



The University of Sydney
Faculty of Economics and Business

Business and Professional Ethics Group

2008-2009



bpeg

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A 3D maze rendered in shades of blue, with the text "About BPEG" overlaid in white. The maze is composed of thick, rectangular walls that create a complex, winding path. The lighting is dramatic, with deep shadows in the recesses and bright highlights on the raised surfaces, giving it a three-dimensional appearance. The text "About BPEG" is centered in the lower half of the image in a clean, white, sans-serif font.

About BPEG

The Business and Professional Ethics Group (BPEG) is an interdisciplinary group deliberately set up to engage the existing ethics knowledge and expertise across the Faculty of Economics and Business at the University of Sydney. It aims to promote and develop high quality ethics focused research, teaching and outreach activities within the University, the wider community and business settings.

A 3D maze rendered in shades of blue, with the title text overlaid in the center.

Message from the General Convenor

It is with great pleasure that I introduce BPEG's first biennial publication. From relatively small beginnings, BPEG has grown rapidly to become a dynamic force in ethics research and education.

BPEG was established at the University of Sydney in 2006 by a nucleus of interested people with a passion for bringing ethics to the fore in the business world, particularly in business education and research. From that handful of committed people has grown a group consisting of over 50 members, representing over eight Disciplines within the Faculty of Economics and Business. This includes members of Faculty staff, members of other Faculties in the University and members of the wider community. A BPEG student society is also active, drawing in students from across the University.

BPEG organises a range of activities throughout the year, appealing to a broad cross-section of its membership. These activities are open to the whole community, not only BPEG members. Seminars are attended by colleagues from both the Faculty of Economics and Business and other Faculties, by members of various professional bodies, colleagues from other universities and members of the corporate world. BPEG is truly an interdisciplinary group.

The breadth of areas in which BPEG is involved is illustrated by the articles in this publication, the subjects of which range from the future of business education in Australia to the potential clash between regulation and professional ethics. We are pleased to include an article commissioned by BPEG for this publication by well-known business journalist, Stephen Long. It's a thought-provoking piece on the role of ethics in the current financial crisis.

Looking to the future, BPEG plans to continue its engagement in the debate about ethics and its place in business and professional life. Recently BPEG updated its constitution, extending associate membership to colleagues outside the Faculty of Economics and Business. The new constitution has also made possible honorary membership, enabling us to recognise our two founding members, Irene Moss and Professor Grant Michelson, without whom BPEG would not exist and whose ongoing support is invaluable.

BPEG has become an integral part of the fabric of the Faculty of Economics and Business, not least because of the support of the Dean, Peter Wolnizer. Without this support, and that of the University more widely, through the Vice-Chancellor, Dr Michael Spence, interdisciplinary groups such as BPEG would not flourish.

Finally, I thank the publication committee and the contributors to this first BPEG publication – their work reminds us of what ethics means and its centrality to all that we do. I do hope you enjoy their work.

Associate Professor Nonna Martinov-Bennie
General Convenor

The image features a complex, three-dimensional maze rendered in various shades of blue. The maze is composed of thick, rectangular walls that create a series of interconnected paths and dead ends. The lighting is dramatic, with deep shadows in the recesses and bright highlights on the raised edges, giving the maze a sense of depth and complexity. The overall color palette is monochromatic, ranging from dark navy to bright cyan. Centered over the maze is the text "Message from the Vice Chancellor" in a clean, white, sans-serif font.

**Message from the
Vice Chancellor**

If the last few years in business life have taught us anything, it is that a keen understanding of business and professional ethics is no mere optional extra for those involved in commercial life. If our system of markets is to survive, such an understanding is a crucial part of the toolkit of every businessperson.

At the University of Sydney we are committed to business education in a broad university context, drawing upon the skills of all the disciplines better to understand and to advance the prosperity of our society in a responsible and sustainable way. Our work in business and professional ethics is at the heart of that learning. I am sure that you will be as impressed as I have been by the work outlined in this booklet.

Dr Michael Spence
Vice-Chancellor

A 3D maze rendered in shades of blue, with the title "Message from the Dean" overlaid in white text. The maze is composed of thick, rectangular walls that create a complex, winding path. The lighting is dramatic, with deep shadows in the recesses and bright highlights on the raised surfaces, giving it a three-dimensional appearance. The text is centered in the middle-right portion of the image.

**Message from
the Dean**

There can be few more topical or important subjects in the current corporate climate than business and professional ethics. While debate about ethics is hardly new, recent events mean that ethics has a central role in the way business approaches its role as a global citizen.

The Business and Professional Ethics Group at the University of Sydney provides outstanding leadership and scholarship in the area of ethics. It takes an interdisciplinary approach by drawing on existing knowledge and expertise across the Faculty of Economics and Business, as well as from other Faculties in the University and the business and professional communities

The BPEG events outlined in this booklet demonstrate the way in which we engage with students, the professions and the community. The articles in this booklet make for thought-provoking reading.

The Faculty of Economics and Business is proud to be associated with BPEG and its commitment to ethics in business and professional life.

Professor Peter Wolnizer
Dean, Faculty of Economics and Business

A 3D maze rendered in shades of blue, with the word "Articles" overlaid in white text. The maze is composed of thick, rectangular walls that create a complex network of paths and dead ends. The lighting is dramatic, with deep shadows in the recesses and bright highlights on the raised surfaces, giving it a three-dimensional appearance. The word "Articles" is positioned in the lower right quadrant of the image, centered vertically relative to the maze's depth.

Articles

Ethical Finance — Urgent Necessity or Oxymoron

Stephen Long

Stephen Long is the ABC's economics correspondent

When the music stops, in terms of liquidity, things will be complicated. But as long as the music is playing, you've got to get up and dance. We're still dancing. – Charles ("Chuck") Prince, CEO, Citigroup.

On the 26th of July 2007 a couple of hundred finance professionals gathered at the Hilton Hotel in Sydney. They were attending one of those industry confabs where men and women gather around trade displays to schmooze and network, between sessions where their ilk deliver learned papers and share their wisdom. Merrill Lynch was one of the sponsors; its stall was handing out cute foam toy versions of its icon, the raging bull. The bull market was, of course, about to collapse. Within 14 months Merrill Lynch would be close to collapse too, rescued only by a distressed sale to Bank of America. But in the conference rooms, many of the speakers were apparently in denial about the risks that would bring on the financial crash. A senior trader from ANZ bank ran through series of neat graphs that explained how collateralised debt obligations were sliced and diced into tranches – the lower the tranche, the higher the risk. He reassured the audience that, despite the wave of sub-prime mortgage defaults in America, it was almost beyond belief that things could get so bad that the higher-rated tranches would be hit. Later, a chap from a global investment bank scoffed at the idea that the global

credit markets might seize up because “a couple of million losers in America lied about their income” when they took out mortgages.

It's a vignette that no doubt has parallels around the globe. It could fit easily into the narrative of industry executives and regulators who excused their lack of foresight and action on the basis that “nobody could see this coming” – but the warnings were there. The issue is not that nobody could see this coming. It's why so many failed to see it coming, while others realised the potential for disaster yet failed to act. To what extent was it a failure of governance, regulation, ethics or all of the above? To what extent was the crisis in the nature of the beast; a mother of meltdowns, to be sure, but an expression of an inherent tendency to crisis in financial markets and in capitalism?

There were of course many Cassandra's (in retrospect, the number claiming that status seems to be swelling by the day). Notable among the prophets of disaster in the United States are Professor Nouriel Roubini from the Stern School of Business at New York University, and Harvard Professor Robert Shiller who warned of the US housing bubble; here, the economist Steve Keen and the risk analyst and author Satyajit Das – who wrote and spoke about the unsustainable debt and leverage and correctly identified that the collapse of CDOs would precipitate the “coming global credit crash”. But those within academe, markets or journalism who were sounding the warning bells were often dismissed, ridiculed or ignored. When critics questioned the levels of leverage or the valuations of a prominent financial engineering concern, its routine response was: “Sophisticated investors understand the model”. In the financial markets, there were some latter day parallels to Hans Christian Anderson's fairy tale The Emperor's New Clothes.

Yet within the financial services industry and among regulators there was also growing unease and concern in the lead-up to the crisis; a fear that the credit derivatives and securities that were the source of so much profit could become, in Warren Buffet's words, “financial weapons of mass destruction”; a sense that the structures finance had created were out of control.

In September 2006, about 7000 delegates descended on Sydney for a banking conference at Darling

Harbour. At one session, speakers and delegates talked about the inability of their back offices to process the huge volumes of credit derivatives, credit default swaps and opaque financial instruments being produced. It was, they complained, impossible to properly assess counter-party risk; should push come to shove and disaster strike, even to work out who owed what to whom. It would “all be fine in the absence of Murphy’s Law”, a former Goldman Sachs executive said, the trouble being that Murphy’s Law by its nature had a tendency to happen.

The fears were evident in a survey of banking industry players done each year by PriceWaterHouseCoopers and Britain’s Centre for Financial Innovation. In 2006, for the second year in a row, “excessive regulation” was ranked as the greatest risk banks faced (the irony is exquisite). The number two concern was credit quality. Financial derivatives were ranked as the third highest risk overall but second by bank chief executives; they were worried about the huge growth in the volume and complexity of financial derivatives and securities. They were worried about counter-party risks, defaults and a drying up of liquidity (with good reason). Many bank executives, a PWC representative told me at the time, felt they did not understand the products their wunderkinder invented and traded.

The survey report quoted an unnamed US banking regulator: “Exotic mortgage products may come back to haunt us in an increasing interest rate environment. When the bankruptcies in both borrowers and lenders reach certain critical mass, the financial system’s capacity to absorb the loss may struggle to cope.” Prescient indeed! So why didn’t the regulators act? Why did the watchdogs merely sit and watch?

The acronyms coined for the sub-prime loans that were bundled up into those “exotic mortgage products” should have been a giveaway. “NINA” loans (no income, no assets) and “NINJA” loans (no income, no assets, no job). Forget interest only: lenders offered loans with repayments in the early years that were so low they failed to amortise the debt – the money owed increased, rather than fell. This was Ponzi finance and those in the business knew it. As early as 2005, from ten thousand miles away in Sydney, I heard the joke doing the

rounds on Wall Street that sub-prime mortgages were loans you gave to suckers who could never pay you back. “Liar loans”, in the jargon of the industry, that invited people to lie – tell us what you earn, and we won’t check. It was Ponzi finance on a vast and probably unprecedented scale.

The drivers for the lending frenzy were topsyturvy. It’s highly unlikely that so many dubious mortgages would have been sold had it not been for Wall Street’s huge demand for loans that could be securitised and then converted into products to be traded: the collateralised debt obligations and similar assets that were sold around the world. The demand for loans that could be pooled, tranced and sold around the world encouraged the deterioration in credit checking, underwriting standards and credit quality. The products that were meant to disseminate and dissipate risk merely globalised it when the assets turned “toxic” and nearly caused a systemic collapse of the entire financial system. It was financialisation’s equivalent of chaos theory. A butterfly flaps its wings in the Amazon and sets off a tornado in Texas; a mortgage broker sells loans to poor Black families in Detroit and the banking system collapses in Iceland.

There are many apparent villains in this saga’s dramatic personae. Among them:

Alan Greenspan: aptly described in the journalist Peter Hartcher’s biography as “bubble man”. Under his leadership, the Federal Reserve helped to solve a recession caused by the bursting of one bubble, in technology stocks, by pumping up a much bigger one, in housing. The Fed’s decision to cut the benchmark interest rate to a then record low of 1 per cent in 2002, and signal that it would remain low for a sustained period, created a flood of cheap debt and a surge of new lending in an already overheating housing market. It also meant that investing in Treasury bonds would deliver very meagre returns; this was one of the reasons why investors, searching for higher yields, shifted money into the exotic securities being created by the big global investment banks.

The Greenspan Fed not only failed to properly regulate or oversee the growth of exotic securities and unprecedented levels of debt and leverage; it actively encouraged it. “Not since Benjamin Strong (in the 1920s) has one man’s ideas, brilliance, personality, and personalisation of policy had such a

profound impact on the nature of financial (and, thus, economic) activities,” wrote Doug Noland, portfolio manager with the Prudent Bear fund, in 2005. “It is no exaggeration to state that Alan Greenspan is the father of ‘contemporary Wall Street finance’, having nurtured and accommodated a marketable securities-based credit system from its infancy some 18 years ago.” Under the reign of this disciple of Ayn Rand, he wrote, “the loan officer, banking system, and borrowing for business investment were supplanted as the prominent creators of finance by a New Paradigm securities, ‘structured finance’, and asset-based financial apparatus. At the same time, Fed open-market operations and bank reserve requirements were relinquished as purveyors of system liquidity. The benign bank loan was cast out as an anachronism, replaced by myriad ‘sophisticated’ securities, instruments, derivative contracts, and leveraged speculation. The US securities markets evolved into The Global Fountainhead of Liquidity Overabundance. Truth be told, Mr Greenspan is a monetary policy radical. He presided over the greatest expansion of speculative finance in history.”

Greenspan was a cheerleader for the loans that became the collateral for the crisis. He saw a four-to-five fold increase in the share of lending taken up by sub-prime mortgages not as a concern but as an outcome of superior risk management and the financial innovations that had made America great. “Where once more marginal applicants would simply have been denied credit, lenders are now able to quite efficiently judge the risk posed by individual applicants and to price that risk appropriately,” he argued in April 2005. “These improvements have led to a rapid growth in sub-prime mortgage lending.” (<http://www.federalreserve.gov/BoardDocs/>).

He opposed regulation of derivatives and relaxed regulation of banks. Greenspan’s ideological faith in unfettered markets predisposed him to see securitisation and financial engineering through a positive lens and, at least until very late in the piece, blinded him to the risks. Eventually there was a mea culpa, of sorts. Testifying before Congress on the 23rd of October, 2008, Greenspan conceded he had been “partially” wrong to oppose regulation and had “found a flaw” in his ideology: “Those of us”, he said, “who have looked to the self-interest of lending institutions

to protect shareholder’s equity – myself especially – are in a state of shocked disbelief”.

Credit Ratings Agencies: The inadequacy of the ratings of CDOs and other asset-backed securities is well-documented. So, too, the conflicts of interest that gave ratings agencies a vested interest in promoting the vast expansion of credit products that would cause much of the chaos. Standard & Poor’s, Moody’s et al hid behind disclaimers. The agencies, which were begun by journalists in the 19th century, relied on the protection of the First Amendment of the United States constitution that guarantees free speech and freedom of the press. Complain that securities they rated AAA had no basis for being rated AAA and the rejoinder was: the rating is “merely an opinion”. Yet the ratings agencies were actively involved in developing the securities. They advised their clients on how they should be structured to achieve the desired credit rating. “The analogy that I sometimes like to draw is with the restaurant critic, David Grais, a US litigation attorney, told Stan Correy of Radio National’s Background Briefing program. “If the restaurant critic dons his disguise and goes to the restaurant and eats dinner and writes a review, he’s clearly a journalist. But if he steps into the kitchen and samples the sauce and makes suggestions to the chef about how to correct the seasoning, and then comes back out and writes a review of the meal that he helped to create, he’s acting as something more than a journalist because journalists do not participate in the events that they cover. I think that in structured finance the rating agencies were back in the kitchen.”

Back in the kitchen making a mess of the meal. One reason why the ratings were so flawed is that the credit agencies’ analysts relied on historical default rates to assess securities built from mortgages. History was no guide because there was no precedent for the growth in sub-prime loans or the deterioration of lending standards. Curiously, as well as providing credit ratings, Standard & Poor’s owns and publishes the Case-Shiller Home Price Index, based on a methodology developed by Professor Karl Case of Wellesley College and Harvard’s Professor Robert Shiller. These academics had been warning for years before the sub-prime mortgage meltdown and the housing market collapse that real estate was overpriced, with the United States in the grip of a huge property bubble.

Accounting rules: If you believe the claims of many investment bankers, and some regulators, mark to market accounting was the culprit in this crisis. The practice of assigning a current market price to mortgage-backed securities and financial derivatives moved from “mark to market” to “mark to meltdown” when liquidity dried up and the market for the securities collapsed. There is truth in this, but it conveniently overlooks the upside that financial institutions and financiers gained from the practice before the crisis hit. When debt was cheap and asset prices were rising, mark to market rules allowed them to make big paper gains by revaluing assets. Financial institutions in effect front-loaded profits through discounted cash flow models that delivered generous assessments of future income. These accounting techniques and manipulations helped to underpin strong paper profits, dividends, and huge bonuses for those in the game while back-ending the risk that would emerge later on down the track. Few complained until the cycle turned.

Bank Regulations: It is a statement of the obvious to say that the rules designed to ensure that banks had sufficient capital failed miserably. In 2004, the Basel II Accord – the globally agreed framework for banking regulation – introduced updated standardised risk weightings that put the credit ratings agencies on centre stage. Banks were required to hold more capital against supposedly riskier assets with low credit ratings and allowed to hold less capital against higher-rated assets, changing the one-size capital fits all model that had prevailed under Basel 1. On the face of it, the approach looks eminently sensible but in practice it was a disaster. The risk weightings presented banks with a huge arbitrage opportunity – take a pool of sub-prime mortgages or other junk debt and, through the wonders of financial engineering, turn it into AAA rated securities. It is no wonder that Collateralised Debt Obligations and similar products that sliced and diced debt into risk-weighted tranches proliferated after Basel II.

The irony was that it was supposedly high quality, highly-rated assets that brought the banks undone. Banks borrowed heavily against these “assets” on a thin base of capital, but as the saying goes, you can put lipstick on a pig and it’s still a pig. As losses mounted on the underlying mortgages and other loans, the AAA-rated assets were downgraded. Banks had to write down asset valuations and suf-

fered huge mark-to-market losses. The opportunity the banks exploited turned against them and they belatedly learnt some home truths: no structured security is liquid and the assumptions underlying the rating models were made under favourable (and unsustainable) conditions which no longer prevailed. Mark-to-market works both ways. Because banks had been required to hold only minimal capital against these assets, the problem compounded. Banks found themselves hugely undercapitalised to absorb the pain. The house of cards came tumbling down, triggering the most serious financial crisis since the Great Depression. Inevitably, the banks’ problems became society’s problem. Governments in the US, the UK and elsewhere were forced to absorb bank losses and bail-out financial institutions run for profit with taxpayer funds. It was a case of socialise the losses; the gains had already been privatised.

The crisis was, in short, the bursting of massive, concurrent bubbles: in credit and asset prices. There was too much lending, too much leverage and too much debt. In the US in 2005, households borrowed more than a trillion US dollars for home mortgages – a 700 per cent increase on the amount Americans borrowed to buy homes ten years earlier. There was no precedent for the run-up of household debt in western nations in the decade before the bust. From Main Street to Wall Street, there was too much money chasing too few assets. An abundance of cheap and readily available credit drove up the price of houses and securities; equity markets soared as margin lending allowed investors to ride the bull market on borrowed money and leveraged buy-out firms used cheap debt to bid for listed firms.

Underlying the debt and asset bubbles was a series of global economic distortions and imbalances. There was a symbiotic relationship between the debt-fuelled consumption in the west, the massive growth of financial capitalism, and what one might call the Wal-Mart division of labour. As companies outsourced manufacturing en masse to the emerging economies of Asia, most notably China, a flood of low-cost goods made with low-cost labour pushed down consumer prices: China and other Asian economies in effect exported deflation to the west. The seemingly benign environment of low inflation encouraged central banks to cut benchmark interest rates. At the same time China amassed enormous foreign currency reserves from

its exports – aided by exchange rate controls that stopped the appreciation of the Yuan. Between 2000 and 2007, its foreign exchange reserve ballooned from \$US166 Billion to more than \$US1.5 Trillion. Foreign currency reserves from China and other parts of Asia were funnelled into US Treasury bonds, suppressing money market interest rates which were benchmarked on bonds. The result: a ready supply of cheap debt that encouraged borrowing and helped drive up asset prices.

As Robert Peston, the BBC's Business Editor, put it:

“In crude terms, for much of the past decade, millions of Chinese slaved away on near subsistence wages and still managed to save, both as a nation ... and as individuals. To a large extent they were working to improve our living standards, because they made more and more of the stuff we wanted at cheaper and cheaper prices – and clever bankers took their savings and lent the cash to us, so that we could buy the houses we cherished, the cars we desired, the flat-screen TVs.”

While the west binged on borrowed money, the east built a giant pool of savings. The debt of the west was, in large measure, savings and surpluses of China, some other Asian economies, and the oil-producing states of the Middle East, recycled through the capital markets. Coupled with the retirement savings being accumulated on behalf of workers in the west, the savings from Asia and the oil-producing states formed a tsunami of investible funds. Adrian Blundell-Wignall, the deputy director of financial and enterprise affairs at the OECD, has likened the glut of money to a rolling wave, or bubble, of excess liquidity that surfed from market to market, driving up asset prices. It provided a ready market for mortgages and other loans bundled up into bonds and securities and given a tick of approval by credit ratings agencies. And to sell more mortgage-backed securities, the banks needed more mortgages ...

As credit markets froze and the world economy stalled, there was a sense that this was an epochal event. Two decades after the Berlin Wall tumbled capitalism appeared to be in crisis. The financial press was full of articles about the “future of capitalism”. Some, perhaps many, assumed that there would be a new capitalism where finance would once again become subservient to the “real”

economy: that a bonfire of the vanities would end the reign of the financiers; that the stratospheric bonuses and other remuneration practices that encouraged excessive risk-taking would go; that speculative financial activity would be curtailed and the era of “financialisation” – where finance had come to dominate a greater share of the economy and colonise more and more aspects of daily life – was on the wane.

Yet a year on what is most striking is not how much things have changed, but how little. As the crisis abated there was a swift return to, if not business as usual, then something close to it. Wall Street investment banks tried to hand back bail out money to free themselves from the modest constraints on executive remuneration that went with it. Morgan Stanley set aside 72 per cent of its revenue for staff compensation in the second quarter of 2009. Goldman Sachs set aside a record \$US11.4 Billion dollars for employee pay and bonuses in the first half. When President Obama wants advice on finance, he reportedly picks up the phone and calls the CEO of JP Morgan Chase, his friend and confidante Jamie Dimon.

Almost 12 months after the collapse of Lehman Brothers, Adair Turner, head of the UK's Financial Services Authority, said that the finance sector was engaged in “socially useless activity” and had “swollen beyond a socially reasonable size”. He mused at a roundtable discussion for Prospect magazine that it could be cut down by way of a Tobin Tax on financial transactions, which would diminish the incentive for speculative trading. The comments prompted an outcry. There were calls for his sacking. The British Government swiftly reassured the City that there was no prospect whatsoever of such an imposition.

The response to the crisis by governments and regulators was no fatwa on finance – more a desperate attempt to restore it to its rightful place. Some prominent economists such as Nouriel Roubini argued that the crisis could be resolved by giving debt relief to those unable to pay their mortgages – bailing out the home-buyers rather than bailing out the banks – but this was never in serious contemplation. As share prices crashed and financial institutions foundered, the airwaves were full of breathless talk about banks being “nationalised”. But this was socialism for Wall Street: the State intervention was always about saving the

private sector not socialising it. Only in a minority of cases (such as the giant insurer AIG) did governments take over financial institutions in ways that wiped out common stockholders, and the billions in bailout money to recapitalise banks was provided with minor strings attached.

When a newly-elected President Obama proposed taxpayer assistance for struggling homeowners, Ric Santelli, a licensed derivatives trader and on air editor of CNBC's Business News, orchestrated a capitalist outcry. To scattered cheers and applause, he fulminated from the floor of the Chicago Board of Trade against the "moral hazard" involved in "subsidizing the losers' mortgages". "This is America!" he thundered, and threatened a "capitalist tea party". The greater moral hazard may flow from the bank rescue, particularly the ad hoc takeovers and mergers that were orchestrated to prevent financial institutions collapsing. One of the core problems faced by governments and regulators was that many banks, brokerages, and insurers, such as AIG, were too big to fail. The problem was overcome by forced or cajoled marriages that have made strategically important financial institutions even bigger.

If the recapitalisation was designed to cause minimal pain, so too, have been the measures put in place to lighten the load of "toxic assets" weighing down the financial system. In the United States, first the Bush Administration then the Obama Administration proposed State-underwritten auctions to allow banks to sell the distressed assets. But this remedy was in practice quietly shelved in favour of one both simpler and more amenable to institutions carrying the toxic assets. In April 2009 the United States simply modified its accounting rules so that banks no longer had to state a current market value for the toxic assets, and could instead hold them at book value or their own valuation. The change, made hastily by the Financial Accounting Standards Board under considerable pressure from Congress and financial firms, was an acknowledgement that mark to market had become mark to meltdown. Mark to market accounting, it is clear, was deeply flawed in many ways. A requirement that assets be valued at their current market price assumes a price and a market; valuing complex securities was always subjective and fraught and the market disappeared as the credit crash spread panic and stripped out liquidity. It may be that the accounting require-

ments created artificially high paper losses on the downside – just as they had allowed financial institutions to state unrealistic paper gains before the crash. But the suspicion remains that mark to market has been replaced by mark to make believe.

The OECD's Adrian Blundell-Wignall has used the metaphor of a circus performance to critique the strategy. In August 2009, speaking to business economists in Sydney, he likened the accounting modifications to a magician's sleight of hand: "Did we remove the toxic assets from the balance sheet of the banking system, anywhere? No, nowhere ... You change the accounting rules and say, hang on, we don't have to declare any losses on this \$700 billion, this \$800 billion, we can now declare that they're all book value ... It's really there and all those losses are going to be there but we don't have to declare it, and we won't have to raise any capital for it; it'll kind of be there just hidden behind the silk screen." And hope that the confidence trick will inspire a rally on equity markets and allow banks to recapitalise and grow their earnings, aided by official interest rates in most economies at or near zero.

As credit markets froze and trillions of dollars was wiped off the value of stocks and real estate, retirement savings plummeted. Many thousands of retail investors lured into get-rich quick schemes and margin lending went broke. It raised the question: if highly paid financiers and banks staffed with the smartest graduates and mathematical minds could get things so wrong, what hope did lesser mortals have of navigating financial markets? The two decades before the crisis were preceded by a risk-shift that saw responsibility for many aspects of peoples' financial welfare transferred from employers and governments to individuals and households. Defined benefit pensions were superseded by defined contribution superannuation. The mass of ordinary citizens were encouraged to join the "share-owning democracy". Credit-rationing was replaced by the push-selling of credit. An army of financial services salesmen and spruikers offered to guide the unsophisticated through the maze of choice, for a cut of the money. Regulation of the sales effort was based on the assumption that as long as the risks were disclosed, individuals would make rational choices. Yet the industry itself proved incapable of properly assessing risk and making rational decisions. There will be some minor constraints on financial markets' incursions

into the lives of ordinary citizens: some jurisdictions have placed bans on the sale of structured notes and other complex securities to retail investors. But there seems to be no serious questioning at a policy level of whether the “financialisation” of individuals and households makes sense: whether, for example, the vast bulk of workers’ retirement savings should be traded on markets.

Two decades after the Berlin Wall fell, the financial collapse and ensuing global recession would appear to have demolished some of the seeming verities of economics and capitalism. The efficient markets hypothesis is dead. The belief that financial markets are efficient and rational has been exposed as ideology masked as theory: a myth that encouraged the dangerous combination of lax controls, pernicious incentives, asset bubbles and complicated financial instruments. John Maynard Keynes wrote in *The General Theory of Employment, Interest and Money* that the world was ruled by the ideas of defunct economists; that “Madmen in authority, who hear voices in the air, are distilling their frenzy from some academic scribbler of a few years back”. The scribblers from the Chicago School of economics, who stole the commanding heights in the 1980s, look as if they have been toppled; at the very least their grip on the mount is shaky. Milton Friedman and laissez faire are out of favour; Keynes is (temporarily) back. Though the late economist whose views best encapsulate the crisis is not Keynes, but Hyam Minsky.

Minsky believed that prosperous times give rise to speculative euphoria, credit bubbles and boom-bust economic and business cycles. His financial instability hypothesis held that accumulated indebtedness caused capitalist crises and that over the course of the economic cycle there was a shift from sound, or hedge, finance, where borrowers can repay interest and principle from cash flow, to speculative finance where borrowers can repay interest but must regularly refinance the principal, to Ponzi finance where borrowers are relying on rising asset valuations and either refinancing against revaluations or selling assets in a rising market. It’s an apt description of the lending and borrowing that led to the sub-prime mortgage meltdown and the strategies used by financial engineering firms that made a motza from cheap debt and rising asset valuations during the good times but came undone when the cycle turned,

sometimes in spectacular fashion.

The policy implication is clear: markets are not self-correcting and cannot be left to “efficiently” allocate capital with minimal regulation and oversight. The global financial crisis lends weight to the view that financial regulators should use counter-cyclical tools such as contingent capital controls that require banks to hold more capital against assets during the boom times and less during busts. The world is shifting to a form of regulation along these lines. A Minskian analysis would also suggest that central banks should be willing to use monetary policy to lean against asset and credit bubbles, rather than confining their concerns narrowly to consumer price inflation, though central banks still seem reluctant to do so.

The high water mark for the era of light-touch regulation has come and gone. Financial capitalism will be corralled by rules that require it to hold more capital and limit leverage. Derivatives markets and the shadow banking system of hedge funds and off-balance sheet investment vehicles will be subject to greater oversight. But there is only so much regulation can do. One of the lessons of this crash is that accounting rules based on principles that seemed sound had consequences that few imagined, while bank regulations that looked good on paper actually encouraged the proliferation of risky securities. Innovation and exploiting opportunities is the modus operandi of financial capitalism. Real world practice will outstrip or sidestep rules and regulations. As important is the mindset of the watchdogs. Perhaps it would have been better to name the re-established global overseer the Financial Instability Board as a reminder of the markets’ inherent potential. Even with the best of reforms to oversight, the global imbalances that underpinned this crisis won’t be easily solved. In a globalised financial capitalism, policies put in place for the benefit of one nation will encourage arbitrages with consequences across the world. Central banks are (by and large) national; money is fungible, global and capable of almost instantaneous transaction. The emerging nations with “excess” savings may need to spend more while western nations spend less, but that’s the last thing the west desires at the moment: after accumulating unprecedented public debt to rescue their banks and recession-hit economies, the United States and Europe need China and the savings nations to buy their bonds.

And still, the legacy of excessive private debt and leverage that caused the global credit crash is yet to be expunged.

At the time of writing it was not clear whether the credit markets and the global economy were on the path to a genuine and sustainable recovery or whether this was merely a hiatus: to borrow Churchill's phrase after El Alamein, not the end, or even the beginning of the end, but, perhaps, the end of the beginning. Either way, at some stage, there will be another crash and another financial crisis. That's a safer bet than any derivative or exotic security a financial alchemist could conjure.

To what extent did the crisis involve a failure of ethics? Clearly, there was profound immorality and amorality in the behaviour of financial institutions and those involved in them all the way along the line. Any sense of fiduciary duty, or basic care, was lost when lenders devised loans that encouraged people to lie about their income and take on far too much debt. Mortgage brokers shovelled out the loans en masse to households that could never hope to repay them. Borrowers caught up in the get-rich-quick euphoria succumbed to the delusion. The securitisation market into which the loans were bundled up, sold on and traded was meant to spread and minimise risk but instead created a moral hazard where parties, believing they were insulated from risk, showed reckless disregard for it. From the board room to the trading floor, financiers and financial engineers looked to maximise short-term gains – and their own compensation — without due regard for long term consequences. Dodgy credit ratings flowed from conflicted ratings agencies. Self-serving market transactions generated billions in fees and income but often did little to facilitate commerce or generate anything of particular benefit to society. From Struggle Street to Wall Street, greed replaced commonsense. But the fallout hit a multitude who had played little or no part in it. The tens of millions who have lost jobs, homes and retirement income in the west are not necessarily the hardest hit; there are also the many millions who have or will suffer poverty, hunger, even starvation in the Third World as the crisis Born in the USA undermines capital flows and global trade.

The faith that governments and market participants showed in the “invisible hand”, to use the great economist and moral philosopher Adam Smith's metaphor, was not justified; the individual pursuit of self-interest in the marketplace produced collective harm rather than collective benefit. Better perhaps to have heeded Smith's advocacy of laws against usury, his suspicion about the penchant of the merchant class to arrange affairs to suit its private interest at the public expense, and his warning that all money is a matter of belief. There will be regulation, but it would be naive to think that this will produce some kind of transformation in financial capitalism's dynamics. New rules may ameliorate excesses and temper conduct but they won't eliminate risk. A culture of compliance won't necessarily change values or the underlying imperative to maximise income and profits. Over time, inevitably, the pain of the last crisis fades and traders taking big risks to make extreme money tend to be rewarded and celebrated while those voicing doubts and calling for caution tend to be derided and ignored. The deeper, unpalatable question is not what should be done to create an “ethical” or moral financial capitalism but whether it is even possible.

Ethics as a Practical Leadership Strategy in this Age of Transparency*

Irene Moss

Irene Moss is a member of the University Senate and a former ICAC Commissioner. She is a founding member of BPEG and one of two Honorary Members.

This is a time of lost confidence, flawed systems, complex challenges. Ethical behaviour is not simply about moral imperatives, about acting with good conscience, doing the right thing. Good ethics is a practical business and professional strategy. The kind of behaviour people thought they could get away with in years gone by is no longer acceptable.

In 1994, Brian Burke became the first head of any government in Australia to go to prison. He was jailed for seven months for rorting his travel expenses. About a decade later he surfaced again. This time a group of ministers who thought they could rely on non disclosure were forced to resign. They'd breached cabinet confidentiality by telling Burke, who was now working as a political lobbyist, what the cabinet was doing.

Of course Western Australia was not the only state to suffer from leaders who failed the ethics test. Back in the 1980s, one Australian journalist quipped – not entirely in jest – that Sydney was one of the most corrupt cities in the Western world.

What had led to this sorry indictment? Well, one

of the seven judges on Australia's highest court had gone through several inconclusive inquiries and trials on corruption charges. The chief magistrate for New South Wales had gone to jail for perverting the course of justice. The minister for prisons ended up in one after he was convicted of receiving bribes to release prisoners. Two other ministers had been the subject of allegations and speculation. A former Police Commissioner and Deputy Commissioner were charged.

Indeed in the 1980s corruption was such a prominent feature of New South Wales life that in 1989 the Independent Commission Against Corruption (ICAC) was set up to investigate and prevent it. ICAC saw human nature at its worst – and in some cases its most bizarre. In one case, ICAC was trying to detect the theft of specimens from the national nature museum. Cameras were mounted in the premises (including one in a stuffed bear) and eventually caught the janitor, who had been taking exhibits to stock his own collection.

In another case covert surveillance was mounted on local planning authorities. Suspects were using code to talk about the money changing hands. One suit represented \$1,000, so 70 suits stood for \$70,000. One of the tapped suspects was overheard telling his collaborator: "You are doing such a lousy job, you'll be lucky to get a pair of shorts out of this!" In yet another phone tap, it was found that the code "eat pizza" meant getting a bullet in the head.

Human nature being what it is, it would be impossible to ever entirely rid organisations and institutions of corruption. But there is no doubt that tolerance for unethical behaviour has changed, for a number of reasons.

First, we live in a global village. Technology and the speed of communication have broken down trade, financial and social barriers. We came from village societies. There were social constructs that promoted strong incentives to behave in a way that was acceptable to the community. This encouraged transparency. When we moved from our villages to our cities, there was less transparency, resulting in fewer incentives to behave in a "community spirited" way. But the global village spawned in this internet age means

that people who have positions of responsibility are once again highly visible – and accountable. Information is available on anyone, anywhere – at no cost.

So business leaders can never rely on non disclosure. They must assume transparency and accept accountability. Those who don't can suffer severe consequences. AWB's oil-for-food debacle is one example, HHH is another. On the global stage, Enron is a third.

A second argument for adopting ethics as a practical leadership strategy is the changed community attitude to public corporations. There is a sense that listed public companies are custodians of community assets. As such they're being held to standards of accountability that in past times only applied to governments – if at all.

This is borne out by a recent study released by the St James Ethics Centre. Less than one per cent of those surveyed believed that business has no ethical obligations. Ninety three per cent believed organisations have an obligation to act ethically – even if it occasionally harms their profits.

There is no doubt that people's perceptions of unethical behaviour will lead to a loss of credibility and authority and ultimately a loss of efficacy. People may know little more than what's in the headlines. But the association between the organisation and corruption has the capacity to reduce its standing and moral authority.

The unethical behaviour of a small group of options traders cost the CEO of NAB his job and severely embarrassed the Board, and the alleged improprieties of a senior manager caused embarrassment for Coles Myer. The losses produced in these cases were not large relative to the size of the organisations. If losses of a similar size had been incurred through a bad loan or overspend of expenses during normal operations they would have had far less impact.

A question business leaders should ask is: who are our stakeholders? Who is actually affected by the organisation?

Unethical behaviour by corporations often has far-reaching consequences. When Enron fell, the corrupt behaviour of its leadership not only affected

its immediate stakeholders – its employees, shareholders and creditors. It affected public confidence in the entire financial system and the business community.

These issues have become more stark and pressing with the Global Financial Crisis, which has highlighted the short-termism of many corporations in the pursuit of profit over careful risk management. Our society may be strong enough to handle a few Madoffs and Enrons without a loss of confidence in the system. But if unethical behaviour becomes pervasive it can completely undermine incentives to do the right thing because honest people feel there is no point in trying.

Many analysts believe that this is a key issue in Africa right now. That corruption is affecting the economic growth of tens of millions of people. In response the World Bank is making ethical standards a key factor in lending money.

Leaders set the tone for the organisations they lead. Ethical leadership goes beyond ticking boxes, following processes or considering conflicts of interests. It means a genuine regard for issues of independence, responsibility and due diligence. It means an awareness of all stakeholders. It means building an organisational and management culture that emphasises and promotes ethics. It means embedding these in structures and processes so that people come across them in their day-to-day work. Stakeholders expect nothing less.

* This is an edited version of a graduation speech at the University of Sydney, 5 June 2009

Morality, Ethics and Gossip

Grant Michelson

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Communication is a ubiquitous phenomenon in different organisational settings and many would contend that communicating well is one of the more important factors in contributing to an organisation's success. Communication, of course, involves both formally sanctioned channels, such as newsletters, memorandums and company meetings, as well as more informal channels. One well known example of the latter type of communication is gossip – which is defined here as evaluative talk (written or spoken) between at least two persons about an absent third person(s).

However, this widely-practised discourse is inherently underpinned by moral and ethical considerations as reflected in such opening statements as 'I don't like to gossip but...' or 'You haven't heard this from me...'. In spite of apparent personal reservations that may have as their source numerous underlying reasons, the information is nonetheless still transmitted. The internal conflict that this might pose for some individuals would certainly resonate with extant theories

such as Festinger's theory of cognitive dissonance.

The purpose of this short commentary is to simply identify how questions of morality and ethics are indeed present in one of the most common types of informal communication. For present purposes, the discussion is kept relatively brief and does not exhaust the full range of possibilities. Indeed, the intention is simply to reveal some of the ethical issues of potential interest. We turn to some of the reasons against gossip before canvassing some points in favour of gossip.

Against gossip

Gossip has attracted criticism because of its general capacity (attributed to underlying intention or motive) to generate a range of negative outcomes including disharmony, suspicions and seeing the worst in other people. Through gossip, people seem particularly pleased to discover and discuss the faults and weaknesses of others. There seems a pleasure (if many of us are honest) in pointing out the existence of error or wrong-doing in others. To give vent to that pleasure is gossip. Thus, utilitarian arguments based on a range of actual and potential harmful consequences are not uncommon when discussing the case against gossip. Such concerns might be raised both about the content of the gossip and its impact on persons and social situations.

Indeed, the distinction between actions and persons is difficult to separate when it comes to gossip. For example, a derogatory comment about a particular style of suit or dress worn by an absent colleague is essentially a comment about that person's (poor) choice of taste. The action itself (the wearing of 'that' suit or dress) is not morally problematic but the translation of this action to a negative evaluation made by colleagues about the other person is what would be called into question by those against gossip. Shaping the opinion of organisational members through gossip might therefore create a culture of censure that potentially interferes with that individual's freedom, a point on which British philosopher, John Stuart Mill, would certainly oppose.

For those who engage in gossip (the gossipers and his or her audience) the action of gossip itself purportedly can strengthen relationships and trust (see below). However, for persons who are the subject of gossip the act and content of gossip

may damage relationships and serve to perpetuate their sense of being an outsider. The question then arises: does the moral objection against gossip lessen if the subject or target of the gossip is blissfully unaware of the gossip about them?

In other words, the direct harm against the target in this situation would be negligible. Reference to another philosophical perspective would still lead to the same conclusion against gossip. In Kantian terms, one might ask whether you would wish to be treated in the same manner, whether you are treating the subject of gossip with respect, and whether you are using that person simply as a means of enhancing one's own pleasure.

On the point of pleasure, it is arguably those factors from which a person derives pleasure that both forms as well as reveals their character. If gossip is precipitated principally by suspect or sinister motives towards other people then gossip might not merely harm the target of gossip itself but also the gossiper. That is, evaluative talk about other persons might point to and perpetuate flaws such as low self-esteem and self-respect in the gossiper's own character. Concentrating on the ostensible shortcomings and faults of others might, in some cases, be an attempt to deflect or divert attention from one's own limitations or inadequacies.

Further, to concentrate on the faults of others is also an attempt to present oneself in a favourable light; the focus on other persons tends to imply that the gossiper has few, if any, faults. This is most unlikely, of course, but it is interesting that such assumptions about the gossiper's character have seldom been explored in previous studies. While there may be little data available to support the proposition, it does not automatically eliminate this character-based argument as a case against gossip. This is because the transmission of gossip is not always triggered by the pursuit of pleasure; the level of anxiety experienced by a person, for example, has been found by a number of researchers to predict the transmission of gossip.

In defence of gossip

In addition to those moral philosophers who countenance against gossip, there are also scholars from within the philosophical tradition who adopt a more optimistic view towards gossip. Since

gossip entails the exclusion of some persons (the targets of gossip) it can be regarded quite literally as behind-the-back talk (spoken or written) about others. At face value this might appear to contravene the wider moral rule about the treatment of other people: 'Do to others as you would have them do to you' that is endorsed by Kantian philosophy. But talking behind-the-back is not necessarily synonymous with a stab-in-the-back. For instance, if a supervisor tells a subordinate about how they could improve their promotion opportunities with the manager is this a problem when the manager is not opposed to such knowledge being known? If this is an industry that experiences high turnover due, among other factors, to limited career prospects then efforts to retain staff could be assisted by the 'gossip' about the manager's promotion expectations.

Building on this illustration, there are many cogent arguments put forward to justify gossip, or at least some gossip. For example, it has previously been suggested by some scholars that gossip is an inherently democratic process, acting as a resource for moral understanding and freedom of speech. Similarly, one contributor (Ben-Ze'ev) in the edited book, *Good Gossip*, contends that the prohibition of gossip on ethical grounds is not necessarily justified because such prohibition focuses on extreme, non-typical cases, and simply serves to reinforce the negative stereotypes, perception and reputation of gossip. Such reinforcement promotes distortion and misunderstanding, and the positive functions of gossip, including its intrinsic value as an activity that is easygoing and enjoyable, are often ignored. Thus, the issue may have far less to do with the content of gossip as a common objection noted by opponents of gossip, but one of recognising the value of gossip as a means by which people learn to relate well to one another.

The proposition that gossip is primarily about relating and relationships rather than content is of interest because it could assume that what is actually discussed is largely immaterial to the wider purpose of enhancing social bonds between the participants. Since gossip is evaluative talk, value judgments are nonetheless made about content during the process of establishing and building relationships. This is not to suggest that the content is unimportant; simply, that the topics of gossip are not the primary objective of the talk between

the gossip and gossipee. The relationship between the gossip participants and the person(s) who is/are the subject of the gossip is a different matter and was addressed earlier.

It could also be the case that the view of gossip as a moral problem is flawed by misrepresentation of the potential to harm. In order to illustrate this point we draw an analogy for gossip with eating. While excessive eating is harmful, this does not imply an intrinsic evil in eating. Similarly, if we accept that excessive and distorted gossip can potentially also be harmful, this does not establish or validate the intrinsic malicious nature of every piece of gossip. Take, for instance, one employee who notes to an approving co-worker about another colleague, 'I am so pleased to hear about Lisa's new baby'.

In sum, there is no doubt that at a more universal level of understanding gossip enjoys a poor reputation and has been subject to widespread and enduring disapproval and censure. Such objections are often centred on the rights and freedoms of the target or subject of gossip. From the perspective of the gossip and gossipee, the arguments against gossip appear less certain. To suggest that all gossip is harmful is not a position that can be easily accepted as we need to appreciate that different relationships exist between the three main groups (gossiper, gossipee and target). However, to suggest from the short discussion that gossip is regarded as entirely virtuous would also be misleading. To be sure, some gossip can indeed be morally problematic in organisational settings. But equally, there are instances when some gossip should not be condemned.

A 3D maze with blue walls and a bright blue light source at the end of a path. The maze is composed of rectangular blocks that create a complex network of paths and dead ends. The lighting is dramatic, with deep shadows and bright highlights, creating a sense of depth and mystery. The word "Activities" is written in white, bold, sans-serif font in the center of the image.

Activities

BPEG is a vibrant group, which regularly brings together its members and other interested parties from across the Faculty, University and the wider community to engage in ethics related issues.

BPEG organise regular seminars and workshops. Some of the recent events organised by BPEG are featured in the following pages.

A full list of BPEG seminars can be found on p. 35

Further information on BPEG seminars and events can be found on the BPEG website:

<http://bpeg.econ.usyd.edu.au>

**The following articles are the
text of selected seminars
from 2008/09**

The Business School: A Creature of its Time?*

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Imagine the university ten years from now – a university without a business school. A few economists may have reinvented themselves into experts in climate change, health or transport and one or two management academics may have returned to their original disciplines in sociology, psychology or statistics. However, the majority, especially accounting and finance academics, will have retired or be employed with private higher education providers.

There are reasons why the business school may have been a creature of its time: reliance on the market, their lesser role within the university and their lack of an appropriate value proposition. There are also good reasons why the business school should remain within the university, not least of which is the important role of business within society and the values held by business academics.

Australian business schools have been driven by

market demand. Historically business studies, apart from a at few Graduate Schools of Business, were the domain of the vocational sector, TAFE and Colleges of Advanced Education (CAEs). The rise of business degrees in universities was the direct result of the massification and later marketisation of the Australian higher education system. ‘Business’ degrees first appeared in universities following amalgamations with CAEs in the 1980s, the beginning of the massification of higher education. With the deregulation and corporatisation of the Australian higher education system in the late 1980s, and the introduction of fee-paying international and postgraduate students, business degrees became highly popular. By responding to this demand and creating further demand through new international and offshore markets, business schools have flourished in the corporatised environment of the Australian higher education system, as demonstrated in Table 1.

As business schools have lived by the market, they may also wither by it. Uncontained growth is as dangerous as market risk. Demand involves risk, risks related to exchange rates, changes in student subsidies and competition. The entry of online programs and private higher education providers pose threats to the viability of business schools, especially in the areas of finance, accounting and general business. Twelve months after their introduction in 2006, private higher education providers, with both online and face-to-face degree programs, had captured 10 per cent of higher education students, with the biggest demand from international business students¹. Private providers range from multinational companies such as Kaplan and Cengage, to private colleges and professional associations such as CPA and ICAA. They provide for niche markets in high demand areas. With low overheads, including highly casualised teaching staff, they have the ability to provide degree ‘products’ through a teaching only focus and, increasingly, a promise of employment

	1996	2007	% Change
Total student enrolments in Aust higher education system	634,094	1,029,846	62%
% Business students	23%	30%	112%
% International students	8%	27%	448%
% International students in business	50%	51%	352%
% Postgraduate coursework students in business ²	31%	40%	173%

Table 1: Growth in Business Schools³

through their links with industry and professional service organisations. Compared to universities, where academics are increasingly encouraged to disengage from students and professions in favour of research, private providers compete directly for students with university business schools.

Business schools have relatively poor standing within the university community. Success in revenue raising has meant that business schools are regarded in their institutional role as ‘cash cows’. Business schools have been highly successful in commodifying higher education and contributing financially to their universities. They have not only attracted large revenues from fee-paying international and postgraduate coursework students, but minimised costs with the highest staff/student ratios at 1:34⁴. Financial success has sometimes been at the cost of academic respect within the university⁵. They are rarely held out as examples of the university’s strength or contribution to society. Universities have actively encouraged business schools to meet the increasing demand for students and revenue without regard to whether the schools stay within the mission of the university.

Will the university still want its business school, if it ceases to be a ‘cash cow’? This question may lead to the potential demise of the business school. If the business school is unable to enunciate a value proposition that provides a legitimate role within a university, then what is its future? The current value proposition or purpose of an Australian business school seems to lie in the salaries its graduates attract and the revenue it provides to its university. A paper for the Australian Business Dean’s Council⁶ suggested openly that the ‘value’ of a business degree was in attaining higher salaries than other graduates. It is not uncommon for MBA rankings to equate graduate salaries with quality, be that of graduates or the program itself. This type of utilitarian thinking goes beyond promises to students, to the behaviour of business

school managers when they appear to give greater importance to sustaining financial growth than the problems created by the growth. Even if business schools were to substitute financial discussions for less utilitarian concerns, business schools may still have difficulty in articulating a clear and scholarly purpose.

The problem has its basis in understanding whether or not business schools are a professional school or a purely academic school. This is a problem not limited to Australian business schools. The first business schools were established by wealthy philanthropists in the United States over one hundred years ago⁷. Their intention was to give business credibility as a profession equal to medicine, law and engineering. But, unlike other professions, business itself lacks a distinct and common ethos grounded in furthering the quality of life. When this absence of ethos translates to the business school, it stands accused of teaching technique and preaching greed⁸. A professional ethos is missing, both in practice and in the classroom. Further, the business school curriculum remains distinctly multidisciplinary, with little evidence of a distinct body of knowledge or even a convergence of disciplines such as occurs with medicine and law⁹. Current publishing regimes do little to encourage interdisciplinarity. Unlike other professional schools, business school links to practice and practitioners are weak. For many business schools, the strongest link to practitioners is through casual academics, of which there are many.

The quandary presented by the research imperative, is that not only does relevance appear to decline and academics disengage from teaching, but academic individualism and opportunism increase as colleagues compete for points and publications. The social contribution remains unclear and even the financial contribution is put at risk. Continually recruiting established researchers not only drives up salary costs as the pool of such individuals

is small in Australia, but it fails to regenerate the profession while at the same time inflating expenses and deflating surpluses. Despite the emphasis on research, the business school's record in research, especially producing research higher degree students is poor with only 8 per cent of doctoral students compared to 30 per cent of all students in the higher education system¹⁰.

Despite the evidence suggesting business schools are a thing of the past, there remain at least three good reasons why the business school should remain in public universities. First, business is a large and important part of national and international communities. Understanding it, both technically and critically, is an important social contribution, the type of contribution a university should make. Second, the number and percentage of international students studying business provides an important advantage for Australia. However, this advantage must be appreciated and managed for its educational and social value not simply its financial return. Third, business academics are essentially academics at heart. Their beliefs and values are no different to those in other faculties, but their environment is. Business academics want to make a worthy sound contribution, not be relegated to merely fund-raisers¹¹.

Based on our research on business school academics¹², we make two observations to assist business schools to remain as creatures of the university. First, being profitable is not a problem, providing academics have ownership and control of what they do and are not reduced to the level of a factory employee. Business academics can maintain value and values at the same time. Second, smallness and human interaction make for more engaged academics and students. This smallness relates equally to school size and class size. Neither a 'bearpit of ideas' nor a 'creation of understanding' occurs in large schools and large classrooms. A clear and acceptable value proposition will only come through communication, not bureaucratic decree.

A final comment. Academics have different strengths and weaknesses, different contributions to make. A one-size-fits-all approach only serves to alienate individuals either from commitment to their school or to the academic profession or both. Within a professional business school there is room for researchers, teachers, consultants and practitioners, and in combination. Going with the latest fad, whether it be accreditation or

Excellence in Research in Australia, is not always good for business. This is not a statement against research, but against research only. If business schools exclude teaching and practice from their mission, their contribution is diminished. If business schools reject playing image games with marketing, rankings and accreditations, in favour of dealing honestly with their problems, they would help to ensure their place as creatures of the future.

* This is an edited version of a BPEG seminar presented by Suzanne Ryan and James Guthrie in February 2009

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Client Capture and the Professional Service Firm*

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This is a summary of a project currently being undertaken in Canada and funded by the Law Foundation of Ontario and the Alberta Law Foundation.

The project examines one of the more troubling aspects of the corporate failures of the turn of the century: how highly trained professionals, governed by and committed to strong codes of ethics, allowed themselves to become active participants in, and sometimes facilitators of, questionable business practices. Following the collapse of Enron and Arthur Andersen, the primary

public and academic focus was upon the role of the auditors. In this project we turn to the role of lawyers and ethical practices, with a particular focus on lawyers working in large commercial law firms

Our project builds on many years of research where we have examined how professionals, both lawyers and accountants, address ethical dilemmas. Much of our early work looked at corporate counsel – lawyers employed within organisations – and how they dealt with the dual ethical responsibilities to their profession and their employer. We found much the same as others before us had found with other professional employees; that our corporate counsel seems to handle this dual function with remarkably little reported stress or difficulty.

This led us to question why this could be. Surely employed lawyers or accountants at some times will find themselves facing competing loyalties and surely resolving such dilemmas can be troubling? We posited various explanations for why this might not be the case. For example, perhaps lawyers do not face such conflicts despite our prior beliefs. Alternatively, maybe management simply fails to incorporate them in decision making whenever difficult issues arise. Or, perhaps lawyers address issues either so much like legal professionals or so much like managers that they fail to recognise that there is a conflict?

These issues were intriguing yet, at the same time, troubling. Lawyers (in this case) are hired by firms because they are different from managers. They have sometimes been referred to as ‘the conscience of the firm’ since they are trained in ethics and they do owe responsibilities to a powerful external professional body. In the ideal world, corporate counsel is there because, in the right circumstances, they will tell management what it is that they must not do. Yet, if these lawyers are thinking more like managers than lawyers, what value will they add to the firm?

In earlier work motivated by the above questions, we examined ethical decision making by corporate counsel. We identified certain organisational factors that affect how lawyers working within corporations resolve ethical dilemmas. Further, we found evidence of lawyers adopting different identities (innate self-perceptions of which

they may or may not be aware) ranging from highly professional to highly organisational/managerial. We also discovered that the significance of these identities shaped the ethical choices counsel made. Significantly, certain organisational factors (e.g. proximity to top management, available career options) influenced the type of identity adopted. In other words, we found evidence that the organisation itself may shape the individual, which in turn directly shapes the way that this individual approaches and resolves ethical dilemmas.

In our current study, we now turn to lawyers in private practice and, in particular, lawyers in large commercial law firms. The basic premise is that in order to understand how lawyers make ethical decisions we need to understand the relationships between the individuals and the firm. We do not believe that the popular metaphor of the 'bad apple' advances our understanding of these complex issues. While a focus on the individual may at times be warranted, it is our supposition that in many more cases the problems result from systemic causes that require more complex explanations. Organisations seldom set out to hire employees or professional service providers who are 'bad'. Enron (and Arthur Andersen), for example, sought to employ the most talented of young graduates, never suggesting to their new recruits that they abandon their moral compass at the company door. In this study we will examine the ways in which an organisational context itself might generate behaviour in professionals that is ethically problematic.

Our present study will assess the extent to which the client/lawyer relationship – within the context of firm dynamics – might impact ethical decision making; our approach will pay particular attention to the notion of the "autonomous" or "independent" professional. While our lawyers are in Canada, we have good reasons to believe that our findings will be as relevant at least to law firms in the United States and likely in Australia (and other countries) as well. The firm structures and the organisation of the professions are simply very similar (indeed some firms are international).

The proposed study builds on the theoretical insights gained in our study of corporate counsel. We will seek to ascertain whether the nature of the relationship with the client and related firm dynamics also affect the ethical decision making of commercial lawyers in private practice in a similar

fashion. More specifically, the project is designed to discover whether "client capture", the situation in which clients exert undue influence over their professional advisors, can be identified in Canadian corporate law firms and, if so, what its antecedents and implications might be. The study will build on a pilot study conducted in the past year which is reported in the *American Business Law Journal* and the *Journal of Business Ethics*. It will use an interview technique tested in the pilot and will seek responses from interviews of approximately 100 commercial lawyers in large firms across Canada.

* This is an edited version of a BPEG seminar presented by Sally Gunz in March 2009

True and Fair: An Ethical Override?*

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A longstanding ethos

Since 1844 company financial disclosures (in the British system) have been subjected by legislation to the broad ethos that they be true and fair (or equivalent phrasing). We might take that to be the overriding ethical principle imposed on accountants in that setting. To be even more specific, the true and fair ethos is couched generally in terms implying that those disclosures show a 'truthful and fair' depiction of an entity's financial condition and its latest periodic performance leading to it. This was to provide checks and balances to ensure there was equity and fair trading (trust) in those dealing with corporations, especially for those drawing upon companies' financials to assess risk and make forecasts about expected financial positions and returns. Seeking equity and fairness in trading always entails recourse to moral norms. True and fair is a broad ethos designed to underpin companies' financial disclosures, thereby providing a general guide to accountants' professionalism.

Here, we stress that the true and fair criterion is possibly the oldest professional ethos – we note that the Hippocratic oath (406-380 BC) – initially a pagan oath sworn to the pagan god,

Apollo – was first recommended to the medical profession by Percival in the late 18th century. It was taken up in a minor way by the US profession in 1846 and reworded in the 1930s – even now it is not universally embraced in legislation nor indeed by all or many medical schools. We note also in that context, there were all kinds of rewordings, to make it acceptable to Muslims, Jews and Christians over time, whereas the true and fair criterion has remained untouched and basically unchallenged. Our point is that arguably true and fair has enjoyed the longest tenure as an unquestioned standard for a professional practice. It is reasonable to take it that true and fair was not only readily accepted, but that it was so because few had any difficulty for around 125 years in understanding what it meant.

Discussions about ethics and morality could open up a never ending discussion on whether an institutional, Benthamite or deontological approach to ethics ought to be adopted. Rather than open that can of worms, our aim is to limit discussion here to the ethics of a professional, (say accountant and accounting), in the domain of the abstract legal persona, the corporation and its commercial dealings. Specifically we are examining the legal and accounting (primarily the latter) issues pertaining to this legally mandated ethical phrase, 'true and fair view'. We are examining its ambit as it pertains to the actions of directors, officers and auditors in undertaking their functions to ensure there are adequate checks and balances in the way the legal creature, the corporation, conducts, and is accountable for its commercial affairs. This leads us specifically to focus on what is the history of the meaning of the phrase, why it was part of the UK parliamentarian Gladstone's 1844 legislation and beyond, whether it remains applicable in a globalised IFRS world, and how might it be usefully interpreted.

Our primary proposition is that true and fair is a uniquely appropriate, succinct, descriptor of the meta-ethos guiding professional behaviour by participants in a commercial setting in general and accountants and accounting in particular.

The history of true and fair gives insight into how that proposition would have disturbed few for well over a century, and how the centrality of its commercial significance has been reinforced by events in the recent past.

A chronology of works and cases on ‘true and fair’

We observed that for over 125 years practice within the true and fair view rubric was generally uninterrupted and unsullied. Following concerns in the 1970s, 1980s and early 1990s, in Australia at least, uncertainty as to what was meant by true and fair led the accounting profession to promote the idea that compliance with the accounting standards of the day ought to be the primary disclosure criterion. This, possibly, was driven mainly by the perceived certainty that such a move injected reliability into the activities of both regulators and members of the accounting profession. In effect the push was to argue that the previously acknowledged true and fair override was redundant. Many claimed that, in Australia by the early 1990s, the new wording in the Australian companies legislation effectively removed the criterion. Others, like leading Melbourne commercial lawyer Mark Liebler, have continued to disagree with that proposition.

In this context it is instructive to consider Mark Liebler’s 2002 JCPAA Submission which argued that true and fair was still the override – a variant on that submission was subsequently published in the *Australian Accounting Review*¹. Liebler’s views are essentially: “In an ideal world and with a little imagination accounting standards would always produce a true and fair result – [but the world is not ideal] and the legislature in 1998 reaffirmed that there was a need to retain quite independently of compliance with accounting standards, a ‘true and fair’ requirement.”

The meaning of true and fair view

It is worth contemplating what the words mean. We could, for example:

1. offer the legal dictum that – that ordinary words are given ordinary meanings – literal v. substantive approach
2. argue that we use both everyday without difficulty – that they are ordinary words
3. enter issue of professional judgement
4. enter the consumerism – fitness for use criterion as a possible test as to whether the data are true and fair

Summing up

In Britain, despite changes in the wording of the legislation (to accord with the EU), ‘true and

fair’ have been endorsed by the British Financial Reporting Council (FRC) as the *cornerstone of accounting*, most recently in May 2008 (PN 222). Experiences with the ‘true and fair override’ aptly illustrate the perceived incompatibility of a broad-based ethos in a litigious environment, unless that ethos can be operationalised through explicit description. It seems that, whereas the broader the ethos the closer it is to guiding behaviour to meet the individual-specific intention of professional ethics, the greater its susceptibility to facilitate litigation. Likely as not, there is a perception that litigation will be decreased as the ‘rules of engagement’ (compliance with standards) supplant the personal judgement that draws from accumulated experience and wisdom. Somewhat incongruously, it would appear that greater professionalism of practitioners is accompanied by an increased perceived exposure to litigation. But there is a twist – for recourse to the true and fair criterion may still be the best protection for the general public dealing with companies. Perhaps that places in proper balance the risks and rewards that characterise professional behaviour.

Here we draw on the UK FRC’s 19 May 2008 (PN 222) statement which commented on the recent (21 April 2008) QC opinion by Martin Moore. That opinion confirmed a series of earlier QC opinions in the 1980s in the UK which were augmented and reinforced by the UK FRC observation in its August 2005 PN 119 that true and fair was the ‘cornerstone of British corporate financial reporting’. Note that the changes in the UK companies legislation to accommodate the EU requirements did not alter the understanding that the true and fair status we are talking about here is a higher order criterion – indeed a *meta ethos* underpinning accounting disclosure.

It is reasonable to question whether increased regulation is compatible with professional activity – regulation generally needs rules by which improper conduct can be identified and penalised – professionalism requires the exercise of individual judgement?

1. Liebler, M. (2003), “True and fair - an imaginary view”, *Australian Accounting Review*, Vol. 13, No. 31, pp. 61-66.

* This the edited text of a BPEG seminar presented by Frank Clarke and Graeme Dean in June 2008

The following are examples of other BPEG activities in 2008/09

CSR Practitioners Group Workshop (sponsored by BPEG)

A unique collaborative relationship has been formed between BPEG and David Morrissey of 'CSR Practitioners Group, Sydney'. The objective of the collaboration is to jointly organise forums to provide opportunities for practitioners, academics, government officials and interested parties to engage with emerging issues and options relevant to Corporate Social Responsibility as well as networking.

On March 4 2008 the 'CSR Practitioners Sydney Group' and BPEG hosted a special dialogue with Senator Ursula Stephens, Parliamentary Secretary for Social Inclusion and the Voluntary Sector on the engaging topic of 'Corporate Social Responsibility and Social Inclusion'. It was not only an opportunity to meet Senator Stephens and listen to her views on the potential role for government in CSR issues but presented a unique opportunity for all participants to voice their views via group themed table discussions. These discussions centred on themes such as CSR incentives, stakeholders, measurement, legislation, need for CSR framework and education, and diversity in perspectives and business needs.

Practitioners were well represented from firms such as Vodafone, NRMA, Energy Australia, Australia Post, Gilbert & Tobin, IBM, Goldman Sachs Foundation, Westpac, Banarra and St James Ethics Centre. The ongoing relationship with 'CSR Practitioners Sydney' continues to be valuable as some BPEG members attended a CSR Practitioners meeting with Senator Nick Sherry at Goldman Sachs JB Were on 15th July 2008, discussing 'CSR – Back to the Future'. BPEG members look forward to more productive CSR sessions addressing issues that impact our future!

10th National Business Leaders Forum on Sustainable Development, Canberra*

BPEG sponsored two of its members to attend this important Forum in Canberra. The Forum was attended by CEOs and sustainability managers of Australia's larger organisations. The highlight of this year's forum was the launch of UN Global Compact Australia by Georg Kell, Executive Director Global Compact, who called for leadership and raised the question where this leadership should come from. The Forum also hosted the presentation of the Corporate Responsibility Index Awards.

One issue discussed at the Forum was the impact of the financial crisis – whilst it was acknowledged that the crisis hit some countries hard, it was stressed that developing societies and especially women were hit hardest. Insightful from an academic perspective were the calls from the CEO of CSIRO for more translators between science and research to business to increase the benefits of research on a practical level. The conference dinner speakers debated the role of community welfare and whether it is a means to control rather than to enable disadvantaged members of society. Andrew Forrest and Noel Pearson spoke for each side of the debate.

Overall, the Forum's tone was optimistic and most attendees viewed the financial crisis as an opportunity for a green recovery for Australia. This was explicitly clear in the comments and discussions during the workshop sessions on carbon solutions, green cities and the lead up to Copenhagen.

* BPEG members, Susan Shearing and Cornelia Beck would like to thank BPEG for sponsoring them to represent BPEG at this Forum.

A 3D maze rendered in shades of blue, with the word "Seminars" overlaid in white text. The maze is composed of thick, rectangular walls that create a complex, winding path. The lighting is dramatic, with deep shadows in the recesses and bright highlights on the raised surfaces, giving it a three-dimensional appearance. The word "Seminars" is centered in the lower right quadrant of the image.

Seminars

2009

The Business School is a Creature of its Time. What are the Ethical Challenges for the Academic and Professional Communities?

Professor James Guthrie, Chair, Discipline of Accounting, the University of Sydney and Suzanne Ryan, Senior Lecturer, Newcastle Business School

Client Capture and the Professional Service Firm

Professor Sally Gunz, School of Accounting and Finance, The University of Waterloo, Canada and Director of Waterloo's Centre of Accounting Ethics, Section Editor, Accounting and Finance: *Journal of Business Ethics*

2008

True and Fair: An Ethical Override

Honorary Professor Frank Clarke, Discipline of Accounting, the University of Sydney and Professor Graeme Dean, Discipline of Accounting, the University of Sydney

Corporate Responsibility and the Tobacco Industry: An Oxymoron

Professor Simon Chapman, Sydney Medical School, The University of Sydney

Corporate Social Responsibility and Social Inclusion

A workshop for corporate social responsibility practitioners with Senator Ursula Stephens and BPEG members

2007

Conference on Social and Environmental Accounting Research (CSEAR)

BPEG was an active partner in this conference, held at the University of Sydney, sponsoring an ethics-related stream of research papers

Leadership Integrity and Honesty

This seminar, held in conjunction with Work and Organisational Studies at the University of Sydney was presented by Professor Steven Grover, Department of Management, University of Otago

Financial Markets and Social Responsibility

Francis Grey, Australian Manager of the Dow Jones Sustainability Index in Australia

Using Simulations, Drama and Role Play in Teaching: The Case of Business Ethics Education

Kirsi Kettula-Konttas, Department of Forestry Economics, University of Helsinki, Finland

Publishing in the Journal of Business Ethics

Professor Sally Gunz, School of Accounting and Finance, The University of Waterloo, Canada and Director of Waterloo's Centre of Accounting Ethics, Section Editor, Accounting and Finance: *Journal of Business Ethics*

2006

Business Ethics: Analytical Versus Ideological Points of View

Professor Hans Ulrich Kuepper, Director of The Institute of Production Management Accounting, University of Munich

Ethics and the Accounting Profession

Richard George, Chair of the International Ethics Standards Board for Accountants, International Federation of Accountants

A 3D maze rendered in shades of blue, with the text "Student Society" centered in the middle. The maze is composed of thick, rectangular walls that create a complex, winding path. The lighting is dramatic, with deep shadows in the recesses and bright highlights on the raised surfaces, giving it a three-dimensional appearance. The text "Student Society" is written in a bold, white, sans-serif font, positioned centrally over the maze.

Student Society

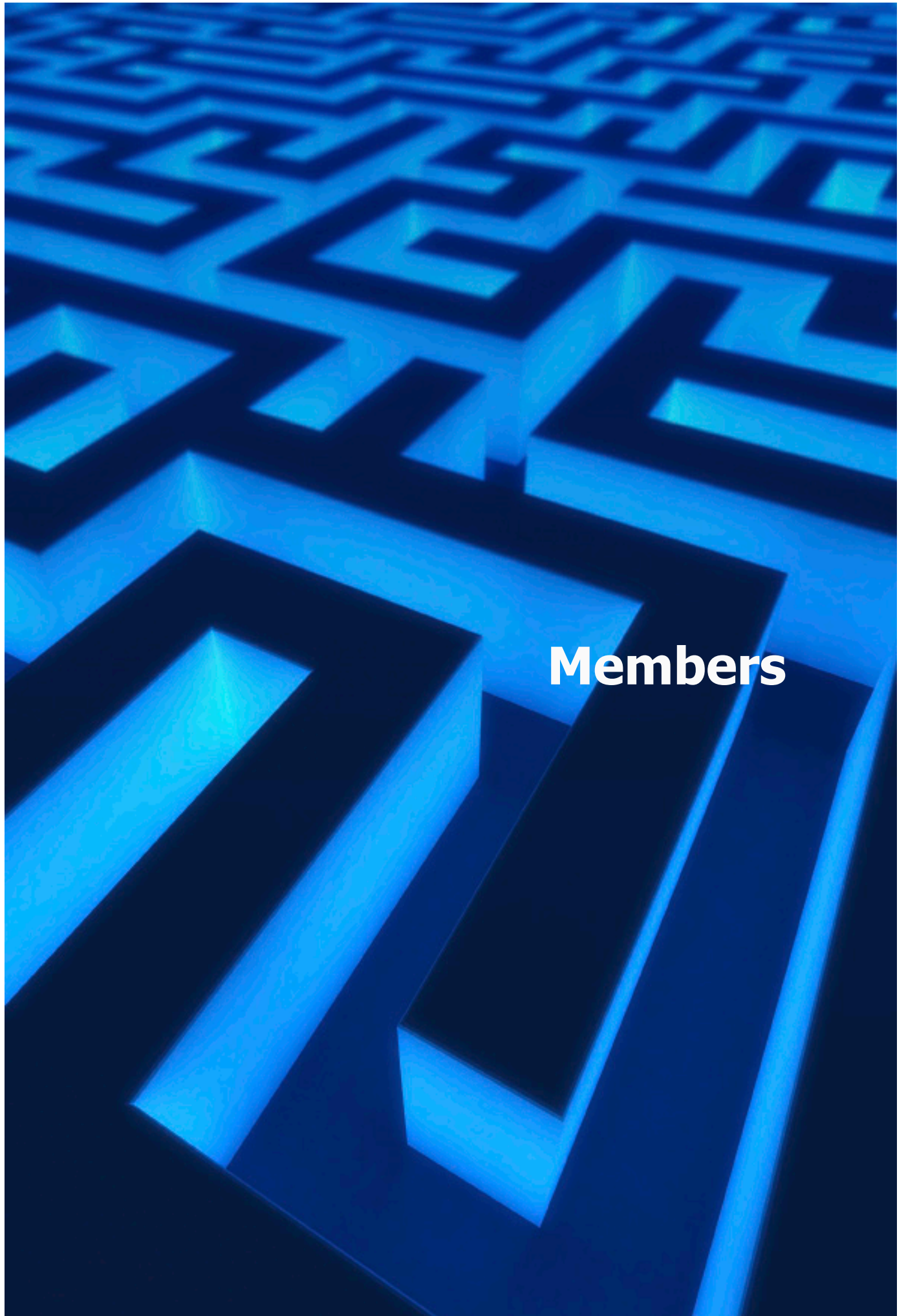
The Business and Professional Ethics Group (BPEG) Student Society's aim is to provide a forum for students to engage in issues related to business ethics. The society formed in its current context in 2008, with a new executive and close links to BPEG.

The Society is comprised of just over 130 members, maintained by eight executives. The bulk of membership is drawn from students in their first three years of study and by degree from students studying single or combined commerce or economics programs. The 2009 President of the Society is Chris Angelos, supported by a Vice President, Treasurer and Secretary and four additional general executives, who assist with every aspect of operations.

The Society held its first event, a student barbecue at the Merewether Lawns, in May 2009. The event had a successful turnout with a consistent flow of students over two hours being able to learn more about the Society and register their interest. The Society has since conducted another very successful barbecue and will be holding a panel discussion on corporate sustainability as it affects employees in October 2009.

The Society is beginning to work in partnership with other external bodies, student groups and Faculties. The possibility of Society members being able to undertake employment at the St James Ethics Centre is currently being explored. Members may also be able to participate in a nationwide business competition, on projects related to business ethics, through the Students in Free Enterprise initiative. In addition, the Society is looking closely at the possibility of an official extension of operations and membership to cover the Faculty of Law, given its recent move to main campus.

The Society is recognised on the Faculty Clubs & Societies Page and can be contacted via email at bpegss@gmail.com, and also has a page on Facebook under 'BPEG Student Society'.



Members

Executive Members

General Convenor
Nonna Martinov-Bennie, Accounting

Research Convenors
Nonna Martinov-Bennie
Angela Hecimovic, Accounting

Teaching Convenor
Henriikka Clarkeburn, OLTEB

Public Relations and Media Contact
Suzanne Jamieson, WOS

Students and External Relations Convenor
Sarah Fletcher, Careers and Employer Relations

Treasurer
Choong Liaw, Faculty Finance

Honorary Members

Irene Moss, Member of the Senate, the University of Sydney

Grant Michelson, Nantes School of Management

Associate Members

Rosemary Sainty, St James Ethics Centre

Susan Shearing, Sydney Law School

General Members

Cornelia Beck, Accounting

Amanda Carrigan, Business Law

Frank Clarke, Accounting

Teresa Davis, Marketing

Graeme Dean, Accounting

Charlotte Epstein, Govt and International Relations

Mark Freeman, OLTEB

Geoff Frost, Accounting

Sid Gray, International Business

Susan Greer, Accounting

James Guthrie, Accounting

Catherine Hardy, Business Information Systems

Geoff Hart, Business Law

Lisa Kelaher, Student Information Office

Harry Knowles, WOS

Janice Loftus, Accounting

Chang-Yuan Loh, Accounting

Brent MacNab, International Business

Barbara Mescher, Business Law

John Mikler, Govt and International Relations

Rohan Miller, Marketing

Rosina Mladenovic, Accounting

Daniel Nyberg, WOS

Sharron O'Neill, Accounting

Greg Patmore, WOS

Gail Pearson, Business Law

Chris Poullaos, Accounting

John Roberts, Accounting

Dominic Soh, Accounting

Rodney Smith, Govt and International Relations

Rod Tiffen, Govt and International Relations

Lesley Treleaven, OLTEB

Sandra van der Laan, Accounting

Nick Wailes, WOS

Brenda Ware, WOS

Rick Warr, Faculty IT

Susan Williams, Business Information Systems