Stern School of Business Administration

Professional Responsibility (B02.3101)  
Markets, Ethics & Law

SYLLABUS

Term: Fall 2004  
Professor: Roy C. Smith

Time: T/TR 10:30-11:50  
Office: KMEC 7-89  
Phone: 8-0719

Classroom:  
Email: rsmith@stern.nyu.edu

Secretary: Gloria Asuncion   
Teaching Assistant: none
(gasuncio@stern.nyu.edu)

Objectives
The purpose of this course is to introduce the student to a broad range of “non-market” issues encountered by managers and business professionals, and to help the student develop a set of analytical perspectives for making judgments when such issues arise. In economics many of these issues can be described as market failures or imperfections. To a limited extent, we will illustrate how the legal system is used to redress such failures of the market economy. We will also examine the role of ethical norms and reasoning in resolving such issues in managerial life, and in establishing standards of professional responsibility.

More directly, the student in this course will exercise professional judgment through discussion and analysis. Most such exercises will require the analysis of one or more cases, as indicated on the attached schedule of class assignments. In addition, we will study writings in the fields of ethical reasoning, professional responsibility, and the law.

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
Each student should perform a written analysis for 5 study questions 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 pages in length. The student can submit more than 5 written analyses, but only the top 5 grades will count.
**Student Communications**  
Course information is posted on Blackboard

**Term Project**  
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:

**Professional Responsibility: Markets, Ethics, and Law**  
**Cases and Readings for 2004-2005**

The textbook is available in the NYU Professional Bookstore. *Note that the edition for the current academic year, 2004-05, is different from prior editions.* Make sure you have the current edition.
TERM PROJECT: 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. In any event, the requirements are that the situation raise ethical or legal issues and that the student was there. It would not be appropriate to analyze a situation if you were not in a position to observe it directly.

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 before session 10
TOPIC AND ASSIGNMENTS

SESSION #1  Introduction - Market Failures & Professional Dilemmas
DATE: Sept 7, 2004

Read: “The Price of Lobster Thermidor” from The Economist (p.365)

“Pollution Case Highlights Trend to Let Employees Take the Rap” by Dean Starkman (p.309)

“Economic Theories of Regulation: Normative v Positive” by Linda N. Edwards and Franklin R. Edwards (p.5)
(A. Economics of Market Failure)

“Making an Ethical Decision” by Terry Halbert and Elaine Ingulli (p.15)
(B. Ethical Theories)

Study Questions
1. Why do market failures tend to bring about law or regulation to counter their effects?

2. What market failures or imperfections are present in the “Lobster Thermidor” case? In the ‘Pollution’ case?

3. How might ethical methodology help an executive or legislator to make more effective decisions in the presence of market imperfections?

4. Based on the Halbert & Ingulli reading identify at least one market failure related to your employment situation and apply the methods of ethical reasoning to this market failure.

SESSION #2  Truth & Disclosure
DATE: Sept 9

Cases: “Bitter Pill” by Ralph T. King, Jr. (p.47)

“Familiar Refrain: Consultant’s Advice on Diversity was Anything but Diverse” by Douglas A. Blackmon (p.53)

“Today’s Analyst Often Wears Two Hats” by Roger Lowenstein (p.59)

“Heartfelt Advice, Hefty Fees” by Melody Petersen (p.61)

Read: “Is Business Bluffing Ethical?” by Albert Z. Carr (p.66)
“Ethics and the New Game Theory” by Gary Miller (p.26)

“Double Agents in the Financial System” by Roy C. Smith (p.71)

Study Questions
1. Would Albert Carr voice any objections to the (i) corporate actions of Boots described in “Bitter Pill” and (ii) Towers Perrin in the “Familiar Refrain” case? Do you agree with Carr? Can you identify any market failures in “Bitter Pill” and “Familiar Refrain”?

2. How would Gary Miller assess the long-term effects of bluffing as applied to (i) the job of an equity analyst (Lowenstein & Smith readings) and (ii) celebrity endorser (“Heartfelt Advice”)? Would Albert Carr agree?

3. Is there anything ethically wrong about the actions of Towers Perrin, as described in “Familiar Refrain”? What would happen if all or most consulting companies behaved in similar ways?

SESSION #3 Gifts, Side Deals & Conflicts of Interest
DATE: Sept 14

Cases: “Buynow Stores” by Bruce Buchanan (p.79)

“Roger Berg” by Ronald M. Green (p.82)

“Friends and Family” by Melanie Warner (p.84)

“Wall St. and the Nursery School: A New York Story” by Gretchen Morgenson and Pat McGeehan (p.94)

“Tobacco Industry Fought Drug’s Marketing “ by Kenneth Chang (p.97)

“U.S. Warns Drug Makers on Illegal Sales Practices by Robert Pear (p.99)

Read: “Neutral Omni-Partial Rule Making” by Ronald M. Green (p.22)

“Battling International Bribery 2001” (p.90)

“Code ‘Is Failing’ To Prevent Rich Companies from Bribing Officials” by Alan Beattie (p.88)

Visit: www.transparency.org

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.

3. Have tobacco and drug companies created any market failures or engaged in any conflicts of interest in their current marketing practices as presented in the Chang and Pear readings?

4. How should American executives respond when their foreign competitors are bribing officials in developing countries? Should they refrain and risk losing business? Or make the payment, perhaps through a series of intermediaries?

SESSION #4 Whistle Blowing & Loyalty
DATE: Sept 21

Cases: “Aircraft Brake Scandal” By Kermit Vandiver (p.149)

“He Told. He Suffered. Now He’s a Hero.” by Kurt Eichenwald (p.159)

“A Whistle-Blower Rocks an Industry” by Charles Haddad, with Amy Barrett (p.168)

“Doctor Explains Why He Blew the Whistle” by Melody Petersen (p.172)

“How Ex-Accountant Added Up To Trouble for Humbled Xerox” by James Bandler and Mark Maremont (p.176)

“Former Mattel Employee’s Battle Shows Whistle-Blowers Walking a Fine Line” by Michael Hitzik (p.180)

Read: “The Return of Qui Tam” by Priscilla R. Budeiri (p.183)

“States Passing Whistleblower Statutes” by Steve Seidenberg (p.174)

Study Questions
1. Consider the position of Searle Lawson in the “Aircraft Brake Scandal” case. At what point, if any, should he have blown the whistle to someone outside B.F. Goodrich? Use ethical concepts and reasoning to support your position.

2. Compare the situations in “A Whistle-Blower Rocks an Industry” and “Doctor Explains Why He Blew the Whistle” to “Aircraft Brake Scandal” and assess the role that *qui tam* laws play in resolving such situations.

3. Mark Jorgeson (“He Told He Suffered” - Prudential) and James Bingham
(“How Ex-Accountant” - Xerox) worked at major corporations where they tried to bring truthful accounting numbers to the attention of top management and investors. What personal risks did they run? And how did the outcomes of their cases differ with their approach to whistleblowing?

4. Is the Qui Tam policy is a good idea? Should corporations also use it; that is, should corporations offer rewards to employees who blow the whistle on their colleagues?

SESSION #5 Agency & Fiduciary Duty
DATE: Sept 23

Cases: “Quality Department Stores” by Lawrence Zicklin (p.103)
   “Old City Enterprises” by Lawrence Zicklin (p.104)
   “Plasma International” by TW. Zimmer and P.L.Preston (p.107)
   “You Bought, They Sold” by Mark Gimein (p.109)

Read: “Duties of Principals and Agents” By Kenneth Clarkson, et al. (p.116)
   “Moral Hazard” by Robert Pindyck and Daniel L. Rubenfeld (p.10)
   (A. Economics of Market Failure)

Study Questions
1. Sketch out the relationships between parties described or implied in the case “Quality Department Stores.” Which of these can be called “fiduciary” relationships? Justify your answers. Given your analysis, how should the investment manager vote?

2. Which fiduciary duties might be at issue in “Old City Enterprises” and in “Plasma International”? Are Ed Stevens in Old City and Sol Levin of Plasma acting properly in terms of shareholder interests as well as ethical standards? Are there any moral hazards present here?

3. Considering the Gimein reading (“You Bought, They Sold”) what are appropriate limits, if any, on sales of stock by corporate insiders? Does this behavior present any moral hazards, particularly to shareholders?

SESSION #6 Sales Ethics in Financial Markets
DATE: Sept 28

Cases: “Commissions on Sales at Brock Mason” by Tom L. Beauchamp (p.121)
“West Virginia CIF” by Ingo Walter (p.124)

“Responsibility, Yes -- but to Whom” by Larry Zicklin (p.128)


“Disorders made to Order” Brendan I. Koerner (p.133)

Read: “Investment Management: Business . . . or Profession and What Role Does the Law Play?” by John C. Bogle (p.140)

Study Questions
1. In the Brock Mason case, Mr. Tithe, the branch manager, describes the situation with the widow as “unfortunate” but not “unfair.” Do you agree? Use ethical methods and concepts to justify your position. How is the situation at Brock Mason similar to that at SSB described in “Outrage is Rising As Options Turn To Dust.”

2. Are there any material difference between the behavior of Jim Edwards, head trader, in “Responsibility Yes, but to Whom?” and Chung Wu, broker, in “The Man Who Paid the Price” in relationship to ethical responsibility and/or fiduciary duties?

3. In what ways, if any, could we determine that pharmaceutical companies are ethically responsible for promoting new mental illnesses in order to boost their profits from drug sales?

4. In his article, “Investment Management: Business . . . or Profession,” John Bogle implies that much of the mutual fund business is driven by moral hazards and agency problems. Do you agree? Justify your position.

SESSION #7 Trade Secrets
Date: Sept 30

Cases: “Stockbroker’s Story” by Bruce Buchanan (p.191)

“Fare Game” by William M. Carley (p.192)

“Corporate Spies: The Pizza Plot” by Adam L. Penenberg and Marc Barry (p.196)

“Foote Cone Loses Two Accounts From Coke in Wake of Pepsi Suit” by Suzanne Vranica (p.201)
Read: “Trade Secrets, Patents, and Morality” Robert E. Frederick & Milton Snoeyenbos (p.203)

“Protecting Trade Secrets: Using ‘Inevitable Misappropriation’ and The Exit Interview” by Michael B. Carlinsky & Lara Kreiger (p.209)

Study Questions:
1. Are customer records, such as those described in “Stockbroker’s Story” trade secrets, or do they belong to the departing broker? What criteria can we apply in making this determination?

2. How does the situation in “Fare Game” differ from the “Stockbroker’s Story” with respect to the idea of a trade secret?

3. What practices in “The Pizza Plot” do you judge to be inappropriate? What are your criteria for saying so?

SESSION #8 Management & Directors - Corporations & Shareholders
DATE: October 5

Cases: “The Hot Seat” by Joan Lubin (p.219)

“For Executives, Nest Egg is Wrapped in a Security Blanket” by David Leonhardt (p.223)

“Testing the Limits of the Business Judgment Rule” by Roger Leroy Miller & Gaylord Jentz (p.226)

“Manager’s Journal: Corporate Boards: A Director’s Cut” by Stanley Gold (p.227)

“Ready and Able?” by Phyllis Plitch (p.229)

“Sarbanes-Oxley: Danger for Directors” by Porcher L. Taylor III (p.234)

“How to Fix a Broken System: A Rush of New Plans Promise to Make Corporate Boards More Accountable: Will They Work?” by Carol Hymowitz (p.243)

“One Size Doesn’t Fit All: In Europe, Corporate Governance Rules Are Not in the Details” by Silvia Ascarelli (p.246)

“Caesar’s Cousin at the Big Board” from the Wall Street Journal (p.250)

“Sarbanes-Oxley Act: Coming Litigation Crisis” by John C. Coffee Jr. (p.252)
**Read:** “Our Schizophrenic Conception of the Business Corporation” by William T. Allen (p.255)

“Crisis of Corporate Ethics” by Roy C. Smith (p.268)

**Study Questions:**

1. According to William Allen which conception of the business corporation currently dominates the crisis in corporate governance and why?

2. Which market failures does the Sarbanes-Oxley Act address? What would be Smith’s (“Crisis of Corporate Ethics”) response to the Sarbanes-Oxley Act as a remedy for recent failures in corporate governance?

3. Taking into consideration the perspectives of Lubin (“The Hot Seat”), Leonhardt (“Nest Egg”) and Miller/Jentz (“Testing the Limits”) what reasonable methods might a Compensation Committee use to decide on executive pay, benefit and severance packages?

**SESSION #9 Insider Trading**

**DATE:** Oct. 7

**Cases:** “An Accountant’s Small Time Insider Trading” by Tom L. Beauchamp (p.277)

“Raymond Dirks and Equity Funding of America” by Roy C. Smith (p.295)

“Trading Room Ethics” by Lawrence Zicklin (p.284)

“The Case for Insider Trading” by Henry G. Manne (p.287)

“In Focus: Corporate Governance SEC Acts on Selective Disclosure” by Eric Dejong, Paul Sassalos and Stewart Landefeld (p.290)

**Read:** “The Cost of Inequity” The Economist (p.282)

“Insider Trading Notes” by Constance E. Bagley (p.298)

**Study Questions**

1. Should the accountant, Donald Davidson, trade on the information he has obtained from Warner Wolff? Use ethical concepts and methods to support your position.

2. Is Ray Dirks’ behavior consistent with the concept of fiduciary duty? Why was he reprimanded by the SEC but ultimately exonerated by the Supreme Court?
Use ethical concepts and methods to support your position.

3. Read “Trading Room Ethics” carefully and outline the exact procedure Teri Forman employs to move large blocks of stock. Is this insider trading? Why or why not?

4. Do laws forbidding insider trading make financial markets more or less efficient? Use ideas from both economics and ethics to justify your position as well as including Manne’s thesis (“The Case for Insider Trading”) on insider trading.

SESSION #10 Control by Law – TERM PAPERS DUE
DATE: Oct 12

Read: “Living with the Organizational Sentencing Guidelines” by Jeffrey Kaplan, Linda S. Dakin, Melinda R. Smolin (p.328)

“When the Company Becomes a Cop” by Linda Himelstein (p.307)

“Pollution Case Highlights Trend to Let Employees Take the Rap” by Dean Starkman (p.309)

“Life in a Federal Prosecutor’s Cross Hairs” by Ann Davis (p.311)

“DOJ Gets Tougher on Corporations” by Steve Seidenberg and Tamara Loomis (p.313)

“Corporate Crime: Government Seeks Tougher Sentences” by Sue Reisinger (p.316)

“Enough is Enough” by Clifton Leaf (p.318)

Study Questions:
1. How do you think the U.S. Sentencing Guidelines will change corporate behavior? Consider this from the perspective of the corporation in the Himelstein (“Company Becomes Cop”) and Starkman (“Pollution Case”) readings.

2. Are the compliance costs that the U.S. sentencing guidelines imply justified? Does Leaf (“Enough is Enough”) agree with the guideline’s approach to white-collar crime? Use ethical concepts and methods to support your position.

3. 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.
SESSION #11 Social Responsibility To Stakeholders  
DATE: Oct 14

**Cases:**  “Toy Maker Faces Dilemma as Water Gun Spurs Violence” by Joseph Pereira (p.341)

“Bally’s Grand Casino, For Elaine Cohen, Is Her One True Home” by Heidi Evans (p.343)

“Credit Card Companies Target New Niche: the Mentally Disabled” by Joseph Cahill (p.346)

“The Right Thing: When Good Ethics Aren’t Good Business” by Jeffrey Seglin (p.350)

“Cut Loose” by Anne-Marie Cusac (p.352)

**Read:** “The Social Responsibility of Business is to Increase Its Profits” by Milton Friedman (p.358)

“Restricted Reasons and Permissible Violation” by Arthur Isak Applbaum (p.19)

**Study Questions**

1. What advice would Milton Friedman give to the CEO of Larami Corp., manufacturer of the Super Soaker? Would you agree with him? Use ethical methods and concepts to support your position.

2. If you were the manager of Bally’s Grand Casino, would you do anything differently with respect to Elaine Cohen? Use ethical methods and concepts to support your position.

3. Did the CEO of Smith & Wesson fulfill his fiduciary duties? Justify your position. How would Arthur Applbaum (“Restricted Reasons and Permissible Violation”) judge his behavior?

4. Does IBM owe any duty to Fran Asbeck (“Cut Loose”) regarding his health care benefits upon retirement? How would Allen (Schizophrenic Conception of the Business Corporation) and Friedman (“Social Responsibility is to Increase Profits) respond to IBM’s behavior?

SESSION #12 Moral Standards Across Borders  
DATE: Oct 19

**Cases:** “The Oil Rig” by Joanne B. Ciulla (p.367)
“For Cruise Workers, Life is No Love Boat” by Joshua Harris Prager (p.369)

“Stretching Federal Labor Law Into South Pacific” by Seth Faison (p.371)

“Lives Held Cheap in Bangladesh Sweatshops” by Barry Bearak (p.375)

Read: “In Praise of Cheap Labor: Bad Jobs at Bad Wages Are Better than No Jobs at All” by Paul Krugman (p.380)

“Moral Minimums for Multinationals” by Thomas Donaldson (p.384)

**Study Questions**

1. Would Donaldson (“Moral Minimums”) feel that any basic human rights been violated in the “Oil Rig” case? Are the ex-pats justified in getting better treatment than the Angolans?

2. Should cruise workers that service US ports enjoy the rights of other US workers? Would Krugman (“Praise of Cheap Labor”) or any of the other ethical thinkers we have studied think that this was an unethical situation?

3. Should US labor and safety laws apply to the Northern Mariana Islands? Why or why not? Are sweatshops unethical according to Krugman or Donaldson or any other ethical methods that we have studied?

4. Donaldson argues for the existence of 10 basic human rights. Do human rights exist? If so, what responsibilities do corporations have to see that they are respected? And how would you apply these ideas to workers on cruise ships or in the Bangladesh sweatshops?

**SESSION #13 Product Liability**

**DATE: Oct 21**

**Cases:** “A.H. Robins: Dalkon Shield” by A. R. Gini & Terry Sullivan (p.399)

“The Class-Action Quandary: Cash Payment, No Apology” by Meryl Gordon (p.407)

*In Breast Implants Scandal, Where Was Dow Corning’s Concern for Women?” by Andrew W. Singer (p.409)*

“Will the Lawyers Kill Off Norplant?” by Gina Kolata (p.414)

“Legal Myths: The McDonald’s Hot Coffee Case” (p.419)

By J. Jones (p.421)

**Read:** “Strict Product Liability & Product Liability” by Kenneth W. Clarkson, et.al. (p.423)

“The Coase Theorem” by A. Mitchell Polinsky (p.8)

**Study Questions**

1. Should A.H. Robins have introduced the Dalkon Shield when it did? Why or why not? What method of ethical reasoning seems most appropriate to this problem? Why?

2. Was McDonald’s “negligent” in the “hot coffee” case? Should McDonald’s also be subject to “strict” product liability for selling “unreasonably dangerous” coffee? Does McDonald’s have any legal defenses? Can the judicial opinion in “Greene v Boddie Noell Enterprises, Inc.” be distinguished from the opinion in the McDonald’s case?

3. Can you draw any distinctions between the Dalkon Shield, Norplant and breast implant cases? Are moral hazards present in these cases or in product liability cases in general?

**SESSION #14 Discrimination & Privacy**

**DATE:** Oct 26

**Discrimination Cases:**

“Foreign Assignment” by Thomas Dunfee and Diana Robertson (p.431)

“Now Look Who’s Taunting. Now Look Who’s Suing” by Jane Gross (p.433)

“When Fear of Firing Deters Hiring” by Jeffrey L. Seglin (p.436)

“Is this the Right Time to Come Out?” by Alistair D. Williamson (p.438)

“Too Old to Work?” by Adam Cohen (p.447)

**Read:** “EEOC Guidelines Excerpt” (p.443)

“Sexual-Orientation Protection Added to New York Law” by Casey J. Dickinson (p.454)

“McKinney’s Consolidated Laws of New York” (p. 456)

**Discrimination Study Questions**
1. In the “Foreign Assignment” case, how would you judge the actions of Bill Vitam? Use ethical concepts and methods, as well as the law, to justify your position. Can the bank (employer) be held liable, according to the EEOC, for the sexually harassing behavior of its employees? Does the bank have any defenses?

2. Is sexual harassment against men a legitimate concern? Is the situation at Jenny Craig comparable to that in Foreign Assignment? Why or why not?

3. If a group such as white males is over-represented in terms of demographic proportions within certain executive job categories, can a firm actively favor women or non-whites in filling future vacancies? And if so, what are the criteria?

4. Is discrimination because of sexual orientation different from discrimination because of sex? Should similar laws and regulations be applied to both? Justify your position.

**Privacy Cases:** “Monday 9:01 A.M.” by Ronald H. Smithies (p.461)

“Open Secrets” by Ellen E. Schultz (p.462)

“Prying Times” by Ann Carrns (p.466)

“Monitoring of Employees Still Growing” by Allison Michael and Scott M. Lidman (p.470)

“Free Prozac in the Junk Mail Draws a Lawsuit” by Adam Liptak (p. 484)

“TGB Insurance Services Corp. v. Superior Court (p.487)

**Read:** “HIPAA Privacy Rule to Go Into Effect” by Michael N. Mercurio (p.475)

“’Privacy Procrastination: HIPAA Rules Are Now In Effect, Yet Few Companies Are in Compliance’ by Tamara Loomis (p.479)

“HIPAA: New Federal Privacy Rules and Their Implications” by Nick Littlefield and Colin Zick (p.482)

**Privacy Study Questions:**

1. Should firms face any restrictions on the internal use of data gathered from their own employees? Why or why not? Consider this specifically with respect to medical/psychological information. Use ethical concepts and methods to justify your position.

2. Is the idea of privacy for individuals becoming obsolete in the Internet age? How do privacy and technology interact?
3. What market failures surround the issue of privacy? How, then, does the right to privacy interact with economic efficiency?

4. (A) Draft a policy guideline for a firm as to what aspects of its employees lives are to be considered private, along with applicable safeguards. Assume this memo will be distributed to all employees, both current and prospective. (B) Briefly state your reasoning in setting this policy.