SYLLABUS

Term: Fall 2006 (1st Half)  
Professor: Roy C. Smith  
Time: T/TR 1:30-2:50 pm  
Office: KMEC; Phone: 8-0719  
Classroom:  
Email: rsmith@stern.nyu.edu  
Secretary:  
Teaching Assistant:  

Objectives of this Particular Course

The purpose of this particular section of Professional Responsibility is to combine some of the basic principles taught in the regular PR course with a broad understanding of the causes and consequences of market failure and the history, structure, and responsibilities associated with the governance of corporations in our modern society.

The course will rely on a new book by Prof. Smith and Prof Ingo Walter called *Governing the Modern Corporation* (Oxford Univ. Press, 2006) which will be available in the bookstore. This book examines the role of corporations, investors, intermediaries and regulators in the events that preceded and followed the build-up and bursting of the financial bubble in 2000-2004.

There is also a series of reading from the MEL textbook, *Professional Responsibility*, which will be handed out in class at no cost to the students.

*The syllabus indicates the nature of the material to be covered, and students should familiarize themselves with it before deciding to sign up for this course. Other sections of Professional Responsibility that do not involve the Smith and Walter book are available for those students preferring the traditional approach to the course.*

Preparation for Class

The student’s primary obligation in this course is to prepare for class discussion by thorough reading and analysis of assigned materials. Case discussions and in-class activities are an essential part of the course. All students are responsible for preparing answers to all the “study questions” raised for each session before coming to class. The instructor will ask some students to provide their answers orally, as a basis for further discussion.

Written Study Question Analyses

For full credit, each student must submit a written analysis of one or more of the “study questions” associated with each session, on five different occasions over the course of the term. That is, for 5 sessions of his or her choosing the student should write out his or her analysis for any one of the assigned study questions. These analyses should be 2-3
The student may submit one more than the required 5 written analyses for extra credit.

**Student Communications**
Course information is posted on Blackboard

**Term Paper**
Students are responsible for a term paper, described on the next page.

**Grading**
The weights for the student’s overall grade are:

- Class Participation 30%
- Written Study Question Analysis 30%
- Term Project 40%

**Textbook**
All cases and readings for this course are found in:

*Governing the Modern Corporation* available in the NYU Professional Bookstore.

*Selected readings from Professional Responsibility: Markets, Ethics, and Law Cases and Readings for 2006-2007*
TERM PAPER: GUIDELINES FOR CASE ANALYSES

The purpose of this paper is to allow the student to apply principles of professional responsibility to an actual, specific business situation. The student will describe a situation with which he or she has first-hand familiarity, or a current event reported in the press. In any event, the requirement is that the situation raise ethical or legal issues that require some course of action or analysis.

The paper should have the following major sections:

I. Situation
Provide a description of the situation or practice; this description must be detailed and rich enough to allow the reader to get a clear sense of the issues and circumstances (2-4 pages).

II. Analysis
Apply some method or methods of ethical (or perhaps legal) reasoning to the situation and examine the results of this application. Are the results logical, beneficial, counter intuitive, or in any other way problematic? Here the student should apply, wherever appropriate, concepts from the course and its readings. Also, the student should cite the relevant law (2-4 pages).

III. Resolution & Conclusion
Describe how the situation was actually resolved. Discuss this resolution in light of the ethical analysis from section II (2-4 pages).

In sum, this paper should be roughly 8-12 typed, double-spaced pages.

IMPORTANT: Good performance (hence good grades) on this assignment consists of systematically and thoroughly applying relevant concepts and methods from the course to the situation, and in testing the worth of those concepts and methods in resolving the ethical issues it presents.

NOTE: Written Projects Due at session 10 (Oct. 5, 2006)
SESSIONS, TOPICS AND ASSIGNMENTS

SESSION #1  Sept. 5, 2006

Introduction - Market Failures & Ethical Theories

Read: “Economic Theories of Regulation: Normative v Positive”
by Linda N. Edwards and Franklin R. Edwards

“The Coase Theorem,” by Mitchell Polinsky

“Moral Hazard”
by Robert Pindyck and Daniel Rubinfeld

Study Questions

1. What is “market failure?” Why do market failures tend to bring about law or regulation to counter their effects? What does Coase propose as an alternative?

2. What is “moral hazard” in practical business terms?

SESSION #2   Sept. 7, 2006

Truth & Disclosure

Read: “Is Business Bluffing Ethical?” by Albert Z. Carr

“The Numbers Game” by Arthur Levitt

“Making and Ethical Decision” by Terry Halbert and Elaine Ingulli

Study Questions

1. Would Albert Carr voice any objections to the financial analysts or the rest of the financial industry described by Levitt? Do you agree with Carr?

2. Can you identify any market failures resulting from the actions described by Levitt?

3. How would you assess the long-term effects of bluffing as applied to the job of an equity analyst? Would Albert Carr agree?

4. How would you square the practice of earnings management (described by Levitt) with the article by Halbert and Ingulli?
SESSION #3 Sept. 12, 2006

Gifts, Side Deals & Conflicts of Interest

Cases: “Buynow Stores” by Bruce Buchanan
          “Roger Berg” by Ronald M. Green
          “Friends and Family” by Melanie Warner
          “Wall St. and the Nursery School: A New York Story” by Gretchen Morgenson and Pat McGeehan

Read: “A Bribe by Any Other Name,” Neil Weinberg

Study Questions

1. Make a list of all the gift practices described in Buynow Stores. In your judgment, which of these, if any, are inappropriate? Use ethical concepts and methods from the Green and Halbert/Ingulli readings to support your position.

2. Do the Roger Berg and Wall Street Nursery School cases differ materially from Buynow Stores? Use ethical concepts and methods from the Green and Halbert/Ingulli readings to support your position.

SESSION #4 Sept. 14, 2006

Governance in Context: Bubbles and Fluid Markets

Read: Governing the Modern Corporation (GMC), Preface and intro to Part I, and

       Chapter 1 Irrational Exuberance
       Chapter 2 New Financial Markets

Study Questions:

1. What were the major contributing factors in the massive expansion of traded financial markets in the 1980s and 1990s?

2. What effects did such developments in capital markets have on corporate
officers and directors during the 1990s?

3. How could so much damage to investors in financial markets occur during a period of high public transparency, and extensive and detailed regulation intended to protect investors from abusive practices of corporations or unscrupulous individuals?

SESSION #5   Sept. 19, 2006

Corporations and Their Governance

Read:  GMC (Intro to Part II, and

   Chapter 4       The Role and Duties of Corporate Directors

   Chapter 5       Evolution and Powers of the CEO

Study Questions:

1. How do the powers of a public corporation differ from those of a private partnership and of a closely held corporation?

2. How do the market failures of the 1930s compare with those of the 2000s?

3. How did the governance objectives of corporations change from the 1920s to the 1970s to the 1990s?

4. What are the arguments for and against separating the roles of chief executive from board chairman?

SESSION #6   Sept. 21, 2006

Corporate Governance and Capital Market Institutions

Read:  GMC (Intro to Part III, and

   Chapter 6       Institutional Investors

Study Questions:

1. How do financial institutions “police” the marketplace? Is their role effective?

2. What are the similarities between public corporations and institutional investors? What agency costs can be associated with institutional investors?
3. What led to the breakdown of fiduciary conduct of institutions during the 1990s?

SESSION #7   Sept. 26, 2006

Corporate Governance and Capital Market Institutions

Read: GMC

Chapter 7  The Auditors

Study Questions:

1. Describe the basic principles that provide the regulatory framework for the auditing profession?

2. What happened to these principles during the 1990s? What were the consequences of the changes in their application? Who is responsible to defending these principles?

3. After the failure of Enron, its auditor, Arthur Andersen, was prosecuted by the Federal Government, convicted and forced into liquidation. A few years later the US Supreme Court overturned the Enron conviction? Was Andersen treated unfairly? What else could the government have done to assert its interest in the case?

SESSION #8   Sept. 28, 2006

Corporate Governance and Capital Market Institutions

Read: GMC

Chapter 8  The Bankers

Study Questions:

1. Make a list of the offenses alleged to have been committed by investment banks and brokerage firms during the 1990s, and indicate what laws these offenses might have broken.
2. How did competitive conditions for wholesale banks change during the 1990s. What affects resulted from such changes?

SESSION #9 Oct. 3, 2006

Governance, Restraints and Conflicts of Interest

Read: GMC (Intro to Part IV, and

Chapter 9 Law and Regulation

“Our Schizophrenic Conception of the Business Corporation” by William T. Allen

“Double Agents in the Financial System,” by R C Smith

Study Questions:

1. Discuss the pros and cons of the “Global Settlement” of the top underwriting firms with NY State Attorney General Spitzer and the SEC? Why did the matter end in a settlement rather than go to trial?

2. What have been the consequences to the bankers and certain individual employees as a result of being caught up in the regulatory “crack down” that followed the market collapse of 2001-2002? Have these consequences been fairly applied, and do you expect them to act as a significant restraint of the actions of bankers in the future?

3. How would William Allen explain the current emphasis on corporate governance and tighter regulation of intermediaries?

SESSION #10 Oct. 5, 2006 [Term Papers Due]

Control by Law

Read:

“Prosecutors Tough New Tactics Turn Firms Against Employees,” by Laurie Cohen

“Life in a Federal Prosecutor’s Cross Hairs” by Ann Davis

“Living with the Organizational Sentencing Guidelines” by Jeffrey Kaplan, Linda S. Dakin, Melinda R. Smolin
“The revised Corporate Sentencing Guidelines,” by Jeffrey Kaplan

Study Questions:

1. How do you think the U.S. Sentencing Guidelines (and their recent revisions) will change corporate behavior? How are these guidelines determined, and how do they contrast with the corporate governance requirements of Sarbanes-Oxley?

2. What are the implications of the Corporate Sentencing Guidelines for the individual employee? Consider the situation of the Darling employees (“Pollution Case”) and Sharon Hogge (“Prosecutor’s Cross Hairs”). Also use your own intended career path as a basis for judgment and be as specific as you can.

3. Have the guidelines shifted too much power into the hands of public prosecutors? Do we otherwise have sufficient regulation of business and fiduciary conduct to make these enforcement powers superfluous? Who is responsible when prosecutors bring charges against businesses and individuals that are later thrown out or overturned?

SESSION #11  Oct. 10, 2006

The Future of Governance

Read: GMC

Chapter 10 and Chapter 11

Study Questions:

1. Has Sarbanes-Oxley struck the right balance of market regulation and self-governance? What are the regulatory costs that SOX imposes and to whom do they apply? Has SOX restored confidence in American capital markets?

2. What is the future of “enforcement competition” and of class action lawsuits? Do these restore confidence in American capital markets?

3. To whom among the players in capital markets do fiduciary liabilities apply? Are fiduciary liabilities well enforced at present? How?

4. Are there other governance models that Americans might look to as an alternative to our expensive regulatory capital markets system? How should conflicts be resolved in a well-regulated, healthy market system? Were they so resolved in the 1990s?
SESSION #12  Oct. 12, 2006

Social Responsibilities of Business

Read: Milton Friedman, “The Social Responsibility of Business is to Increase its Profits”

Study Questions:

1. What would Milton Friedman have to say about the corporate and financial scandals of the late 1990s?

2. How do corporations in the late 1990s compare with “institutional corporations” of the late 1960s? What does your crystal ball predict for corporations of the 2020s?

SESSION #13  October 17, 2006

Whistleblowing

Read: Kurt Eichenwald, “He Told, He Suffered, Now He’s a Hero”
Priscilla Budeiri, “The Return of Qui Tam”

Study Questions:

1. Under what circumstances would it make sense to become a whistleblower?

2. What should corporations do to employees to come forward with disclosures of harmful activities?