

# TRUST and HONESTY

AMERICA'S BUSINESS CULTURE  
AT A CROSSROAD

TAMAR FRANKEL

# *Trust and Honesty*

America's Business Culture at a Crossroad

Tamar Frankel

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## Preface

WHEN I WAS YOUNGER, I used to take a long walk after my birthday festivities. The gifts were examined and enjoyed, the candles were blown, and the cake was eaten. It was time for reflecting. As I walked, I used to ask myself: What has happened to me during the past year, and where was I heading? The many things that happened—both good and bad—were unanticipated. I took them in stride without much thought. They became part of my life and I adjusted to them, often unknowingly. Now it was time to bring these events and my own behavior to the fore. It was time to think about them consciously. As I grew older, I recognize that this walk need not take place on birthdays only. From time to time, it is important to stop and take stock.

This book invites you, the reader, to take this kind of a long walk. Where was trust and honesty in America in the past, and where it is going? But wait! Is this walk necessary? Who would object to trust and honesty? After all, reputation for honesty is valuable and advantageous. Everyone knows that trust and honesty are important in both personal and business relationships.

And yet, why does talk about these virtues sound like the “Sermon from the Mount,” a “holier than thou” speech? Why does it “feel” divorced from “reality” and why is seeking trust and honesty viewed by some people as “hopeless”? There is a nagging suspicion that reality is not about being honest but about seeming to be honest; that reality is about discovering what is behind the façade of honesty, because surely such a façade exists. It is tiring and tiresome to live in such a reality, with innuendoes and vague signals raising anxious concerns that what we see is not what truly is.

Just the other day, I received a card to be opened immediately, by “American Senior Alliance,” P.O. Box 100125, Marietta, GA, 30061-9900. It notifies senior citizens of changes in the law, offers help, and seeks information. Tucker Sutherland, editor of *Senior Journal*, suggests that this organization “should be viewed with caution” because “no one has been able to locate this company.” He advises “seniors not respond to the mailing” (see the website available online at [<http://seniorjournal.com/NEWS/Features/4-111-30AmSrAllicanc.htm>]). This card was received a year ago, but fraudulent

e-mails seeking information “to update” my accounts (which I do not have) continue to arrive. And little has changed, except that we might become jaded and used to this. Seniors and citizens must be careful; check and recheck actions and publications by “strangers.” Do not trust—verify! This is a tiring, tiresome, and “hopeless” reality.

And yet, we have some power over our reality. We are the ones who shape our relationships with others. And even though we cannot dictate the behavior of everyone, we can influence how we, as well as others, would behave: We are not merely followers but also leaders. Make no mistake about it. We might imitate the behavior of others, but others follow our behavior, be they our children, our students, our spouses, our peers, and sometimes our superiors and the public. Our reaction to the above advertising may change the behavior of the people who wrote the advertising and the behavior of seniors generally. If this is a sham organization, people need not wait for the government to find the senders of the advertising, and to punish them for trying to defraud helpless people. If the millions of potential victims decide to help enforce trust and honesty, they present a formidable force that can do part of the job. Few can become policemen. But many more can work hard to change attitudes, both their own and others.

This book is about the empowerment of those who would like to see America moving toward a higher level of trust and honesty. It invites the reader to take the long walk and reflect on where America is today, where America is going, and—if the direction is wrong—what the reader can do about it.

## Acknowledgments

BOOKS OFFER NEW IDEAS and draw on existing ideas. I am grateful to so many: the writers whose books and articles I read, and the colleagues who offered me their thoughts and suggestions, and helped to bring this book to fruition. Professors Diego Gambetta, Colin Mayer, and Avner Offer of Oxford University and Professor Peter Tufano of the Harvard Business School opened new doors to the insights of other disciplines. Professor Larry Cunningham of Boston College, Professor Duncan Kennedy of the Harvard Law School, Mr. Rajeev Bhattacharya, and Dean Ronald Cass and my colleagues at the Boston University Law School contributed their knowledge, understandings, and, best of all—their supportive criticism. Ann Rutledge and Ed and Mary Weyhing offered their very helpful reactions.

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When I am tired and discouraged, I am sustained by the thoughts of my two children, Anat Bird and Michael Frankel, and contact with them and with my grandchildren Guy and Assi Yalif, Paul, Liat, Gil, and Arik Bird. Thinking of them and talking to them gives infinite joy and energy. A special place in my life and work belongs to my husband, Ray. He has always offered unbiased opinions and wonderfully warm and steady support. To all I am very grateful.

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# Trust and Honesty





## Introduction

THE INITIAL TITLE of this book was “Abuse of Trust.” Then news about frauds, which started as a trickle, grew to a downpour. And as I continued my research, it became clear that something different from the past and more basic has been happening to America. It is that America is *becoming used to* abuse of trust and deception. It is that American culture has been moving toward dishonesty, regardless of whether fraud has been actually rising. And that became the focus and title of this book.

Culture reflects the habits of society; at its base is a set of assumptions that we take for granted about how people behave. Like habits, culture develops with repetition, and with increasingly automatic behavior. This behavior becomes more comfortable and predictable. Eventually it is “understood without saying.”

What convinced me of this culture trend? There is no comprehensive study on all people’s sentiments. There is no decisive database that compares today’s fraud in America with fraud in the past. But newspapers, magazines, court cases, and studies point to spreading and rising fraud in America. Deception covers the population in all walks of life: management and employees; Main Street and Wall Street corporations; lawyers, accountants, and physicians. More individuals cheat in healthcare and insurance claims. More young people cheat in school examinations and in sports. More job applicants cheat on their resumes. More people and businesses defraud more vulnerable consumers. Fraud has contaminated science, journalism, newspaper management, the professions, and the financial infrastructure. Chapter 1 in part I of this book documents these findings, and the counterarguments that there is nothing new in the recent developments.

Events alone, however shocking, do not change a culture, unless they affect general attitudes. I found evidence of a move toward greater acceptance of dishonesty as a “way of life” and toward justifications—“dishonesty is not that bad.” There are even attempts by some leaders and their advocates to redefine fraud out of existence. For example, there are arguments that shareholders are not the owners of corporations. Therefore, directors can serve other interests without breaching their duties

to the shareholders. The final stage in this process would be a culture in which dishonesty is taken for granted, and no one can imagine any other order of things or alternative behavior. If America reaches this final stage, then what we consider to be fraudulent behavior today will be the natural and smart way to behave. America is not yet there, but it is moving in that direction.

The change in culture, like the change in habit, does not happen overnight. It evolves. Between assumptions that harden into an automatic habit and no assumptions at all, there is a direction that culture takes. American culture has been moving in the direction of dishonesty for some time. It took more than three decades to plant and nurture the seeds that produced the fruits of the 1990s. Chapters 5–8 show the shifting balance between temptations and opportunities to defraud on the one hand and the barriers against abuse of trust on the other. During the past 30 years, and especially in the 1990s, these temptations and opportunities have risen while the barriers have fallen.

The regulation of trusted persons was diluted. The prohibitions on abuse of trust and fraud were weakened. Lawyers, businesspersons, government regulators, and legislators denigrated the law to a greater extent than before. The markets were put on a higher pedestal than before. Self-interest and individualism were exalted at the expense of commitment to society. The professions, such as physicians and lawyers who should have acted in the public service first and sought compensation second, turned into businesses whose first and foremost goal is sale for profit. Moral behavior—withstanding temptation even if there are no police around—is no longer a virtue. And, as the materials in chapters 8–11 demonstrate, the enforcement and punishments of white-collar criminals have been weak and reporting of abuse of trust even weaker.

Culture, trust, deception, and their synonyms mean relationships, as chapters 2–4 analyze. We may speak metaphorically of a person who trusts his self-control or deceives himself. But in this book, *trust* and *mistrust*, *honesty*, *dishonesty*, *cheating*, and *deceiving* mean relationships among people. Throughout the book I use these synonyms interchangeably—*honesty* and *trust*, and their opposites: *dishonesty*, and *distrust*, *deception*, and *fraud*. These words have different flavors but point to a direction. Honesty relates to integrity and openness toward other people, while dishonesty represents the opposite: deceit, corruption, shame, cheating, and duplicity toward others. Trust is based on belief in other people, while distrust and mistrust represent the opposite: disbelief, doubts, and suspicions of others.

As the large number of these synonyms shows, people's relationships are not identical. There are gray areas between clear-cut situations on which most, if not all, people would agree. There are gray areas between unqualified trust and unquestioned abuse of trust, between absolutely honest and truthful communication and clear deceit. Within these areas, one can move in small steps, one at a time, from honesty to dishonesty. One can shift in small steps, one at a time, from truth to deception. And one can slip and creep, in small steps, from trustworthiness to abuse of trust.

The rise and spread of dishonesty can be slow and gradual. Like aging, it can be hard to see the difference unless you come across an old picture and face the change. The comparison can shock, as one recognizes the old self. A picture of today's culture can shock, as one recognizes the current direction of America and its maturing into a culture of dishonesty.

Does all this seem obvious to you, the reader? Do you remember recent episodes in your everyday life that point to the danger of a dishonest culture? Do you recall in the workplace and among friends the admiration for people who know how to use dishonesty (or shades of dishonesty) to their advantage and "get away with it?"

Still, you may ask: "Why should I care? How does this story affect me? So what if smart people know how to finagle benefits for themselves at the expense of stupid people, or just devise a new misleading way to catch unaware buyers in the net? Let the people beware."

You should care, because dishonesty and mistrust are not free. Their cost can destroy the foundation of our economy and prosperity. See the signs of mistrust around you. There was a time when the doctor's advice was sufficient for both patient and doctor. Now the patient seeks a second opinion, and the doctor and the hospital require the patient to sign waivers of all sorts. The patient will mistrust the doctor; the doctor will mistrust the patient. Blaming the litigation bar and the high insurance costs, doctors have begun to investigate new patients to determine their "litigation past," and some doctors refuse to treat litigation lawyers. All these special protections cost the parties, the doctors, and, in the final analysis, the economy. Mistrust corrodes the wheels of exchange and commerce and contaminates trusted professional services. We can still recognize the symptoms. When they become automatic habits, we will accept them without thought or recognition. And we will pay the price without remembering the alternatives.

Some people may say: "Even suppose all this is true, what can one person do? Besides, no matter what we do, nothing will change." But this is not the American way. Whether things will change depends not only on the leadership but also on the citizens. In this country, leaders are not anointed. They rise from among the population. The population decides.

Make no mistake about it. America will continue to have its con artists, rogue brokers, and powerful white-collar abusers of trust. That will not change. What should change are the general attitude and the tolerance of dishonesty. What should change is the direction of America's culture to an *aspiration to honesty*, an aspiration that "goes without saying." Attitude and aspiration redirect and transform culture.

America needs a better balance of pressures and a healthier perspective. Ideologies and rigid dogmas should give way to a middle ground. There is a balance between self-interest on the one hand and morality and altruism on the other; between taking and giving; between individualism and a commitment to society; between rigid ideology and an ideal of honesty—even if it can never be fully reached. People are

not only self-interested; society is not only a market, and relationships are not only an exchange. Moral people who withstand temptation are not stupid. Their attitudes are crucial to a prosperous society. Greed is not good. It destroys the greedy persons and those around them. Law is not the enemy of business. It is the enemy of *crooked business*. Law does not necessarily undermine free markets and competition. It can protect free markets from *competition by deception*.

Most Americans practice this balance. Most Americans are honest and compassionate—they take but also give; they are self-interested but also committed to others and to America. How come they are moving toward a society and a leadership that fails to resemble them? How come too many Americans, including the younger generation, have begun to accept less honesty?

One explanation is rooted in the behavior of most Americans. Gradually and increasingly, the people have abdicated their power to political, financial, and academic leaders who have not been in sync with the public's inclinations. The honest majority of Americans have remained passive. The fraudulent minority has grown, taken the lead, exploited, and corrupted.

Therefore, the American people can redirect America's culture if they get involved. If Americans have had enough of financial abuse and exploitation, and if they are concerned about the effect of mistrust and fraud on their children, the population, and the economy, they can demand of their leaders and of each other more honesty and less cynicism, more trust and less doubting. Rather than follow, Americans can lead this country to reject the actions, attitudes, theories, and assumptions that brought us the 1990s.

*PART I*

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*The Eroding Trust, Truth,  
and Culture of Honesty*



## *The Spreading Abuse of Trust and Deception*

ABUSE OF TRUST has spread throughout America. It has covered corporations and individuals; sellers and consumers; leaders and followers; young and mature. It has touched activities that had been “clean” and self-regulating, such as science and journalism. And it seems that many of these abuses have been on the rise.

### THE DISCOVERIES OF SCANDALOUS BEHAVIOR IN THE 1990S

In 2001, America woke up to the astonishing discovery of Enron Corporation’s failure. Mimi Swartz and Sherron Watkins reveal a pattern of mistakes, arrogance, and deception leaving behind the fundamentals of business and emerging as fraudulent images that mimic truth [Swartz & Watkins]. Since the Enron discovery, embezzlement, fraud, and incredible avarice—sometimes heartless and grasping—have been uncovered in other corporations, springing and spreading from the country’s largest firms to large mutual funds, insurance brokers, securities analysts, and securities brokers, and involving, directly or indirectly, a number of their top management.

The news kept pouring in. In 15 months, WorldCom padded its accounts to the tune of \$3.9 billion. The company also developed a practice of “rolling revenue,” that is, registering the same sale many times over to inflate the revenues and its stock price. At the same time, the practice depleted the company’s assets by paying the salespersons “rolling” commissions, that is, multiple commissions for the same sale.<sup>1</sup> Xerox Corporation overstated its profits by \$1.4 billion.<sup>2</sup> The Federal Home Loan Mortgage Corporation (Freddie Mac) understated its gains by about \$5 billion.<sup>3</sup>

There were allegations that large corporations defrauded each other. Among these allegations was that WorldCom has been rerouting telephone calls, and defrauding its competitors of hundreds of millions of dollars during a nine-year period.<sup>4</sup> This accounting fraud was alleged to amount to over \$9 billion.<sup>5</sup> Boeing Corporation won a large contract with the Air Force by using documents that had been stolen from



Lockheed (a bidding competitor for the contract). And HealthSouth officials pleaded guilty to charges of fraud.<sup>6</sup>

Large contractors corrupted government officials. Boeing was further accused of having received proprietary pricing data from Darleen Druyun, an Air Force official who later went to work for Boeing.<sup>7</sup> Darleen Druyun, who controlled a \$30 billion annual procurement budget of the military, pleaded guilty to a federal charge of conspiracy to obstruct justice. She tried to cover up the fact that she brokered an executive position with Boeing Corporation paying \$250,000 a year when she signed, on behalf of the Air Force, a \$20 billion contract for Boeing.<sup>8</sup> Boeing's chief financial officer "pleaded guilty to illegally negotiating an executive job" for Druyun "while she still had authority over billions of dollars in Boeing contracts." He promised to "help federal prosecutors investigate ethical issues at the highest levels of the company," and he might face a six-month prison sentence.<sup>9</sup>

Other large corporations have violated the government bidding rules. Since 1990, General Electric paid about \$1 billion in fines for 87 alleged or actual violations. "Lockheed Martin has paid over \$426 million for 84 alleged or real misdeeds. Boeing has 50 counts on its record and \$378 million in payouts. Northrop Grumman, Raytheon, United Technologies, General Motors, Textron and TRW are not far behind."<sup>10</sup> Halliburton, a large oil company, was accused of overcharging the U.S. army by about \$61 million for gasoline in Iraq.<sup>11</sup> A month later, the firm was accused of overcharging the U.S. government for meals served to American troops in Iraq and Kuwait.<sup>12</sup> A large corporation corrupted officials in other countries. Xerox Corporation was accused of making "improper payments" to the tune of \$600,000 to \$700,000 to government officials in India in order to increase sales in that country.<sup>13</sup>

Citigroup and J. P. Morgan were accused of helping Enron Corporation to hide manipulations of its financial statements. These two financial institutions paid \$305 million to settle a case against them. The Canadian bank CIBC was fined \$80 million for helping Enron's financial machinations.<sup>14</sup> On June 22, 2004, came the news of price-fixing investigations in the chemical industry: "Corporate Whistle-Blowers Win Prosecutors' Amnesty, Help Widen Scope of Probes." A two-year-old investigation revealed "just the tip of the iceberg" and has been broadened considerably. The fines have risen from \$5 million, which was the maximum for a single Sherman Act criminal count 10 years ago, to \$10 million or more against 40 corporate defendants and one individual. The five largest fines ranged from \$110 million to \$500 million.<sup>15</sup>

In mid-2003 came the discoveries of abuses by mutual fund advisers, who prided themselves on being "clean." For decades, that pride was earned. But in the 1990s, fund managers offered insider information and allowed preferred customers to profit from transactions in fund shares at the expense of other long-term fund investors. Fund managers and advisers benefited from these practices in various ways, and some personally participated in the practices. Investigations into mutual funds' abusive trading practices were followed by charges of fraud, resignations, and dismissals.<sup>16</sup>