Fair Enough: Ethics and Entrepreneurship

Robert G. Crawford
robert_crawford@byu.edu

Follow this and additional works at: https://scholarsarchive.byu.edu/facpub

Part of the Finance Commons

Original Publication Citation
Ethics in Entrepreneurship", Yale Economic Review. Issue Summer 26, Pages 21-26, Yale University, New Haven, 6, 26. Yale University 26-6 211-1-27 English eng en Articles Text application/pdf
Brigham Young University Marriott School of Management Finance FinanceDepartment
MarriottSchool © 26 Yale University. http://lib.byu.edu/about/copyright/generic.php 1 Fair Enough: Ethics and Entrepreneurship Robert G. Crawford May 25, 26 Acknowledgements This paper draws upon the phenomenological tradition of = Continental’ philosophy from Edmund Husserl, Martin Heidegger, and Emmanuel Levinas. Lise Crawford and Laura Rawlins provided helpful suggestions. This research was sponsored by the Center for Entrepreneurship in the Marriott School at Brigham Young University.

BYU ScholarsArchive Citation
https://scholarsarchive.byu.edu/facpub/1233

This Peer-Reviewed Article is brought to you for free and open access by BYU ScholarsArchive. It has been accepted for inclusion in All Faculty Publications by an authorized administrator of BYU ScholarsArchive. For more information, please contact scholarsarchive@byu.edu, ellen_amatangelo@byu.edu.
Fair Enough: Ethics and Entrepreneurship

Robert G. Crawford

May 25, 2006

Acknowledgements

This paper draws upon the phenomenological tradition of ‘Continental’ philosophy from Edmund Husserl, Martin Heidegger, and Emmanuel Levinas. Lise Crawford and Laura Rawlins provided helpful suggestions. This research was sponsored by the Center for Entrepreneurship in the Marriott School at Brigham Young University.

The “new” is presumptively something that ought to be but isn’t. On what grounds should that something be permitted? In business, why are some things legal for sale - deemed moral - while other similar things are deemed illegal - or immoral? Is the ground of this approval process rational? Or is the ground for making such decisions just competing moral perspectives?

Consider pharmaceutical innovation. Before any firm can offer a new drug for sale in Western industrialized countries, its beneficence must pass a formal process with established criteria. Demonstrating efficacy is probabilistic, and interpreting results of the process is a judgment subject to disagreement. None the less, the need for the process is accepted as a moral requirement even if particular outcomes may not be accepted. Many beneficial drugs are approved for marketing, but how many other potentially beneficial drugs are withheld from the market? The negative consequence of withholding is unknown. Alternatively, some approved drugs - like Thalidomide - are later discovered to have such negative effects that approval must be retracted. In today’s marketing environment most often the approved drugs are profitable and it is highly likely that many of the denied drugs would have been profitable as well. However, the approval process increases drug development costs, possibly preventing some beneficial drugs from ever reaching their intended beneficiaries.

For those who determine approval, profitability is irrelevant, much to the chagrin of unrequited free marketers. However, as Patricia H. Werhane explains in the book *Adam Smith and His Legacy for Modern Capitalism*, all markets are embedded in some supra-market social context that specifies a set of rights - the morality - governing participant behavior in the market, even if that set is complete laissez-faire. Free markets are presumably markets with a small set of restrictions on behavior. But in a market society where the consumer is king why abrogate the fundamental efficiency of the market? Successful abrogation has a mixed history.
The process of denying the sale of drugs on the basis of a supra-market process is not uniformly accepted. Two notable and contrasting cases are alcohol and marijuana, a proxy for all illegal drugs. Denied the opportunity for legal sale in the United States during Prohibition, a decision later reversed in recognition of Prohibition’s failure, alcohol is available for authorized sale and likely will remain so. The unintended consequences of alcohol consumption are negative and costly. However, the unintended consequences of prohibiting alcohol’s sale were also negative and possibly more costly.

Marijuana is not currently universally legal for sale in the United States. Yet, like alcohol during Prohibition, it is clandestinely sold. The unintended consequences of such illegal sale are deemed by some to have negative consequences similar to the illegal sale of alcohol during Prohibition, and these consequential costs are lower for marijuana than those for alcohol only because of lower marijuana consumption. Some argue that the unintended consequences of marijuana prohibition cost the United States more than the imagined cost of its legalization would, as evidenced in some industrialized countries where marijuana or similar drugs are legal.

Often without a formal approval process like the one in the drug industry, business continuously introduces new products and services to society, the consequences of which can be both harmful and beneficial. Are new things introduced for the benefit of others - and therefore for the entrepreneur as well - or are they solely introduced for the entrepreneur’s gain? Is gain alone sufficient justification for introduction?

Obligation

A well-developed philosophy literature grounds the perspective that each is responsible for others, prior to their “acts of choice.” That literature grounds the thesis that entrepreneurship - economic innovation, the creation of the new - is a moral response to others that arises out of the ethical relation - the obligation one has for another person - or ethics. “Being-for-others” is a short name for this view. Being-for-others is not a view that is commonly held in economics, and its inspiration is the philosophical writing of Emmanuel Levinas. The contrasting view, that entrepreneurial activity arises out of a ‘utility-maximizing self-interest’ that is morally indifferent or neutral to one’s relation with others, is the dominant view - the modern, naturalistic or egoistic view. “Being-for-self” is a short name of this view, which derives its inspiration from a multitude of philosophers, Hobbes and Mill perhaps the most familiar in economics.

The word obligation usually connotes the volitional meaning “result of choice” or “contractual agreement between parties with no prior ground.” This “result of choice” definition is usually how obligation is understood in modern economics, because the ground for activity is individual choice founded on utility maximization, according to George Stigler in “Economics or Ethics?” However,
moral obligation is also consistent with a more fundamental view that obligation is the primal
I/Other - intersubjective - relation. In this view, choice formalized by a contract is not the
establishment of the obligation but a delineation of what the prior or pre-choice obligation entails.

Obligation is prior to choice in that it establishes choice. Obligation is the felt experience of
the encounter with another person, because an encounter with another person is unlike the
encounter with any other existent of experience. (“Feeling” is used to describe this experience
because obligation is not conceptual; however the word feeling does not connote that the experience
is sensory in the same sense as emotion or other common feeling.) This claim that obligation is the
primal relation of one to another follows from several ideas or philosophical conclusions of
phenomenology, and this view commenced with Edmund Husserl and was significantly elaborated
by Martin Heidegger.

In the book Totality and Infinity, Levinas names this experience of obligation “ethics” and
states it as “the calling into question of my [egoist] spontaneity by the presence of the other person.”
In Levinas’ works – including Existence and Existent, Time and the Other, Totality and Infinity, and
Otherwise than Being or Beyond Essence – the ethical relation is the person-to-person or intersubjective
relationship. All objective experience in general and all economic activity in particular is founded
upon the relationship one has with other people. The key to understanding obligation is the
understanding that the relation with the other person is not one of comprehension or understanding
in the epistemic sense of these concepts but rather is simply one of experience.

Each person is obligated to other people, not in a psychological motivation sense, but as a
constitutive moment of what it means to be a ‘self’ in society. Obligation in this sense is not a choice;
obligation is prior to choice. It is the foundation of choice. The primary focus of obligation is
meeting the needs of others. Levinas’ perspective means that each person is obligated to meet the
concrete material needs of other persons, not just to regard the other person in passive beatific
contemplation. The foreword to Levinas’ book “Difficult Liberty” clearly states this principle. “The
other’s hunger is sacred; only the hunger of the third party limits its rights.” That is, obligation entails
satisfying the material demands of others. It hardly seems necessary to say that economics is the
theory of meeting other’s material needs. Nor does it seem necessary to state that business is the
dominant practical means of doing so. And since others’ needs present one’s ethical obligation,
business is a primary means of fulfilling this dimension of one’s ethical obligation. That is, an
exchange economy of markets and prices is the primary means through which the majority of
obligations are met. That which currently satisfies a need was once new, and producing something
new is the essence of entrepreneurship. In short the entrepreneurial act - originating business - is
ethics.
Ethical Interpretation of Competitive Market Theory

Contemporary market/business theory, arising from the dominant interpretation of Adam Smith, seemingly assumes a values-neutral, amoral, autonomous self acting self-interestedly to maximize private utility subject to constraints. This perspective of contemporary economic theory and business thought make it egological. Consequently, eco-nomics is an ego-nomics. This is the essential meaning of the positive vs. normative theoretical stance that additionally regards the normative view as a deficit mode of analysis. The assertion that Adam Smith could be or even is the foundation for the theoretical excursion justifying the moral-value neutrality of this neoclassical position has been adroitly contested by Patricia H. Werhane in the book *Adam Smith and His Legacy for Modern Capitalism*. Werhane’s careful reading of Adam Smith, not filtered by the presupposition of egoist self-interest, shows that the current reduction of self-interest to ego-interest misappropriates Smith. The challenge is to provide a non-egological account of economics and business.

This account begins by noting that any one capable of participating in the economy soon becomes aware of being enmeshed in a system where others already own everything. Aside from inherited monetary wealth, people make places for themselves in this economy by offering service to others. Such offers are congruent with the notion that encounters with others are experienced as obligations. Because everyone must have a place in the economy, each person must choose how to take up his or her obligation. Assuming obligation to others is commenced by becoming aware that self-reliant participation in the system requires being of service to others. Adam Smith says in “Wealth of Nations” that this awareness is not so much a matter of rational calculation or forethought as it is the reflective conclusion from initially serving one’s neighbor and then realizing that one is providing a service valuable enough in volume to make it a regular course of activity – one’s business. Anything one chooses is a manner of taking up of this obligation. As presented in all introductory economics courses, the economic problem - how best to accomplish one’s obligation - requires not only judging “what” service to render and to “whom,” but also “how” to render it.

For a nonegoist argument to hold, the judgment of the how, what, and whom of service must not originate in the ego. Undoubtedly, “egoist choosing,” as currently interpreted, dominates the way this judgment is understood. Egoist choosing is not necessarily contrary to this argument if the context of the choice is considered, because adjudicating what, how, and for whom finds its origin exterior to the ego in the context of the choice. That is, the market context of adjudication means that one’s economic choice is essentially a response to a summons, making choice more like a response to a call, rather than a spontaneous act originating in a utility maximizing ego.

How can this summons or call be manifest to a responding and responsible economic agent? Clearly in economics, the decision of which particular Other to serve, or more specifically, supply,
originates with Others. The chooser is directed to serve the one most in need of service, the one who has the strongest claim amongst the multitude of valid alternative claims. This means that choosers do not merely serve the one claim that suits their egoist utility, independent of the one served. That is, the response to one claim for service must not discount every other claim. Therefore the what, whom and how of the decision must be revealed by others. This argument recognizes that markets and prices guide an innate willingness to act rather than create the incentive to act.

The market is the most effective social institution to accomplish such a revealing or guiding of action. In the theory of demand - under the provisional assumptions of certainty - all individuals place a value on a good and express that value by their bid price. The highest price defines the highest valuing user and directs or attracts the service response. The manner of responding must cover the cost of response, where cost is the second highest valued claim. Further, the response usually cannot be just a one-time response, through which all future obligations are absolved. Rather, for the server, the service must be sustainable or perpetual. Sustainable service requires that it be profitable service - profit interpreted in its economic sense of revenue covering all costs, including cost of capital.

Since economic profit tends to zero in competitive markets, economic profit is not an unearned surplus. Zero economic profit means accounting profit is the minimum necessary to keep assets employed in current employment. It does not mean that the server takes more from others than they are willing to give for the service. Economic profit functions as the signaling device: it signals the relative strength of all claims, thereby signaling whom to serve. Because profit measures the value, net of all costs, of each claim, the response to profit’s signal takes into account the fact that service could be to others. Because economic profit tends to zero and since it is determined by other’s valuation of the service, profit is not ego determined but it is an imperative call to serve others at their discretion. In this sense, profit is a moral command, as Israel M. Kirzner argues in the book *Competition & Entrepreneurship*. In a practical sense, it determines what one ought to do.

Profit in the above analysis is the signaling device that informs the servant whether or not the service is acceptable to the particular one served. Thus the claim of the ‘third’ has not been ignored. Profit, in this sense, is not a direct pursuit of the servant; it is an after the fact warrant that the service has met the requirements of the served. Profit is not pursued and is not the object of pursuit; profit ensues from directly pursuing proper service to others, properness as determined by them in the larger context of a transcendent judgment that the service is permissible.

Responding to other’s demands under the profit constraint - the burden of covering all the costs of response - is the ordinary way to best, or efficiently, take up the obligation to others on an enduring basis. This efficiency justification is the common account of business. But it isn’t necessarily an egoological account; profit maximizing behavior so-called is consistent with an ethical account. In
fact, under the theoretical conditions implicit in pure competition, economic agents must maximize profits to be moral. As contrary to reason as this assertion appears to most who misunderstand competitive markets, their misunderstanding is aided by an economics which does not make clear the implicit assumptions that lurk in the background of competitive economic theory. Although acting through markets is ordinarily the main way to take up obligations of responsibility for others, business obviously cannot be the only way. Market theory has implicit assumptions that, if not satisfied, mean that meeting the material needs of others solely through markets can not fulfill the ethical obligations economic agents have for all others.

First, market theory presupposes that the economy is an aggregation of essentially similar atomistic ‘selves’ - homo economicus - each equally prepared to participate in the economy, thereby creating a de facto economy of equals. Empirical observation clearly shows this assumption is false. The economy has many de facto unequals - the emotionally, mentally and physically challenged, the racial, ethnic and gender discriminatees, those with inherited family and wealth differences. All of these inequalities influence market outcomes, mainly by precluding full market participation. Therefore, to fully assume ethical responsibility, each person must find alternative ways to fulfill their obligations to those on the margin of or outside the market system that are unable to make their needs known via the assumed market participation. Obviously, this alternative has to be through non-market or quasi-market mechanisms and institutions. Government and religious or charitable institutions are the dominant form for this alternative in most societies.

Secondly, this argument, while still about being-for-others (being ethical) by responding to their demands, also presumes that no preferences of any particular Other are less worthy of response than the preferences of every Other. The fungibility of money as the medium that reveals value through money prices indicates this presumption. Fungibility presumes that each particular Other has an equally worthy claim on all others. Lived experience has likewise proven this assumption false. The fungibility of money in a market system means that a rich person’s cat might have milk while the poor mother’s child goes without. While such preferences may be viewed as equally worthy of satisfaction under common abundance, simple market price adjudication is too thin to assess fully these ethical nuances that become more apparent in periods of uncommon shortages or famine. Thus even avowedly market oriented economies resort to supramarket rationing of necessities during periods of scarcity engendered by war or famine.

Scarcity - the fundamental relative economic problem - requires the relative merits of preferences must always be adjudicated. This adjudication is the origin of the common law (described by Arthur R. Hogue in Origins of the Common Law) - a forerunner of other law. Law and property rights are essential to the efficient functioning of markets. These social contrivances are commonly recognized elements of the morality markets require - and they are grounded in the ethical relation.
Further, history is replete with examples of individual preferences that are unworthy of a response under any condition. In fact, such unworthy preferences have been and continue to be subject to restraints thereby preventing them from eliciting any fulfilling responses. This judgment of worthiness and their associated act of restraint presupposes some idea of transcendence - the determination of what is proper - determining the worthiness of some preferences. This transcendence also governs the morality of the inter-subjective interchange meant to fulfill ethical obligations. The existence of law (morals) in all societies is prima facie evidence that at least some transcendence governs the fulfillment of one’s obligation. Law (morality) concretizes the claim of the ‘third’ - the claim of all others - on the spontaneity of the ego.

Law governs the “what” of interpersonal exchange relationships in a broad sense that parallels the way costs function to govern the how of specific responses to others via exchange. However, since cost presumes and is conditioned by the context of a pre-existing law, the law is a factor in constituting costs. Changes in the law change the contextual web of relations that constitute costs, thereby altering those costs. Altering cost alters the specific acts by which economic agents fulfill their obligations to others. Therefore, the moral web of the act that fulfills one’s ethical obligation is unlikely to be governed by some atemporal absolute moral principle invariant to context. This consequence renders morality contextual but not relative in the conventional understanding of the commonly called “situational ethics.”

Since exchange is an intersubjective relation - the ethical relation - the whole of business is unequivocally ethically involved. Hence, the specific transactions that arise in business and how they are enacted are embedded in a moral web based upon spheres of transcendence, each sphere connected to other spheres, the union of which constitutes the morality of a specific transaction. However, this union does not necessarily imply a final or ultimate sphere or union of spheres that is most universal or comprehensive - the principle of principles regarding morality. Morality unlikely reaches a final or absolute state. The check on the morality of any specific transaction exists in the ethical relation that persists in questioning every moral rule and every spontaneous act.

The Moral Quandary of Entrepreneurial Profit

The contemporary view, described by Israel M. Kirzner in *Competition & Entrepreneurship*, conceives entrepreneurship as the seeing of a profit opportunity - often misinterpreted as merely an opportunity for personal gain - and taking the necessary actions to realize that opportunity. The ethical view has no quarrel with this level of abstraction because “opportunity” is not specified. Analysis at this level of abstraction has an acontextual aura. What constitutes a gain is likewise not yet
revealed. Without specifics that reveal the identity of the agent as well as the response to the demand and the demand itself, little can be concluded about morality. Economic theory often remains at this level of abstraction. In concrete business practice, the efficacy of acts fulfilling demand is measured by accounting profit - revenue from the activity minus the contractual costs necessary for its undertaking. These accounting numbers arise under the presumption that their preferential context is moral.

As stated above, the ethical response is signaled by economic profit, which entails accounting profit because accounting profit assures perseverance in being-of-service to others. Therefore, in its practicality, it is not surprising that entrepreneurial service gets reduced to the maximization of accounting profits. In the appropriate context, looking to profit as a guide to behavior is required. But profit doesn’t create its appropriate context. Consequently, in an acontextual direct pursuit of profits, the morality of service to the other that initiates entrepreneurial acts becomes effaced. This effacement occurs because the acontextual direct pursuit of profit is ego driven, where ego is indifferent to or neglects the Other. Profit’s direct pursuit and achievement sublimates or inverts the significance of the Other, forgetting or even ignoring that it is the Other’s demand for the service that determines profit. It is true that business is always susceptible to egoism – me first – a privileging of me over you in every context. But so is every other form of intersubjective relation. Egoism is perhaps more virulent in non-business forms of intersubjective governance since competition is usually lacking or contextually ineffective or limited – as in politics.

To summarize, in the restricted confines of a competitive market exchange economy, the enduring moral act will be profitable; however, a profitable act need not be moral. Therefore, the morality of an activity cannot be judged by its profitability. Consequently, using accounting profit as the common adjudication standard of entrepreneurial morality is acontextually inappropriate.

Because uncertainty manifests the asymmetry of information market participants’ possess, accounting costs can temporarily be reduced and accounting profit temporarily increased by deception - that is by cheating through lowering the standard of service in ways costly to detect. The possibility of cheating, while temporarily enhancing profit, renders accounting profits useless in signaling the morality of the service rendered. Thus accounting profits, while necessary for sustained activity, cannot be a sufficient criterion for adjudicating the moral merit of specific entrepreneurial action. The inadequacy of accounting profit as a moral gauge necessitates a more transcendent indicator that attaches the act to its authorizing context. Furthermore, since observed accounting profit is rarely congruent with the concept of economic profit, as George Bentsen argues in “Accounting numbers and economic values,” and since economic profit is an ex post facto concept, anticipated economic profit is an impractical guide to the moral status of anticipatory entrepreneurial action. Logically, because entrepreneurial activity creates the new, the judgment of the morality of
entrepreneurial acts cannot solely rely on a competitive past - a history that has been ethically scrutinized or sanitized as a guide to innovation. Therefore, neither can anticipated profit be an inscrutable moral guide.

The temporal structure of innovation exposes the entrepreneur’s wealth to risk. But the act of making an investment necessary to an approved entrepreneurial undertaking prior to receiving the anticipated return deemed essential to the profitability of the act is the sine qua non of ethics - a ‘being for others before being for me.’ Potentially, temporality provides a way for the ethical injunction of service to be moral when considered in a context of competition. While the morality of the act is independent of the goodness of the entrepreneur initiating it, temporality can indirectly require goodness-like behavior.

As for any economic act - or any entrepreneurial act - profit is a residual earned after the act. This practical delay requires alternatives that assure morality. The social process of morality via an anticipatory prescriptive law, for instance, is incapable of complete moral specification. Even without the delay, anticipating all pending immoral acts is impossible. Thus there is no ex ante systemic guarantee that prevents immorality. A quasi assurance is subtended by the asset value of entrepreneurial reputation. While a specific entrepreneurial intention does not possess a history that classifies it according to standards of morality, the entrepreneur often does have a history of (or the prospect of) a reputation. Therefore, since the existing or ascribed reputation of the entrepreneur precedes the intended act, some indication of the morality of the action is given by the entrepreneur’s moral reputation. The capitalized reputational loss sustained by an immoral entrepreneurial act includes the withdrawal of acceptance of the entrepreneur’s future ventures. The present value of potential losses serves as moral self-monitors.

Where the withdrawal of future business is insufficient to assure moral action, the law has an analogous anticipatory moral gauge: ex post facto accountability for the action. Knowledge that they will be held accountable after the fact makes entrepreneurs responsible before the fact. However, responsibility and hence morality retain significance only in a probabilistic sense because the efficacy of the anticipatory or forward-looking structure of all action only probabilistically redounds to the reputation of the actor. Therefore, reputation is an uncertain indicator of morality.

The effectiveness of ex post facto assessment of the entrepreneur’s ‘reputational value’ in assuring the morality of entrepreneurial innovation depends on the extent to which society regards an action as negatively affecting social welfare. Societal indifference to an act means that even if the act fails a transcendent standard, it may still be accomplished and be profitable as a consequence of social indifference. The moral identity of those whose association and interactions constitute society is indeed relevant to the outcome of the moral adjudication of entrepreneurial activity. This is clearly
manifest in the different outcomes regarding the morality of alcohol and the immorality of marijuana. The morality of the entrepreneurial venture is thus always yet to be determined and never final.

**The Morality of the Market Response**

The interpersonal - intersubjective - relation of one person to another is the ethical relation. It is a relation of obligation that is not a psychological matter of intent. Rather, obligation - and its corollary responsibility - is a way of being with others that is constitutive of selfhood. But this sense of ethical obligation is not compulsory. Obligation is not a coercive relation that overrides agentive will. Obligation is the ‘meaning’ of the other person, a meaning possibly and often easily ignored. The presence of other people is an invitation to distance oneself from one’s egoistic living by responding to them and meeting their wants. In responding to the wants of another, the respondent must consider their obligation to the third person that always conditions any intersubjective relation. Because one is also obligated to other Others, all competing obligations must be adjudicated on grounds that are not determined by the respondent’s egoist preferences - contrary to conventional economic analysis; however, recognizing these obligations is consistent with egoist will. Such response is called for by those benefiting from the response. Market response, guided by profit as a moral signal, best fulfills the obligation to serve others under two conditions: (1) everyone is equally well-suited to participate in the market, and (2) every preference is equally worthy of satisfaction. Under these two conditions, competitive fulfillment of wants meets ethical obligations.

These two conditions are rarely realized in actual markets. Failure of the first condition requires supplementary modes of response. Failure of the second condition requires supramarket bounds. To some extent, at least partial fulfillment of both requirements already exists in the form of supramarket social institutions, cultural norms and law. In response to the failure of first condition, social institutions are created to charitably - non-reciprocally - serve others by providing interim satisfaction of the wants of those not capable of present market participation. But charitable institutions will not and can not serve as the dominant means of response to others. As Adam Smith wrote in “Wealth of Nations,” “It is not from the benevolence of the butcher, the brewer, or the baker that we expect our dinner, but from their regard to their own interest.” Even in socialist societies, their compulsory charity - the redistribution of resources - succeeds mainly in proportion to the implicit market oriented base. Socialist societies without a strong market base merely equalize poverty.

Regarding failure of the second condition, the extent to which participants do not accept constraints on their spontaneity indicates that they will act as if these constraints are not binding, requiring costly prevention of attempts to appropriate resources. Such being-for-me-by-being-against-others imposes losses on others in excess of gains received by me. Society cannot long
survive such behavior. The proportion of society that is egregiously egoist must be small to maintain that society. If not small, there could not be sufficient net-of-enforcement-cost resources to maintain a society of egoists—contrary to Richard Epstein’s assertions in “Varieties of Self Interest.” Thus the actions of those who are “for-others-as-being-for-me” generate the benefits to society. And such people, for whom “being-for-you-is-being-for-me,” are the core of every successful society. This way of being defines entrepreneurial action, the foundation of societal welfare.