against Trafficking, Exploitation, and Child Labor." But the Committee lacked resources. Only 25 government labor inspectors worked on child labor, and total funds budgeted to fight child labor were only the equivalent of US$588,566. Because of the lack of funds and vehicles, no labor inspections were carried out in the agricultural sector. The national police of the Ministry of Justice was charged with enforcing criminal laws against child trafficking and forced child labor, but in 2012 only five police officers were assigned to the anti-trafficking unit, and they had to share one vehicle and only investigated seven cases that year; five additional officers were hired in 2013.

In the United States, three former child slaves sued Nestlé, ADM, and Cargill, claiming that the companies knew that the farmers supplying their cocoa were using child slaves, yet the companies continued to support the farmers by buying their cocoa; although they controlled the Ivory Coast cocoa market, the suit claimed, the companies had failed to use their control to stop slavery and instead facilitated it. The three former slaves based their lawsuit on the Alien Tort Statute, a federal law that allows foreigners to sue companies that participate in violations of their human rights. Although a district court initially dismissed the case, in 2014, the 9th Circuit Court of Appeals overruled the district court and allowed the case to proceed. The three former slaves charged that they were trafficked as children into Ivory Coast and forced to work for 14 hours a day on cocoa farms. According to the lawsuit, they were fed scraps and frequently whipped and beaten. One said he saw guards cut open the feet of children who tried to escape.

While some cocoa is now being certified as "slave-free," the great majority of the cocoa sourced from Ivory Coast is not. The cocoa beans tainted by the labor of slave boys are, therefore, still being quietly mixed together in bins and warehouses with cocoa beans harvested by free paid workers, so that the two are indistinguishable. From there, they still make their way into the now tainted chocolate candies that Hershey's, M&M Mars, Nestlé, and Kraft Foods make and that we buy here and in Europe. Without an effective system of certification, much of the chocolate we eat that is made from West African (Ivory Coast and Ghana) cocoa probably contains a portion of tainted chocolate made from beans harvested by enslaved children.

WRITING PROMPT

Journal: What Are Your Views on the Nature of Wrong?

1. **What are the systemic, corporate, and individual ethical issues raised by this case?**
2. **In your view, is the kind of child slavery discussed in this case absolutely wrong no matter what, or is it only relatively wrong (i.e., if one happens to live in a society such as ours that disapproves of child slavery)? Explain your view and why you hold it.**
3. **Who shares in the moral responsibility for the slavery occurring in the chocolate industry?**
4. **Consider the bill that Representative Engel and Senator Harkin attempted to enact into a law, but which never became a law because of the lobbying efforts of the chocolate companies. What does this incident show about the view that "to be ethical it is enough for businesspeople to follow the law"?**

▶ The response entered here will appear in the performance dashboard and can be viewed by your instructor.

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Case Notes

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Case Study 1.2: Aaron Beam and the HealthSouth Fraud

In 2015, Richard M. Scrushy's website described him as a "Speaker, Businessman, Entrepreneur." The website does not mention that he is also a convicted felon and that only two years earlier he had finished spending six years and ten months in a federal prison plus three years of supervised probation as his sentence for being found guilty of bribery, conspiracy, and mail fraud. The website also describes him as "a business visionary [with] a successful business career" and "the HealthSouth mogul . . . [who] served as Chairman and Chief Executive Officer of HealthSouth for nearly twenty years." The website omits any mention of the fact that he lost all his money when he was ordered by a judge to pay $2.87 billion in damages because he "knew of and actively participated in the fraud" that nearly destroyed HealthSouth.

HealthSouth was founded by Richard Scrushy and Aaron Beam. Although Scrushy was the company's main founder and leader, much of what became known as the "HealthSouth fraud" was organized and carried out by Aaron Beam.

Aaron Beam was born in November 1943 and grew up in Shreveport, Louisiana. In 1967, he graduated from Louisiana State University with a degree in business. After serving in the Navy, he took accounting courses at the University of Houston and passed the Certified Public Accountant (CPA) exam in 1978. With his CPA in hand, he took a job at Lifemark Corporation, a company that owned and managed several hospitals. There he met Richard Scrushy, whom he described as a "charismatic" leader, an engagingly "charming" person, and a "brilliant" businessman. At Lifemark, Scrushy had worked his way up to the position of chief operating officer after having taught briefly in the respiratory therapy program of the University of Alabama and at Wallace State Community College. In 1983 Lifemark was purchased by American Medical International, and Scrushy invited Beam to join him in starting HealthSouth, a new company that would provide medical rehabilitation services to hospitals and their outpatients in Birmingham, Alabama. Scrushy believed that they would be able to provide rehabilitation therapy to patients at lower costs than regular hospitals, and so hospitals would be glad to send their patients to them for rehabilitation. He would turn out to be right.[2]

The two founded the company in 1984, with Scrushy as CEO and Beam as chief financial officer (CFO). Beam later said that Scrushy ran the company like a "dictator," and with a self-assurance that intimidated people and sometimes made Aaron and others fearful of contradicting him. Scrushy, he said, was "almost a cult-like figure" who inspired intense loyalty and whom people eagerly followed, willingly carrying out his confident orders.[3] Another employee said Scrushy "had boundless energy" and "was a great motivator" who worked "so hard himself, it was almost like you couldn't let him down."[4]

From the beginning, Scrushy and Beam both knew the company had to appear profitable to satisfy investors and lenders and to later succeed in issuing and selling company stock to the public. Although the company was doing reasonably well, Scrushy told Beam that he should do whatever he could to make their financial reports look even better. Although Beam was reluctant at first, he felt both pressured and awed by Scrushy and eventually moved some of the company's startup costs from the "expenses" column to the "capital investments" column, which made their net profits look larger.[5] While he realized doing so might be "a little" misleading, Beam felt it was technically within the bounds of accounting rules and that investors would be sophisticated enough to understand what was happening. He described the move to himself as "aggressive accounting," but definitely "not fraudulent."

In 1986, the company successfully went public, and both Scrushy and Beam as well as their investors made a great deal of money. Moreover, the company continued to expand rapidly, and revenues continued to climb upward just as quickly. With his new riches, Beam was able to buy a beach house, a condo in the French Quarter of New Orleans, a private plane, fancy cars, and $30,000 worth of Hermès ties. Everywhere he went, he was known and respected. When he walked into a restaurant he could see people pointing him out, while others came up to meet him or talk to him, telling him what a wonderful job he was doing. "I was a rock star," he later said, and it was all "pretty heavy stuff." [6]

Scrushy also celebrated his new wealth. He had divorced his first wife and married his second, a woman named Karen with whom he had four children and a passionate but stormy relationship. He bought two Cessna jets, Lamborghini and Rolls Royce cars, 10 yachts, expensive artwork, and several multimillion-dollar houses. He also built himself an estate with a 20-room 14,000 square-foot mansion and a helicopter pad. He made lavish donations to charities, gave money to schools that gratefully named buildings after him, and made such a large gift to a local community college that it named a whole campus the "Richard M. Scrushy Campus." In high school, Scrushy had taught himself to play the guitar and had played in garage bands; now he recruited several professional musicians, formed a country music group named Dallas County Line, and with himself as lead singer, cut a CD and financed a world tour for the group.

Hiding a Shortfall to Appear Profitable

Over the next 10 years the HealthSouth company grew into a $3 billion Fortune 500 company. With 22,000 employees, it was the nation's largest provider of rehabilitation, surgery, and therapy outpatient services. Beam continued using "aggressive accounting" practices in the company's financial reports. When the company expanded to other locations, he had some of the costs capitalized instead of being expensed, and sometimes the added revenues from the new locations were listed as revenue growth from the company's previous locations. Instead of writing off unpaid receivables, Beam just kept them on the books as company "assets." He continued to reassure himself with the thought that "astute investors knew what we were doing and saw it as financial gamesmanship and not outright fraud."[7]

Part way through the second quarter of 1996, Scrushy and Beam realized that the company, for the first time, would fall short of meeting Wall Street analysts' expectations of quarterly revenue by about $50 million. The two men were sure this was a one-time event and that the company would return to meeting analysts' targets the following financial quarter, like it had for the past 40 quarters. However, at the time, the company was negotiating a new credit agreement with a syndicate of 32 lenders from around the world, and while the banks had agreed to extend HealthSouth a line of credit totaling $1.25 billion, they had also made clear that the company had to provide them with favorable quarterly financial statements.[8] Scrushy assured Beam that if the banks got wind of the shortfall, that information would cripple the company they had worked so hard to build. So Beam had to do everything he could to keep as much information about the shortfall as possible from leaking out of the company. If they could just get through the quarter, Scrushy felt, then everything would be okay.[9]

Agreeing with Scrushy's assessment of the situation, Beam decided to fix the company books "this one time." Beam convinced two of the people working for him in the finance department to come in on the plan: Bill Owens, the company controller, and Mike Martin, the company treasurer. With the help of a few other employees, they went through the earnings reports that each of the dozens of HealthSouth clinics scattered around the country turned in to company headquarters each financial quarter. They carefully inflated the numbers by inserting many small additional revenue entries throughout each report. Then they consolidated the reports into a single corporate report.[10] The numerous fictitious additions they made on the reports were all small because they knew the external auditors would only check the validity of large revenue entries, and were highly unlikely to check the many small fictitious entries they were making.[11] Moreover, Scrushy had earlier told Beam that he did not allow the company's own internal auditors access to the corporate general ledgers, which is where the fraud was being carried out.

Although he realized these actions violated generally accepted accounting principles, Beam felt that what he was doing was for the good of everyone in the company. If the company failed, a lot of people would be hurt. Anyway, he was only going to do it just this one time.

Unfortunately, the following quarter company earnings again fell short of Wall Street expectations. This time Scrushy did not have to persuade Beam. After the first time, Beam later said, it had become "a little easier going down that road."[12] The fraud proceeded much like it had the previous quarter, except that more people were brought into the scheme. Ken Livesay, the assistant controller, helped by downloading all of the clinic reports from around the country to his computer and figuring out the gap between the company's true earnings and what Wall Street expected—about $70 million this time.[13] He reported these figures to Bill Owens and Mike Martin. Then Beam, Owens, Martin, Livesay, and a few others worked their way through the clinics' reports, inserting enough fictitious revenue entries to fill in the gap. Because earnings kept falling short of expectations, the process had to be repeated each quarter. Eventually, more finance personnel were added to the group until it grew to about 15 people who started referring to themselves as "the family."

By 1997 HealthSouth was the largest rehabilitation services company in the industry and, with a total of $106 million in compensation, Scrushy was the third-highest-paid CEO in America. A year earlier his second wife had divorced him and now he married his third, Leslie, with whom he had two more children. He became an active member of the Guiding Light Church to which he made sizable donations, and he and his wife eventually began hosting a daily evangelical television show that was broadcast from the church.

Although he was now hardly hesitating to tamper with the company reports, Beam still felt anguished and guilty and found it difficult to sleep. Later he admitted that he did not have the "ethical bearing" that he should have had to stand up to Scrushy. He should, he said, have had the "courage" to say, "no, this is wrong."[14] He felt that he had crossed a line somewhere and now found himself doing things he could not deal with.

Ashamed of what he was now so willingly doing, Beam decided to retire from the company in 1997. He bought several acres of land in the country and there he and his wife built their 5,000 square-foot "dream house." Beam assumed that the company's earnings would eventually improve and that it would once again do well enough to stop having to falsify its financial reports. He was wrong.

Investigation and Outcome

The fraudulent accounting at HealthSouth continued for six more years, until 2003 when the FBI began investigating whether Scrushy might be part of an insider trading scheme. As part of its investigation, the FBI interviewed Weston Smith, who had replaced Beam as CFO. Smith had little to say about the insider trading scheme; instead, he informed the surprised investigators about the fraud that had been going on at HealthSouth.

By the time the government stepped in and prosecuted HealthSouth's executives in 2003, HealthSouth's earnings had been overstated by $2.7 billion. In 2005, saying he did not know that fraudulent entries were being inserted into the books, and in spite of being accused by Beam, Smith, Martin, Owens, Livesay, and others of having known about the scheme, Scrushy was declared innocent of any criminal wrongdoing by a jury. Beam and the other members of "the family" were not so lucky. He and 15 other HealthSouth employees who had helped carry out the fraud were fined and jailed or placed on probation.

Although Scrushy was not convicted of any wrongdoing in the HealthSouth fraud, in 2006 he was found guilty of paying $500,000 in bribes to Alabama Governor Don Siegelman in exchange for a seat on a state hospital regulatory board. Scrushy was sentenced to seven years in prison for the bribe, a sentence he began serving in 2007. Scrushy believed that government prosecutors had filed the bribery charges against him in retaliation for their inability to secure his conviction in the HealthSouth trial, but his lawyers failed to win the appeals they filed on Scrushy's behalf. In 2009, while serving his jail sentence, Scrushy lost a $2.8 billion civil lawsuit brought against him by the company's shareholders; at the end of that trial, the judge said that it was clear to him that "Scrushy knew of and actively participated in the fraud." Scrushy's bank accounts were seized and his houses, boats, cars, and other remaining property were auctioned off to pay the $2.8 billion judgment against him. Distraught by the outcome of the lawsuit which left his wife and children penniless, Scrushy continued to maintain his innocence in both the HealthSouth fraud and in the Siegelman bribe case. His wife remained loyal to him and brought their children to visit him every week while he served his prison sentence. Both his wife and his former pastor at the Guiding Light Church continued to believe in Scrushy's innocence.

Although he could have received up to 30 years in jail and been fined up to $1 million, Beam spent only three months in a federal prison and paid $285,000 in fines and another $250,000 in lawyer's fees. After he was released from prison in 2006, Beam said his experience had taught him some hard lessons, but he still blamed Scrushy for much of what had happened. Scrushy, he later said, was a "sociopath" with a large ego who had little empathy for others and who could "intimidate people." People like Scrushy, he suggested, become managers in many major companies where they ask employees to do things they know are wrong. Employees need to "have some moral character," he said, to resist being influenced by such managers and to avoid being led "down a path that you shouldn't go." [15]

Aaron Beam now runs a lawn service called Green Beam Lawn Service in Alabama, using a lawnmower he bought by bartering 50 of his last remaining Hermès ties. He no longer has numerous employees working for him but, he says, "I'm living my life honestly" and that has given him "a lot of peace of mind." While he has to mow lawns in the Alabama heat for no more than about $50 a lawn, the money he makes, he says, is money he knows he's earned and so is able to "sleep well at night." [16]

Scrushy served out his prison term and was released from prison on July 25, 2012, and began his three years of supervised probation that included providing 500 hours of community service. In November 2014, a judge ruled that he did not have to serve the final eight months of his probation and Scrushy was finally completely free.

Scrushy moved to Houston, Texas, where he now offers his services as an inspirational speaker and experienced businessman. His personal website, richardscrushy.com, makes no mention of the HealthSouth fraud nor of his bribery conviction. Instead, it describes him as a "business visionary" who has a "powerful" record of accomplishment as a "dynamic risk taking entrepreneur."[17]

WRITING PROMPT

Journal: Evaluate Moral Responsibility at HealthSouth

1. Which of the "obstacles" to moral behavior do you see at work in Aaron Beam's behavior and thinking? In Richard Scrushy's?
2. Explain how Beam might have used the loyal agent's argument to defend his actions. Do you think that in Beam's situation, the loyal agent's argument might have been valid? Explain.
3. In terms of Kohlberg's views on moral development, at what stage of moral development would you place Beam? Explain. At what stage would you place Scrushy?
4. Was Beam *morally responsible* for engaging in the "aggressive accounting" methods he used? Was his responsibility *mitigated* in any way? Was he *morally responsible* for changing the clinic reports to increase the company's earnings? Was his responsibility for this *mitigated*? Were those who *cooperated* in his actions morally responsible for those actions? Was their responsibility mitigated? Do you think Scrushy was morally responsible for the accounting fraud? Explain each of your answers.

▶ The response entered here will appear in the performance dashboard and can be viewed by your instructor.

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Summary

1. Ethics is the study of the moral standards that we and others hold, and it aims at developing standards that are reasonable and can be justified. Moral standards are standards that involve serious wrongs or benefits; should be preferred to other standards and to self-interest; are not established by authority figures; are felt to be universal; are based on impartial considerations; and are associated with special emotions (such as guilt and remorse) and vocabulary (such as *obligation, rights, justice*). From the age of three, we seem to be able to distinguish moral from nonmoral standards.
2. Business ethics is a particular kind of ethics: it is the study of the moral standards that should guide business activities, and it aims to develop standards that are reasonable to apply in business. Some argue that ethics does not belong in business because free markets automatically produce ethical behavior, because managers have an obligation to serve their companies regardless of ethics, and because as long as managers follow the law they will behave ethically. All of these arguments, however, are based on false assumptions. Moreover, there are many legitimate reasons to think that ethics should be brought into business. They include the following: ethics applies to all human activities; business needs ethics to survive; ethics is consistent with profit-seeking; customers, employees, and people in general care about ethics in business; studies show that ethics does not lower profits but seems to enhance them. Furthermore, several factors have created new ethical questions for business people; for