted as a sign of a loss of trust. In this example, stakeholders lose trust in the organization when something bad happens, whether or not it was caused by the organization. This is not a pretty scenario, but it is real. To witness this phenomenon, simply watch the comments section of any major online news Web site. Critics frequently emerge to blame just about anyone for a given calamity. When a company is in the midst of a crisis, it will often be perceived by others as blameworthy, even if it did not cause the crisis at hand.

As the company seeks to learn from the crisis they have just experienced, management should acknowledge the various viewpoints that exist. For some, there exists a strong anticorporate mindset. Such critics often feel they are the ethical standard-bearers and thus represent the collective consciousness of society. As a result, company management needs to communicate that it is doing everything it can to learn from each crisis, and to learn how to become better at making ethical decisions in the marketplace.

The Commitment to Organizational Learning

Chapter 9 focused on the process of organizational learning after a crisis. Crises involving ethical breaches should not be repeated. Once an ethical crisis has been resolved, the organization must commit itself to a learning process that seeks to avoid repeating the mistake. Unfortunately, crisis management history teaches us that some companies resort to a "defense-and-attack" mode (Nathan, 2000, p. 3), a tactic that in itself is unethical. The A. H. Robins company used this tactic to discredit the victims who used the Dalkon Shield, a contraceptive device that was surgically inserted into the uterus. When recipients of the Shield became sick, the company resorted to attacking the victims and questioning their sexual practices and partners (Barton, 2001; Hartley, 1993). This is no way to fight a crisis, and A. H. Robins paid dearly in the end by enduring an endless onslaught of consumer lawsuits.

What is expected by both internal and external stakeholders is a commitment by the company to "get it right" by abiding by the law and staying within ethical guidelines. This learning process may involve a number of measures, including getting rid of the executives and managers who caused the problem in the first place. New controls may need to be implemented as well.

The Benefits of Industry Renewal

Some industries seem to have more problems with ethical matters than others. This may sound odd, given that people, not an industry, commit the unethical acts. But some industries have had more "experience" in this area than others. The tobacco industry certainly falls in this category. Many question the ethics of selling a product that causes serious health problems. The industry maintained for many years that cigarettes were not harmful, even though illnesses from tobacco represented a heavy burden on the health care system. In 1998, however, 46 state attorney generals reached an agreement with the five largest tobacco manufacturers in the United States. The settlement required the companies to pay billions of dollars to the state governments each year to alleviate the burden on the state health care systems (Thorne et al., 2003). In terms of industry renewal, there has been a decline in advertising aimed at youth and teenagers, a problem that existed during the Joe Camel advertising days.

The catalyst for industry renewal in the tobacco industry was ultimately a push from state governments. Some industries try to change their ethical problems before the government has a chance to intervene. Marketing practices within the pharmaceutical industry represent one example of an industry establishing its own reforms. Prior to these reforms, gifts and other incentives were frequently lavished on physicians by representatives advocating the use of their company's drugs (Hemphill, 2006). The intent was to influence prescribing behavior, which in itself was not unethical, but the means to achieve this goal was of growing concern. In response, the American Medical Association (AMA) adopted ethical guidelines in 1990 on gift-giving practices. The initial responses were positive but, as Hemphill (2006) notes, a reappraisal of pharmaceutical marketing codes of conduct needs to be performed.

The Inevitability of New Government Regulations

After a major crisis, the government may step in to impose new regulations. This is especially true if the company is large and efforts at self-policing have not been effective. Self-policing refers to efforts on the part of an industry association to get its member organizations to abide by a certain set of standards. The intent of self-policing is to generate positive change without government mandates (Becker, 2006). Nonetheless, when self-policing is not successful, government regulations often follow. Hartley (1993) has noted a general progression from public apathy, to media attention, to public outcry, and finally to government regulation. Table 10.5 overviews this progression.

Today, we see numerous examples of how the government seeks to protect society through regulation. The Environmental Protection Act resulted from public outcry against the pollution crises. The Occupational Safety and Health Administration was a government response to safety inadequacies in the workplace. Sarbanes-Oxley legislation in 2002 was a government effort to improve financial accountability in corporations. Although the effectiveness of such government interventions can be debated, their links to previous crises is clear.

Anticipating New Stakeholder Outlooks

There is a sad irony in the realm of organizational crises events: A significant loss of human life often launches a company into immortality. Unfortunately, this is a stakeholder memory that is hard to erase. For many people from the baby boomer generation, just mentioning the word "Bhopal" immediately brings to mind Union Carbide, the company behind the accidental gas leak that killed thousands in India in 1983. Indeed, Googling "Union Carbide" produces many references to this disaster. The name and incident association is strong. Likewise, Hawks Nest Tunnel contractor Rinehart and Dennis will not be remembered for its previous successful engineering projects; instead, its name will forever be associated with the needless loss of hundreds of workers who died from silicosis.

There is an added irony to the Hawks Nest crisis. The company receiving the electricity that was produced by the tunnel project was Union Carbide. There has been some speculation as to how active Union Carbide was in the tunnel crisis. Some critics have assumed guilt by association, while others claim the company was not involved in promoting unsafe working conditions for the tunnel workers (Deitz, 1990; Jennings, 1997). Nonetheless, name recognition has a strong emotional component; it is associated with good products and services, but can also be associated with death.

There are other stakeholder outlooks that can result from crisis events. Consider the following crisis events and how they changed the viewpoints of many:

- The September 11 terrorist attacks forced air travelers to accept new forms of security that were previously not utilized. They have also created the mindset that the ethical thing for companies to pursue is the safety and welfare of their customers. In the past this viewpoint was implied, but today more and more is expected from companies in safeguarding their people.

TABLE 10.5 The Progression From Crisis to Government Regulation

	Public Apathy →	Media Attention →	Public Resentment and Outcry →	Imposition of Government Regulations
General Description	The general public is not too concerned about potential crises. Likewise, the company is not proactive in diffusing any potential crises.	The media focuses on a crisis event and brings it to the attention of the general public.	The general public reacts to the crisis by asserting that "something must be done" to correct the situation and keep it from reoccurring.	The government will wait for an appropriate period of time in hopes the company or industry will self-regulate. Government regulations will follow if self-regulation does not occur.
Example: The Hawks Nest crisis	The Great Depression was at its height and most people just wanted to work.	In the late 1930s, media attention highlights the abuses of workers who are now dying of silicosis.	Public sympathy is slow at first, but eventually builds momentum to the point that lawsuits and government investigations ensue.	Silicosis legislation is passed in 46 states.[1]
Example: GM's Corvair crisis	Cars were cool. The Corvair was a desirable low-cost sports car for the cost-conscious public.	Reports surface that the Corvair will roll over under certain steering conditions. Ralph Nader's book *Unsafe at Any Speed,* an exposé of the Corvair and GM, gains widespread attention.[2]	The public rallies for safer cars. In time, other safety issues arise with other vehicles, such as the Ford Pinto.	Today, the automobile is the most regulated consumer product in the United States. Focus areas include pollution emissions, fuel economy, and safety provisions.
Example: September 11, 2001 terrorist attacks	Although terrorist threats at airline targets were recognized by the government, passengers, and airlines, few anticipated that a jet airliner would be used as a terrorist weapon.	The attacks on the World Trade Center and the Pentagon are known immediately throughout the world. The Internet makes this news event unfold in real time and with an abundance of visual images.	Airlines' sales drop dramatically after the attacks. All airlines experience financial shocks and some eventually go into bankruptcy.	The government responds with the creation of the U.S. Department of Homeland Security and the Transportation Safety Administration (TSA).

Source: Adapted from Hartley, R. (1993). *Business Ethics: Violations of the Public Trust.* New York: John Wiley & Sons, pg. 26.

Notes: 1. Cherniak (1986); 2. Hartley (1993).

- As the manufacturing of goods is outsourced to overseas vendors, there is a feeling among many that firms are losing direct contact with the means of production (Bertrand & Lajtha, 2002). This anxiety rises when products shipped to the domestic country are flawed in some way, such as toys with lead paint. The question of ethics arises when those who have lost their jobs to outsourcing end up purchasing products—some of them defective—from other countries.
- Recent weather patterns suggest that global warming has occurred in recent years. Some scientists link global temperatures to human activity, namely the production of carbon emissions. The ethical viewpoint held by many is to reduce emissions into the atmosphere because this may be an issue of long-term survival.
- Hurricane Katrina and the ineffective government response prompted wide criticism. Many cite the poor communication and coordination among government agencies, which should have been trained to manage these types of problems. The ego and turf wars that existed among city, state, and federal branches of the government were also obvious and invited the scorn of many who felt let down when elected officials did not work in the best public interest.

Summary

Bertrand and Lajtha (2002) have concluded that all crises can be interpreted as signs of a loss of trust. If this statement is true, then the ethical repercussions are enormous. What this means is that no matter what the crisis is, some stakeholder(s) will feel a loss of trust in the organization.

Consider these common examples where the party obviously at fault is not included in the blame equation, and yet blame, or at least some sense of responsibility, is deflected back onto the organization. The countering questions that follow each event are often raised by the media, or can even be seen on blogs when similar events occur.

- A recently fired employee walks into his former place of work and kills his supervisor along with several other employees: Why was the employee allowed back on the premises? What did the company do to make this employee so agitated?
- An employee is killed on his factory job because he did not follow standard procedures in doing his job, thus leading to the fatal accident: Why did the company hire this person in the first place? How many similar accidents have occurred at this workplace? Why did the company not enforce its own procedures?

Responses like these are common when a crisis occurs. In an attempt to make sense out of what has happened, many people will cognitively distort the situation and assign an ethical cause to the crisis; in their minds, the cause is often the organization. Bertrand and Lajtha's comment about the loss of trust is based on a perception. Nonetheless, perceptions can influence behavior more than reality. Hence, ethical decision making must be at the forefront of all management actions.

Questions for Discussion

1. Give an example of an ethical problem that has occurred either where you currently work or have worked in the past.
2. Using the crisis management framework, conduct a landscape survey and determine the current status of potential ethical issues in your present organization (internal landscape). In your answer, be sure to address the following: the ethical environment and the board of directors, the safety policies of your organization, the extent of greed among top executives and management. (Note: On this question and the ones that follow, you may substitute a former employer if you like.)
3. Conduct a landscape survey to determine the current status of potential ethical issues in your organization's external environment (external landscape). In your answer, address the degree of industry vulnerability, and the vulnerability of the organization in the global environment.
4. Using the strategic management framework, discuss how prepared your current organization is to address these potential ethical crises (internal landscape). In your answer, address the enthusiasm for crisis management planning and training as well as how focused your company is on the prevention of ethical breaches.
5. What is the current status of your organization in meeting government regulations and industry standards (external landscape)?
6. In terms of crisis management, how well did your company perform in managing its internal stakeholders during a recent crisis? How did it perform in managing the external stakeholders? Were there any ethical problems that were not addressed properly?
7. In terms of organizational learning, how did your company improve in its ethical decision making after the crisis was over (internal landscape)? Were there any changes in the industry or new government regulations that appeared as a result of this crisis (external landscape)?

Chapter Exercise

Table 10.2 lists a number of crisis events that the class may not be familiar with. Select several unfamiliar cases. Outside of class, research each case and write a one-page summary of what happened and the outcome of the case. Discuss these in class. Be sure to address the following topics:

- What crisis did the organization face?
- How did mismanagement contribute to the crisis?
- How was the crisis finally resolved and what legal implications were present (the settlement of lawsuits, etc.)?

MINI CASE

HP—WHERE "UNCOMPROMISING INTEGRITY" AND UNETHICAL BEHAVIOR COLLIDE

Hewlett-Packard (HP) built its reputation on "trust and respect for individuals" and "uncompromising integrity," two statements that are part of the "HP Way" doctrine (Barron, 2007, p. 8). From 2005 to 2006, however, an ethical crisis erupted that tarnished the integrity of the company.

The saga began when it was discovered in the early part of 2005 that a board member had leaked company information to the media. In an effort to find the culprit, an investigation using a private investigation firm was secretly authorized by then–Board Chairwoman Patricia Dunn. Investigators spied on HP employees by digging through their trash and using a practice called pretexting—a means of obtaining private information about a person by assuming a false identity (Ecker, 2006). In the HP investigation, pretexting was used to obtain phone records of journalists who were suspected of communicating with the "leaking" board member, who was later identified as George Keyworth, the longest serving HP board member (Barron, 2007).

One problem had been identified, but a second one was on the horizon. The use of pretexting in this case was deemed to be illegal, according to California Attorney General Bill Lockyer. A lengthy investigation ensued, and when it was over, HP agreed to pay a $14.5 million settlement and to reform its ethical practices (Woellert, 2006). Through it all, the company had to face a mountain of negative publicity and a humiliating crisis.

Diane Swanson, a Kansas State University business professor, sums up the problem well: "What kind of signal does [spying] send to other employees?" (Barron, 2007, p. 10). The carefully crafted HP Way doctrine had been put to the test—and failed.

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