White-collar Crime in Relation to the Financial Sector

An important topic in today's business world is white-collar crime. This can include a number of certain illegal actions, but within the financial sector, insider trading is prominent. Insider trading includes illegal buying and selling of securities as well as legal conduct. Corporate employees are legally able to buy and sell stock of their company shares and report this to the SEC (Securities and Exchange Commission). Illegal insider trading signifies the use of nonpublic information or misappropriation of that knowledge. These actions undermine the integrity of the investing markets and therefore illegal insider trading is considered a serious crime with adequate punishment (United States Securities and Exchange Commission, 2013). An example of illegal insider trading would be when an employee who currently invests in their company's stock comes across confidential, nonpublic company information pertinent to how the stock price will change in the future. This could be through any means, including a tippee or accidentally overhearing a conversation. The employee then buys or sells shares using that information. This gives that investor a great advantage over other investors. However, the legal sort of insider trading is slightly different. Without any sort of fraud or misappropriation of information, there are no repercussions. Employees can trade company stock and notify the SEC when they do so to ensure their trades are accounted for. As long as the trades are not based off of any nonpublic or disclosed information that was traded, the trades are considered legal. This paper addresses the legal sort of insider trading. Many employees engage in investing in shares of their organization, especially if this organization is growing or maintaining value well. Employees can also be given shares of company stock as compensation. The main goal of investing is to maximize the value of your original investment, so investors want to make sound decisions based off of their research and knowledge of the markets. The question being addressed here is, "Is it ethical for a middle manager to buy or sell personal shares of company stock when they anticipate an increase or decrease in the stock's price based on their experience with and insight of their company?" This paper is focusing on the 'based on experience with and insight if their company' phrase of the question. Instead of a more controversial topic of insider trading where an individual tips off another in return for a certain reward of benefit, this is about one individual who uses their own knowledge to make trades.

The laws for insider trading are constantly in review, even today. One law regarding information one might receive states, "…regardless of their motivation or occupation come into possession of material corporate information that they know is confidential and know or should know came from a corporate insider, they must either publicly disclose that information or refrain from trading" (Eisenberg, Hastings, and Porter, 2016). This law basically lays out that when an employee makes a trade, they need to report it to the SEC. Some instances that can become legal issues include when employees of a corporation or even their friends, family, or any ‘tippees’ uses confidential business information to buy or sell stock. It is also illegal for business partners of an organization to be given information about the market in exchange for services. There are also specific laws pertaining to non-business relationships and how those relationships can determine if a person is guilty of illegal insider trading (United States Securities and Exchange Commission, 2013). Insider trading is prevalent more so today than before, with nearly 25% of trades coming from insider information (United States Securities and Exchange Commission, 2013).

Insider trading causes most tension with the government, considering most actions are illegal. However, the question being addressed speaks to a different side of insider trading. The tension exists where one trading party has an advantage, and therefore a greater chance of making more money, than another. This advantage is based off of knowledge and experience, which is not in any ways illegal to have. However, when a company employee does have great knowledge of their company and experience from working there, should they be able to use that to trade their shares of company stock? This is where tension is created. Some people believe that it is not fair for some to use that kind of information, even though it is not misappropriated, to their own personal advantage within the stock markets. To determine who exactly would be affected by these acts of insider trading, one must evaluate the stakeholders.

The stakeholders who would be a part of this ethical dilemma would be the employees (investors using their experience), other investors (without the same experience), the organization as a whole, the government, economy, and financial institutions. The stakeholders directly affected are considered primary stakeholders. The primary stakeholders would be the employees who are actively insider trading as well as the investors who are trading but do not have the same knowledge. On the other hand, there are stakeholders that are considered secondary because they are not directly affected by the actions or decisions in this situation. The secondary stakeholders would be the organization, the government, economy, and financial institutions. The primary stakeholders are the employees of companies that gain knowledge and experience through their years and work done at that particular company. The insight of the company being referred to is not specific, as it differs for each individual as well as the company. Another primary stakeholder would be the other investors in the market, whether that be other employees in the same company or other investors in the same stock. These people are affected by the advantage the employees using company experience have. Those employees have the upper hand on whether or not the stock price will decline or rise, where the other investors in the stock market do not have the same type of knowledge. With their disadvantage, the investors could lose a significant portion of their investment.

Each stakeholder has significant moral impacts regarding the ethics of insider trading. For the primary stakeholders, the employee engaging in the insider trading is benefitting from the actions. The employee is using their gained knowledge or insight to improve the value of their stock. With their experience with the company, the employee will be able to anticipate an increase or decrease in the stock’s price and therefore sell or buy accordingly. This will ultimately cause them to either gain more money through the stock, or to refrain from losing a large sum if that is the case. This gives the employee somewhat financial stability, as long as their insight of the company serves them correctly. It is possible the employee might invest incorrectly and then lose money, which would be harming them instead. But mostly this will help the investor to increase the value of their shares of stock. The employee is also exercising their right to own and trade their personal shares of stock according to their level of expertise. There is no misappropriation or fraud involved in this situation, and therefore the employer has a right to do so. On the other hand, the individuals investing alongside that particular employee can potentially be harmed or benefitted, according to the markets. However, those investors do not have the same exact insight of the company and therefore are being harmed by having less knowledge. These investors might not be able to anticipate an increase or decrease in price and might end up losing large amounts of money had they been more aware of the company.

The moral impacts to the secondary stakeholders depend a lot on what the financial markets look like, considering they could lose or gain money independent of what a single investor chooses to do. The company would be affected by the decision if the employees and their investments. The company is exercising their right to give employees shares of stock and letting those employees invest. This would benefit the company by adding value to their market shares. The economy as a whole can change by market manipulations, however, that topic is not addressed in this specific ethical question. The government is secondhandedly affected and is definitely exercising their rights in regulating the securities market. This is the government’s responsibility to seek and punish illegal behavior to keep the market honest. The government is also benefitting by keeping order. The economy would be impact as well, either with a harm or a benefit. Different studies show how insider trading effects the financial markets. These studies contain two conclusions, that insider trading either benefits or harms the economy as a whole. Engelen and Liedekerke show in their journal that a reduction of insider trading will in turn reduce market efficiency. However, during real trading it is difficult to determine between a sort of trading that enhances market efficiency like insider trading, or one that reduces efficiency, like market manipulation (2007). Even with multiple studies and opinions on this topic, it is undiscernible to conclude which type of securities affect what. Many people come to their own conclusions about how insider trading effects the overall market. Most agree with the theory that illegal insider trading, or market manipulation, will hurt market efficiency and decrease value. However, the legal sort of insider trading is basically increasing market efficiency and value. There is no fraud or deception occurring, so it occurs as normal investing would occur. The economy would benefit from the value of stock and money increasing, or the economy would be harmed if the value fell. Financial institutions would be effected in the same way the economy would be—either harmed or benefitted according to how the markets play out.

Insider trading was explained regarding the ethical question, “Is it ethical for a middle manager to buy or sell personal shares of company stock when they anticipate an increase or decrease in the stock’s price based on their experience with and insight of their company?” This sort of trading is legal for businesspeople versus the more controversial illegal insider trading. The term of insider trading was defined as the illegal buying and selling of shares as well as how corporate employees can trade shares legally by reporting to the SEC. However, legal insider trading is what is being addressed. Employees can use their own knowledge and experience to buy and sell shares of personal stock. The tensions lay within the investors regarding who has the competitive advantage and who does not. The main and primary stakeholders include the employees of the company investing in company shares using their experience to make decisions as well as the other investors in the same stock that do not have the same kind of company knowledge. The next steps needing to be taken are to determine if insider trading is ethical or not. This paper consists of three elements including: economic outcomes, legal requirements, and ethical duty systems. These three elements are used as steps taken to come to a conclusion about the ethicality of the question being asked.

The economic outcomes of this ethical questions can by outlined by a certain model. The Freidman model fits this ethical question the best. This economic outcome model, also named the shareholder model, emphasizes profits. There are three main points to this model. One states that corporations cannot hold social responsibility. This means that only people as individuals can have social responsibility. The second point states that employees cannot make the company socially responsible. This is because within a company, employees and employers have a principal-agent relationship. The employer is the principal that delegates responsibilities to the agent, which is the employee. The employees, as agents, have a direct responsibility to answer to the principal which is the employer. The responsibility of the agent is to conduct business in accordance with the desires of the owners, or employers. This desire is to make as much money as possible and maximize profits while being in accordance with the law without deception or fraud. The third point is that individuals can have social responsibilities. It is a person’s right and choice to have those social responsibilities because it is an individual’s choice what they do in their free time and with their own money. Every stakeholder within the company should be able to choose where or when they spend money. This does not mean an individual can make a company social responsible because the corporate responsibility is separate from its employee’s individual responsibility. However, the sole social responsibility for a business is increasing profits while staying within the boundaries of law without deception or fraud. If some sort of social responsibility generates goodwill as a byproduct of expenditures that leads to an increase in profits, then the social responsibility is beneficial in the long run. This type of goodwill can be defined as creating a reputation of a business that is used as an asset in order to create higher company value. This makes sense from a shareholder viewpoint if the goodwill individuals create increases the company’s profits, as long as it is in correlation with the principal’s desires for the business.

This economic outcome model fits best for the ethical question regarding insider trading. Friedman's model focuses on profits, which is essentially the focus for insider trading. The only reason individuals take part in buying or selling shares is to increase their profits. They can potentially use as much information as they can to give themselves competitive advantage over other traders in order to increase their own profits. The employee who is making the trades and buying shares of stock is their own principal and has the ability to take action in the ways they deem most profitable. Even when the employee receives shares of company stock as compensation, they still invest in attempts to make the most money. In this way, the trader of stock can be considered a 'business,' since they are working to make a profit. This 'business' does not need to be socially responsible because it exists to create value for the owners (the trader). The second point of the Friedman model states that employees cannot make the company socially responsible. This supports the idea that the individual that is trading shares does not need to be socially responsible to others and can use the insight from their work experience to make trades. Even though other traders of the stock do not have the same knowledge, the individual with the experience should be able to use that to make educated trades under this model. Social responsibility is not taken into account within the business community and profits are the most important aspect. Even though an individual has the right to have social responsibilities, they also have the choice to exercise or deny that right. That takes into account Friedman's third point of his model. The overall goal is to maximize profits within the boundaries of the law without deception or fraud. This ethical question of this legal type of insider trading completes this goal. Insider trading using unique company experience does in fact complete the goal of maximizing profits for the 'business.' This type of insider trading also complies with all laws, with the individual using only their knowledge and not participating in any illegal activities regarding trading shares. There is no deception in this case because the employee is publicly known to be working for the specific company and they must comply with SEC regulations and report to the SEC with trade information. I consider this type of insider trading that this ethical question addresses fits best within the Friedman model of economic outcomes primarily because both emphasize maximizing profits. I agree with the focus on maximizing profits legally. Regarding this economic outcome model, insider trading is deemed ethical.

Insider trading consists of various situations and circumstances regarding individuals within the business community. Certain types of insider trading are illegal and others are not. This all depends on what information is being used to trade shares and where exactly that information came from. Legality also depends upon if the individual buying or selling shares reports their actions to the SEC. The laws upheld by the government are constantly being reviewed and changed from case to case, but some have been around for a number of years. The Securities Act of 1933 sets requirements that investors must comply with by registering with the government (SEC). The main form of illegal insider trading is security fraud. This includes a multitude of different situations including using untrue information to obtain money or practice deceit upon the purchaser of any security. Another section states that it is unlawful for anyone to trade a security for consideration without formally disclosing the receipt. There are some exemption, such as the Accredited Investor Exemption. This exempts those who have financial expertise from their own experience and insight to make informed investment decisions. This is decided on a scale of financial sophistication, knowledge, and experience (United States Securities and Exchange Commission, 2013). This would many times apply to the employee who is trading the shares of company stock, since that investor has the means to be highly educated and able to make intelligent investment decisions. This is definitely taking into account the legal side of insider trading. The government also takes into consideration the information being traded as well as business relationships and non-business relations. This can be considered security fraud if the information is confidential and non-public. However, those laws only pertain to an individual partaking in the illegal sort of insider trading.

The type of insider trading the ethical question addresses is considered legal by the standards of the United States law. An employee using their own experience and insight to buy and sell personal shares of company stock is complying with the standards set by the government. This is completely legal according to the law because the information they hold is technically not confidential and could be publicly known. Other employees are privy to the same information. This allows employees to use insider trading legally as long as they still report to the SEC. Accredited Investors are even exempt from explicitly reporting the receipts, considering that they have extensive financial expertise in the markets. The sort of insider trading this ethical question addressed in the paper is of the legal variety, instead of the illegal kind that pertains to many more, complex laws that do not apply to this situation. Therefore, insider trading as defined by this paper is determined to be not only legal, but ethical.

When individual employees are faced with ethical decisions, they must use an ethical system based upon their personal beliefs or life experiences to come to the best decision possible. Individuals can use ethical duty systems, where there are key points that provide guidance in making a hard decision. However, these systems all have certain flaws about them that leave some issues unaddressed. This makes it necessary to take multiple duty systems into consideration to make a fully educated decision from looking at the issues from multiple viewpoints. All of the duty systems provide a decent way of concluding what duties individuals believe they owe other people based upon rational thought processes. Most of these systems use the principles approach, which looks for some type of underlying universal principles that provide a solid foundation to base decisions on. The two systems that I like the best that also apply to insider trading is the Principles of Universal Duties and the Utilitarianism System.

The Principles of Universal Duties is an ethical duty system in which one can use as a base to make a decision when faced with an ethical issue. This system is mainly contributed by Immanuel Kant. The main principle in making decisions is to never take any action or make any decision that you would not want to see others do or make in the same situation. This principle is deontological, which focuses on the duties. The advantages of this system is that it is universal and creates respect for people because it is based upon the reasoning behind what is considered right and what is considered wrong. All of a person's actions are taken into account leading up to the decision and consequences of that decision. A guiding principle is necessary when determining right from wrong because nothing in life is an absolute good except a person's good will. This good will is very different from the previous mentioned 'goodwill' in the business world. An individual's good will takes into account their positive intent, beneficial desire, and their recognized duty to help others. This is challenging to determine, however, because good will is internal and privatized within the individual. The Principles of Universal Duties consists of three moral principles that are considered categorical imperatives. The first is that people must act only on reasons that they would be willing to have anyone in a similar situation act on. Everyone is treated as a free person equal to all others under this imperative. People hold a correlative duty to treat others in the same way they expect to be treated. This creates universality with respect applying to everyone and respect flowing both ways. The second imperative is named the principle of ends. This principle states that every individual should treat others as ends that are worthy of dignity and respect. People should never be treated as mere means to others' ends. This highlights the point that every person is deserving of dignity and moral worth. Humans should never be exploited or manipulated. The last imperative is called the principle of autonomy, stating that every rational being is able to regard oneself as a maker of universal law. There is no need for an external authority. Examples of external authorities would be any god, government, culture, or any being that would determine moral law. Rational beings are deemed as able to discover moral truth for themselves. This imperative focuses on a person's interior motivations instead of the consequences of their external actions. However, this duty system has its flaws. There are no tools of measurement to compare. Moral truths and rights will conflict from person to person. One can also argue that not every being is rational and that some humans are not capable of reaching any conclusions about moral truth. These flaws are the reason not only one ethical duty system can be relied upon.

The second ethical duty system is call the Utilitarianism System. This system's main point is that an individual should not take any action that will not result in greater net benefits than harms. This should be exercised within a society or community that one is a part of, including businesses. A person should try to maximize the positive outcomes or minimize the harms. The main contributors of this system are Jeremy Bentham and John Mill. These founders realized that the law had value in society. They recognized that obedience to the law is a basic requirement for a productive and pleasant society. This also means that some certain laws can be manipulated and misdirected for individual gain, especially by powerful central authorities such as the government. Both Bentham and Mill wanted a means to evaluate the laws that were good and therefore should be obeyed as well as the laws that were not good and therefore should not be obeyed. They discovered that utility can be that means. Individuals are governed by the concept of increasing pleasure and decreasing pain. A party in a community is a collection of individuals that freely associate. The fundamental principle of the Utilitarianism system is that an action should be taken to create the greatest net good for everyone in the society. This system is teleological, which focuses on the consequences and end results of the decision or actions taken instead of the method taken to reach the end. This means that an individual should review and compare all the consequences of the possible outcomes of a certain decisions and choose the one that benefits the most people within a society. There should be a greater balance of benefits over costs for everyone affected. There are flaws with this system as well. There is no tools to measure happiness between people. This system also focuses on ends instead of the means and methods that should be taken. There is also a danger of paralysis by analysis. Using these two systems together can help an individual reach a decision regarding the ethics behind insider trading.

The Principles of Universal Duties is good system to use to analyze the ethics of insider trading. This is because insider trading primarily deals with the employee that is making the trades as well as the other players in the stock market. The main principle of the duty system is to not make a decision or take an action that you would not want to see others free and encouraged to take. This can be applied to the employee who is buying and selling shares of stock because they can consider how their actions will affect others and if they would want others to use their own experience to trade stocks. They key advantages of this system are universality, so it can apply to business and insider trading as well. This system also is based off of respect for other people, which one should take into consideration when deciding to participate in insider trading. The three categorical imperatives can be applied to the ethical question of insider trading as well. According to the first imperative, an individual must only act on reasons they would be willing to have anyone else in the same situation act upon. As long as the employee using their experience of their company to trade shares would be comfortable with other employees doing the same, this imperative is met. Everyone is being treated the same way, regardless of what company they work for or what specific knowledge they have to use in the stock market (within legal boundaries). The second imperative is met because no person is being treated as a means to an end. In other words, no exploitation or manipulation is occurring within this addressed type of insider trading. The third imperative states that every rational being has the right to discover the truths of moral law themselves without an external authority. This implies that the trader would have the right to determine if their actions are ethical or not, based upon the assumption they are a rational being and can come to that conclusion. The employee that is engaged with the trading meets this imperative by having the capacity to determine the moral truths. I think that the Golden Rule is an important aspect to consider when making a decision. I like how the decision is based off of everyone receiving equal treatment. In these ways I consider insider trading of shares using an employee’s unique company insight ethical.

Another ethical framework is necessary to look at all of the viewpoints, even from other stakeholders. Using the Utilitarianism system, insider trading can be analyzed to determine if it is ethical or not. This system states that an individual should not take any action that does not result in greater net benefits than harms for the society. Applying this to insider trading, the individual buying and selling shares should discern whether or not their use of knowledge will affect other stakeholders in a net positive or negative way. The goal is to maximize the benefits and minimize the harms. An individual should take the morally right course in any situation after comparing all of the other possible options that will produce the greatest balance of benefits over costs for everyone affected. The trader would look at all of the possible stakeholders, which would include the company, other traders, government, and economy, and determine how their actions affect those people. The employee trading shares is within the boundaries of law, which is a universally followed law by other traders. They all determined that these stock trading laws were good and needed for a more productive and pleasant society. The laws regarding insider trading help regulate the market to keep it fair for everyone involved. This helps to increase the 'pleasure,' or profits in this case, and decrease the pain of losing money. The employee who wants to use their insight of the company obviously needs to comply with the laws put into place by the government. This minimizes harms done to themselves as well as other investors in the market. To maximize benefits, the employee would need to consider who exactly would benefit from their trading transactions. The employee himself would benefit the most, creating profits for themselves and most likely increasing company value. These educated investments would also create value within the market. Overall, many benefits would be produced from this legal type of insider trading. I can see the value in the laws used regarding security trading and I definitely agree that they create a more even playing field. I conclude that by using the Utilitarianism system, insider trading is viewed as an ethical activity.

The ethics of insider trading can vary from person to person and business to business. Everyone understands that using confidential company knowledge or trading that information for any other type of reward is considered illegal within the United States. However, when all the laws are followed and the employees report their trades to the SEC, insider trading is a bit more complicated to define. An employee of a company has a multitude of information only he or she knows about that certain business that can be applied to how shares of stock are traded. This insight and experience cannot be easily ignored when making an educated decision regarding how their personal company shares are being traded. Any other employee in their same situation would have the same type of knowledge. Other employees from similar businesses can have the same type of insight in their respective company. All investors in the stock market have the right to use their intelligence and experience to make the best decision possible to make the most money. Friedman's economic outcome model proves that this concept of insider trading is ethical, bearing that it maximizes profits for the individual while staying within the boundaries of law without deception or fraud. This type of insider trading follows all rules and regulations set up by the government, which are the minimum standards for ethics. This makes insider trading ethical as well. Lastly, the two duty systems used both determine that insider trading is ethical. The Principles of Universal Duties and Utilitarianism prove that this is acceptable by members of the society (other employees or investors). With these three points, an employee using their unique insight to their company to buy and sell personal shares of stock is deemed completely ethical.