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Chapter 2

Ethical Decision Making

CHAPTER SUMMARY

Ethical decision making in business is often difficult and complex. Some situations are easily handled because what one ought to do or what is right and wrong are evident. Those situations that give us pause or produce moral anguish require careful thought and ultimately an ability to engage in ethical reasoning. This chapter contributes to an understanding of ethical decision making by offering a division of business ethics into two parts: an ethics of the market and an ethics of roles and relationships, including firms. In business, we deal with some parties purely as market actors who are on the other side of a market transaction or exchange. For such market activity, certain moral rules or standards apply. These relationships are governed by professional ethics, a prime example being the legal profession. In addition to the law, an attorney must follow professional codes of ethics established by the state bar and/or professional association he or she belongs to. These codes can impose a greater obligation to act in the best interests of the client. For example, the attorney-client relationship imposes on the attorney a duty to avoid conflicts of interests, to protect client property, and to closely guard confidential information. Other professional relationships involving business dealings can also take the form of an agency. These relationships are built on trust and confidence so the principal's interests must be protected. The agent owes the principal a duty of loyalty to act in the principal's best interest in all business dealings involving the agency. When we attempt to think through the ethical issues that arise in business, we are engaging in ethical reasoning, which may be conducted on different levels. Ethical theories, which are presented in the next chapter, can guide ethical reasoning on the highest level by providing the most comprehensive and fundamental grounds for our moral beliefs and judgments. Fortunately, substantial moral arguments that do not require an understanding of these theories can be constructed. Most of our everyday ethical reasoning employs familiar ethical concepts and principles that can be readily understood and applied. Accordingly, this chapter provides a framework of seven basic ethical principles that are sufficient for most business decision making. For those who seek more, though, the next chapter provides a survey of the main philosophical theories of ethics.

CHAPTER OBJECTIVES

2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
2.2: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms
2.3: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct

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SUGGESTED DISCUSSION PROMPTS

1. What is ethically required of participants in a market economic system?
2. In what ways do participants in a market system have to depend upon each other?
3. In what ways do ethical considerations work against perfect operation of a market economy?
4. How does the prisoner's dilemma reflect the limitations of a free market system?
5. What capacities are required of an agent to engage in ethical reasoning?

ASSESSMENT FOR IN-CLASS USE

Multiple Choice Questions

Choose the BEST possible answer for each of the following.

1. A market economy is based fundamentally on _____.
   A. ethicalmotivations
   B. the profit motive
   C. human welfare
   D. manufacturing

   Correct Answer: B
   2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
   Topic/Concept: Market Ethics
   Difficulty Level: Easy
   Skill Level: Understanding

2. A market with perfect competition would require _____.
   A. agents to not be rational
   B. that there be no contracts
   C. that ethics not be necessary
   D. ethical guidelines to be legally codified

   Correct Answer: C
   2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
   Topic/Concept: Market Ethics
   Difficulty Level: Easy
   Skill Level: Understanding

3. Fraud is unethical because _____.
   A. all parties must have access to pertinent information
   B. no one may be permitted to profit too much
   C. market economies require freedom of action

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D. the market requires everyone to further their own interests

Correct Answer: A
2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
Topic/Concept: Market Ethics
Difficulty Level: Easy
Skill Level: Understanding

4. The difference between *Homo economicus* and actual people is that _____.
   A. *Homo economicus* is capable of making any decision
   B. *Homo economicus* pursues many different interests
   C. actual people pursue their own self-interest
   D. actual people are less than perfectly rational

   Correct Answer: D
   2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
   Topic/Concept: Market Ethics
   Difficulty Level: Moderate
   Skill Level: Analysis

5. A market economy alone cannot sustain public goods because _____.
   A. no one would want to take advantage of public goods
   B. people would be free riders if they could be
   C. people would try to sell each other public goods
   D. participants in a market economy are imperfectly rational

   Correct Answer: B
   2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
   Topic/Concept: Market Ethics
   Difficulty Level: Moderate
   Skill Level: Application

6. Market outcomes lead to unequal outcomes mainly because _____.
   A. it involves random processes
   B. participants have differing levels of skill
   C. free markets are inherently unjust
   D. there is government interference

   Correct Answer: B
   2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions

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Topic/Concept: Market Ethics
Difficulty Level: Moderate
Skill Level: Analysis

7. A fiduciary has the special responsibility to _____.
   A. care for another's financial interests
   B. sell goods as efficiently as possible
   C. provide as much information as possible
   D. take a professional interest in another's success

   Correct Answer: A
   2.2: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms
   Topic/Concept: Roles, Relationships, and Firms
   Difficulty Level: Easy
   Skill Level: Understanding

8. Professions have a contract with society whereby they _____ in exchange for sharing the many benefits of their specialized knowledge.
   A. submit to total government regulation
   B. relinquish control over their work
   C. forgo licensing requirements
   D. are granted self-regulation

   Correct Answer: D
   2.2: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms
   Topic/Concept: Roles, Relationships, and Firms
   Difficulty Level: Easy
   Skill Level: Understanding

9. From a traditional economic point of view, a firm was viewed as _____ which sought to maximize its profits.
   A. a combination of markets and relationships
   B. a series of relationships, roles, and markets
   C. a moral actor
   D. a market actor

   Correct Answer: D
   2.2: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms
   Topic/Concept: Roles, Relationships, and Firms
   Difficulty Level: Easy
   Skill Level: Understanding

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10. The ethical concept of dignity most centrally involves _____.
    A. treating all persons equally
    B. disclosing all information that is needed by others
    C. recognizing the intrinsic value of persons or other entities
    D. behaving with high standards of virtue

    Correct Answer: C
    2.3: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct
    Topic/Concept: Ethical Reasoning
    Difficulty Level: Easy
    Skill Level: Understanding

Essay Questions

1. What are the basic components of a market system, and what assumptions are made about human behavior?

   2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions
   Topic/Concept: Market Ethics
   Difficulty Level: Moderate
   Skill Level: Application

2. What is the difference between a fiduciary and an agent? What special obligations are characteristic of a fiduciary that is not an agent?

   2.2: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms
   Topic/Concept: Roles, Relationships, and Firms
   Difficulty Level: Moderate
   Skill Level: Analysis

3. What are the required components of the moral point of view, and how are they exercised in a business setting?

   2.3: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct
   Topic/Concept: Ethical Reasoning
   Difficulty Level: Moderate
   Skill Level: Analysis

4. What are some basic questions that should be asked when making a decision that poses an ethical dilemma?

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2.3: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct
Topic/Concept: Ethical Reasoning
Difficulty Level: Moderate
Skill Level: Application

5. Describe "context" and how it affects ethics and the decision-making process.

   2.3: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct
   Topic/Concept: Ethical Reasoning
   Difficulty Level: Easy
   Skill Level: Understanding

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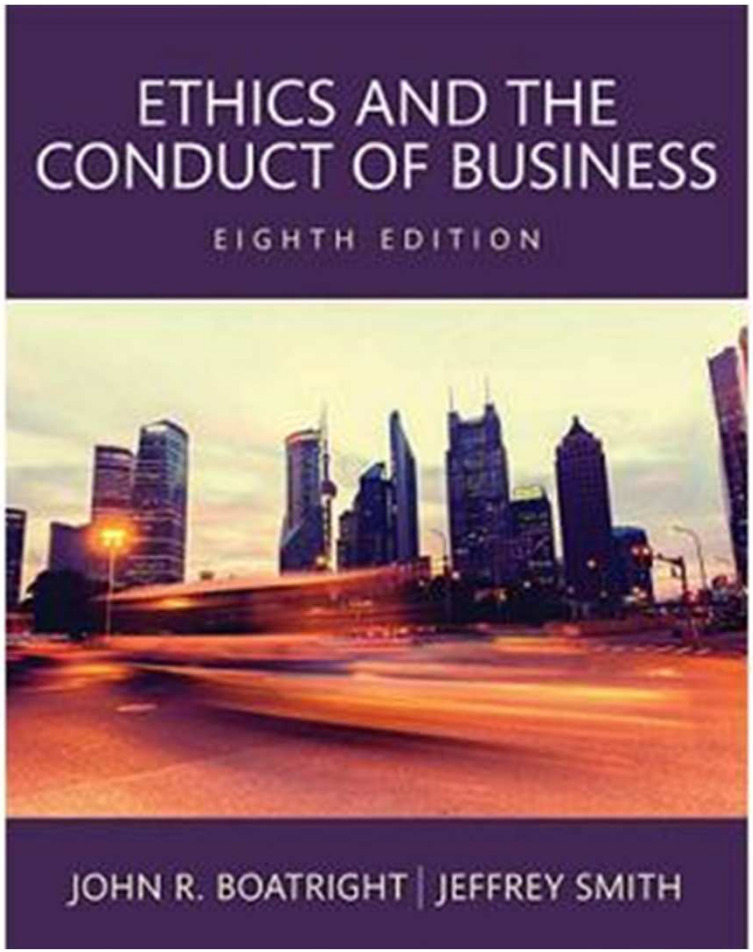

Chapter 2

Ethical Decision Making

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Modules

- Introduction: Ethical Decision Making
- 2.1: Market Ethics
- 2.2: Roles, Relationships, and Firms
- 2.3: Ethical Reasoning
- Conclusion: Ethical Decision Making

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Learning Objectives

2.1: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions

2.2: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms

2.3: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct

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Introduction: Ethical Decision Making

- A buyer and seller come together to trade
- Business activity involves roles and relationships
- Seven basic principles of ethical decision making

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2.1: Market Ethics (1 of 4)

Objective: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions

- 2.1.1: The Market System
  - Features
  - Justification
  - Market outcomes
- 2.1.2: Ethics in Markets
  - Self-interest
  - Morally free zone
  - Ethics for imperfect markets

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2.1: Market Ethics (2 of 4)

Objective: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions

- 2.1.3: Breaches and Fraud
  - Implicit
  - Incomplete
  - Lack remedies
  - Fraud and manipulation
- 2.1.4: Wrongful Harm
  - Obligations of morality
  - Due care and negligence

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2.1: Market Ethics (3 of 4)

Objective: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions

- 2.1.5: Market Failure
  - Conditions
  - Externalities
  - Public goods
  - Collective choice

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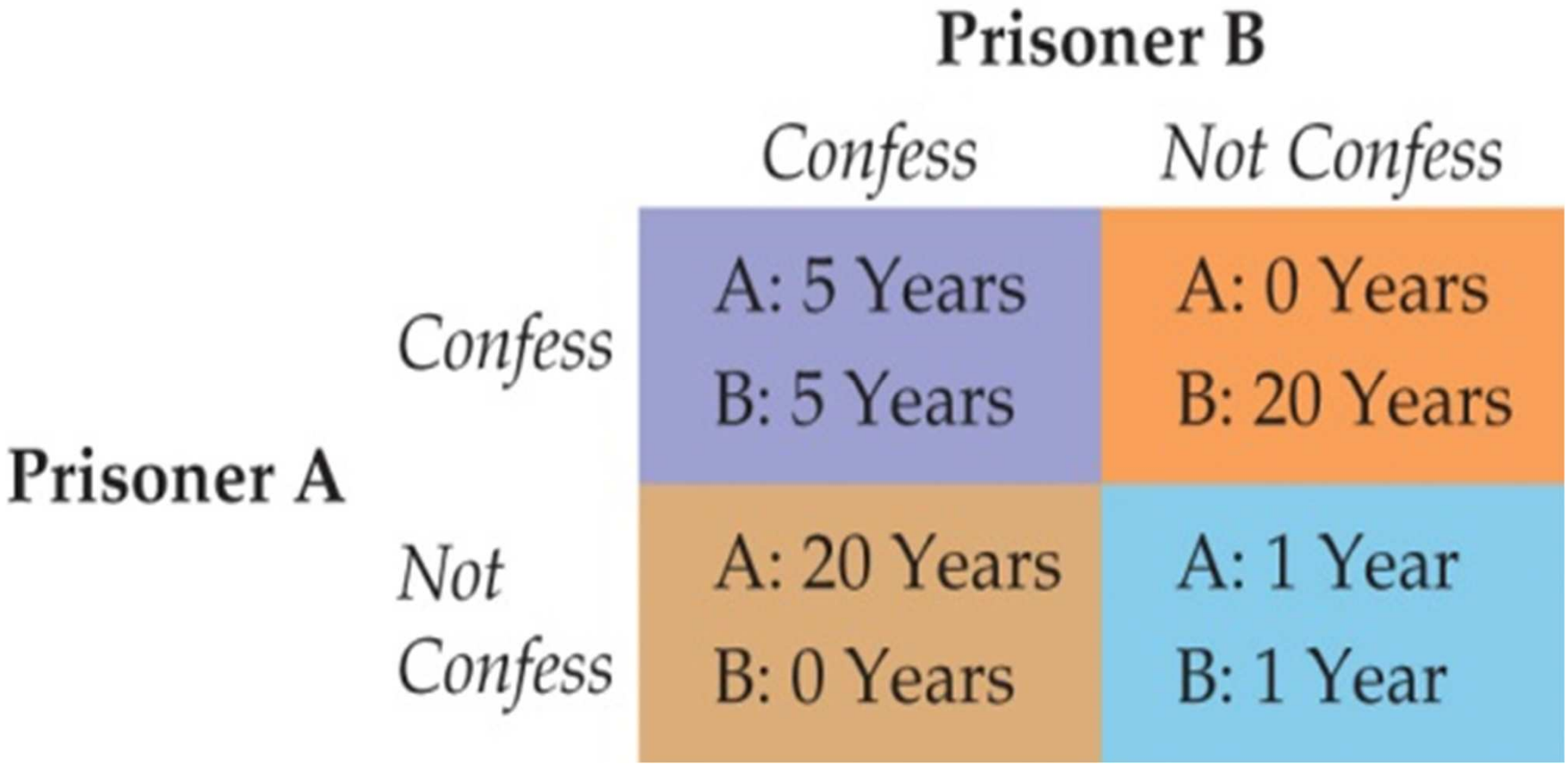
Figure 2.1: Prisoner's dilemma



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2.1: Market Ethics (4 of 4)

Objective: Recognize the features of the market system, the ethics of market transactions, and the problems created by imperfect market conditions

- 2.1.6: Summary of Market Ethics
  - To address problems in imperfect markets
  - Laws

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Table 2.1: Ethics in Markets

Problems	Elements	Solutions
Violation of agreements (breaches of contract)	Breaches of contract often result from agreements that are implicit, incomplete, and lack immediate remedy.	• Contract law • Principles for promise keeping
Misrepresentation of information (fraud)	Fraud involves not only misrepresentation of information but also materiality, intent to deceive, reliance, and harm.	• Anti-fraud law • Principles for honesty
Wrongful harm of others (torts)	Torts are the intentional or negligent violation of rights in such matters as health, safety, privacy, property, and discrimination.	• Tort law • Principles for due care
Market failures (inefficiency)	Market failures result in inefficiency due to low competition, externalities, public goods, and collective choice problems.	• Government regulation and legislation like antitrust law, consumer law, employment law, securities law, environmental law, taxation • Special use of market Mechanisms • Trustworthy behavior

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2.2: Roles, Relationships, and Firms (1 of 2)

Objective: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms

- 2.2.1: Agents and Principals
  - Agents
  - Duties of agents
- 2.2.2: Fiduciaries and Professionals
  - Fiduciary
  - Fiduciary duty
  - Fiduciary relationship
  - Defining features of profession
  - Standard of profession

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2.2: Roles, Relationships, and Firms (2 of 2)

Objective: Identify the duties and obligations associated with fundamental business roles and relationships in markets and firms

- 2.2.3: Firms
  - Economic view
  - Legal view
  - Sociological view
- 2.2.4: Summary of Roles, Relationships, and Firms
  - Divided into two ethics
  - Obligations
  - Myriad roles and relationships

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2.3: Ethical Reasoning (1 of 2)

Objective: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct

- 2.3.1: Philosophical Accounts
  - Moral point view
  - Features of moral point view
- 2.3.2: Psychological Accounts
  - Psychologist's conclusion
  - Daniel Kahneman's perspective
  - Lawrence Kohlberg's perspective

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Table 2.2: Moral Development According to Kohlberg

Level	Stages	Ethical Reasoning
Pre-Conventional Morality	1. Obedience and Punishment Orientation 2. Self-Interest Orientation	People are focused on themselves and incapable of other-oriented ethical reasoning or behavior.
Conventional Morality	3. Good Interpersonal Relations 4. Authority and Social Order Orientation	People* are mindful of others, understand rules and laws, and conform to societal expectations. *Most adults
Post-Conventional Morality	5. Social Contract and Individual Rights Orientation 6. Universal Principle Orientation	People* can engage in mutually advantageous cooperation, understand the value of abstract moral principles, and practice sophisticated ethical reasoning. *Fewer than 20% of adults

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2.3: Ethical Reasoning (2 of 2)

Objective: Describe the philosophical and psychological approaches to ethical reasoning and the principles that constitute a moral framework for business conduct

- 2.3.3: Framework for Reasoning
  - Awareness of issues
  - Identifying issues
  - Resolving issues

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Figure 2.2: Candor, Care, Loyalty

Candor	Care	Loyalty
A fiduciary has a duty of **candor** to disclose all information that the beneficiary would consider relevant to the relationship. A violation of a fiduciary duty of candor could be • an attorney or an investment banker concealing important information from a client, or • the director of a company remaining silent about matters that are critical to a decision under discussion.	When property or assets are entrusted to a fiduciary—the trustee of a trust, for example—that person should manage what is entrusted with **due care**, which is the care that a reasonable, prudent person would exercise. It might be a breach of fiduciary duty, for example, for a trustee to invest trust assets in high-risk securities reasonably incompatible with the beneficiary's interests.	A duty of **loyalty** requires a fiduciary to do two things: • Act in the interest of the beneficiary, by acting as the beneficiary would if he or she had the knowledge and skills of the fiduciary. • Avoid taking any personal advantage of the relationship. *Taking personal advantage* is deriving any benefit from the relationship without the knowledge and consent of the beneficiary.

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Conclusion: Ethical Decision Making

- Two parts of business ethics
- Roles and relationships

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