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BUSINESS LAW & ETHICS CORNER

Fairness in business: Does it matter, and what does it mean?

Joel D. Rubin

Kelley School of Business, Indiana University, 1309 E. Tenth Street, Bloomington, IN 47405-1701, U.S.A.

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Abstract Fairness is a value that is touted and typically reinforced from childhood onward. Its association is universally positive. But does fairness have a place in business? Does it extend to the realm in which profit is emphasized? This Business Law & Ethics Corner delves into the matter and provides guidance for decision makers regarding fairness and its implications for business.

1. Introduction

This past spring was one of the worst on record, weather-wise, in the United States. From Joplin, Missouri to Tuscaloosa, Alabama and many places in between, deadly tornadoes wiped out buildings and trees. . .and most everything else in their path. Assume that you own an apartment building in Tuscaloosa that miraculously was spared damage. Before the tornadoes hit, you were renting apartments for $1,000 per month. Since many apartments were destroyed by the tornadoes, the market rate for apartments like yours has now risen to $1,500 per month. Would it be fair for you to raise the rent on your apartments to $1,500? Would your answer differ if you were dealing with a new tenant versus one who was renewing his/her lease? If you do not raise the rent, how will you decide to whom to lease your vacant apartments?

When we were children, many of us were taught the importance of fairness. As we grew older, however, we were confronted with images and instances of business people not behaving fairly. From editorials calling for the punishment of finance company executives who were involved in the events which led to the recent financial meltdown, to the ritual floggings of oil company executives summoned to testify before Congress when retail gas prices reached ever-higher levels, to Gordon Gekko declaring "greed is good" in the movie *Wall Street*, business people are often seen as being out just for themselves.

This conflict between what we were taught and what we see in the real world leads to two questions: Should business people consider fairness when making decisions? And, if so, what does it mean to be fair?

2. Why be fair?

Why should a business person consider fairness when making a decision? Isn't the singular role of a business person to make money? From an ethical standpoint, there are two primary reasons for considering

E-mail address: jorubin@indiana.edu

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fairness as a factor in decision making: (1) fairness is a virtue, and (2) the positive consequences of being fair outweigh the negative consequences. The first reason is somewhat philosophical, while the latter is more practical.

In general terms, ''virtues are those [admirable character] traits that everyone needs for a good life'' (Boatright, 2009, p. 78). While the exact details of what constitutes a good life and how that concept applies in the business context are open to debate, it seems beyond question that fairness would contribute to a good life under most definitions. Thus, fairness should be considered a virtue and a businessperson who practices fairness virtuous.

While the virtue of fairness might be enough of a reason for some business people to include it in their decision making, for many others the question of whether or not to consider fairness is heavily influenced by the potential consequences. While behaving unfairly can result in a short-term tangible gain—for example, paying employees less than a 'fair' wage or charging customers more than a 'fair' price results in more money in the company's pocket—the longer-term costs can easily outweigh those initial benefits. Chief among these is the harm that can be done to a business' reputation and to its customers' or employees' satisfaction. This, in turn, may adversely impact sales and the business' ability to attract top employees.

The controversy surrounding Nike's treatment of workers in Asia serves as a good example of reputational risk. In the mid-1990s, reports surfaced that Nike—the world's largest manufacturer of athletic footwear and apparel—was not treating its Asian factory workers fairly, subjecting them to long hours in substandard conditions for low wages (Neuborne, 1997). The reports led to a series of protests, staged mainly across U.S. college campuses. Phil Knight, then-chairman and CEO of Nike, summarized the effect of the adverse publicity and protests in a speech given at the National Press Club: ''The Nike product has become synonymous with slave wages, forced overtime, and arbitrary abuse. I truly believe that the American consumer does not want to buy products made in abusive conditions'' (Dionne, 1998, p. A27). While Nike admittedly is an extreme case, it illustrates the fact that perceptions of fairness can have a significant effect on a business' reputation and thereby impact the company's bottom line.

2.1. Academic research on the risks of unfair business

A similar risk of unfair business behavior has been uncovered via academic research. Surveying adult subjects in Toronto and Vancouver, Kahneman, Knetsch, and Thaler (1986b, p. 736) found that ''68 percent of respondents said they would switch their patronage to a drugstore five minutes further away if the one closer to them raised its prices when a competitor was temporarily forced to close'' and that ''69 percent indicated they would switch if the more convenient store discriminated against its older workers.''

Academic research also has found a risk to customer or employee satisfaction. That risk is based on the concept of transaction utility. Richard Thaler (1985) demonstrated that a person's satisfaction with a transaction could be broken down into two components, dubbing these parts 'acquisition utility' and 'transaction utility.' *Acquisition utility* reflects the difference between the value[1] of the specific item being purchased or sold and the price paid for it. For example, imagine that you want a red, Heavy Duti Schwinn bicycle. You've never purchased one before, know nothing about the seller or the suggested retail price, and have no idea how much other people have paid for similar bikes. If the most you're willing to pay is $400, that is the value of the bike. If you purchase it for $380, the happiness created by the $20 difference represents your acquisition utility.

In contrast, *transaction utility* reflects elements of the deal other than price versus the value of the item exchanged. Thaler (1985, p. 206) illustrated that concept with what has come to be known as his 'Beer on the Beach' scenario. For that analysis, he gave participants in an executive development program who said they were regular beer drinkers the following scenario. One subgroup received a version with the words in parentheses, while a second subgroup received a version with the words in square brackets:

> You are lying on the beach on a hot day. All you have to drink is ice water. For the last hour, you have been thinking about how much you would enjoy a nice cold bottle of your favorite brand of beer. A companion gets up to go make a phone call and offers to bring back a beer from the only nearby place where beer is sold (a fancy resort hotel) [a small, run-down grocery store]. He says that the beer might be expensive and so asks how much you are willing to pay for the beer. He says that he will buy the beer if it costs as much or less than the price you state.

[1] From a typical economist's perspective, the value of the item is the amount that would make the purchaser (or other affected party) indifferent between having the cash or the item.