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Insider Trading and the Case of Pro Golfer Phil Mickelson: Understanding the Legal, Ethical, and Social Responsibility Consequences

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ABSTRACT

Understanding how to trade legally can keep investors and ordinary citizens from legal difficulties. This writing focuses on the legal as well as ethical and social responsibility consequences of the "Mickelson case" of alleged insider trading of stocks. In this case, legal concepts and ethical theories related to insider trading as well as notions of social responsibility are provided for critical thinking in order to educate readers as to the basic precepts and concepts. The writing is in the form of a "case study," and thus detailed discussion questions are provided for educational and training purposes. As such, this case provides the legal concepts related to inside information trading for instructors and trainers to understand the importance of proper investing, morality and ethics, and social responsibility affecting management. The case can be used in management, finance, business law, ethics, and/or strategy, and particularly sports management, marketing, law, and ethics type courses.

Keywords: Insider trading, Inside information, Trading, Mickelson, Insiders, Tippers, Tippees, Relief defendant, Ethics, Morality, Social responsibility, Securities and exchange commission, SEC.

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1. INTRODUCTION

Insider trading has very recently been "front-and-center" in major media outlets involving an alleged insider conspiracy among an investment banker, the former chairman of Dean Foods, a sports bettor to whom he owed a great deal of money, and the famous, popular, professional golfer, Phil Mickelson, who also owed the sports bettor money. The major purpose of this case study, therefore, is for the reader to determine, based on the legal, ethical, and social responsibility herein whether professional golfer Phil Mickelson, the other two directly affected parties, as well as other stakeholders, acted in a legal, moral, and socially responsible manner.

In particular, the "Mickelson case" appropriately raises important legal issues that the authors address in this case study, to wit: the definition of material, nonpublic, information, the definition and nature of insider trading, the definition of an insider, the existence of conspiracy between an insider and

a tippee, and the critical distinction between insider trading and trading on inside information. As such, the first part of this case study is the legal section. The authors seek to determine the nature of material, nonpublic information and then to ascertain where the critical line between illegal and legal trading on such information is demarcated. As such, the authors review key security law statutes, SEC rules, pertinent case law interpreting statutes and agency rules, relevant legal and management commentary, as well as current events. The explication of security regulation law herein is not meant to substitute for a securities law attorney or for that matter a securities regulation course; rather, the authors attempt to provide the reader with sufficient information on key aspects of securities law so as to educate the reader as to his or her rights and responsibilities pursuant to the law and to use the legal principles in the discussion questions part to this case study to make principled based and reasoned legal determinations pertaining to the "Mickelson case" and to engage in some thought-provoking legal discussion. Note that the authors put the phrase "Mickelson case" in quotation marks since, as will be seen, no formal charges were brought against the golfer.

Actions, moreover, have more than "mere" legal consequences. Though the law tries to achieve justice, the law is not always just and fair. Accordingly, in the next major section of the case study the authors examine ethics which is a branch of philosophy. As such, four major Western ethical theories are explicated: Ethical Egoism, Ethical Relativism, Utilitarianism, and Kantian ethics. The authors then show how these ethical theories and the principles can be used to make moral determinations, specifically regarding Mickelson and the other affected parties and stakeholders as well as generally in business and otherwise. As with the legal principles the ethical principles can be utilized for critical thinking and to make moral determinations in the "Mickelson case."

Finally, above and beyond law and ethics is the notion of social responsibility, and, as applied to business, corporate social responsibility. Accordingly, in the third major section of the case study the authors attempt to define the term "social responsibility" as well as a major component thereto – the concept of "sustainability." The definitions of these terms can be formulated as principles for the reader to apply to business generally as well as to the "Mickelson case" as per the discussion questions. So, what exactly is involved in this so-named "Mickelson case"?

2. THE FACTS

In May of 2016, several media outlets, including the *Wall Street Journal* (Viswanatha, Hong, and Rothfeld, 2016) the *New York Times* (Goldstein, Protess, and Stevenson, 2016) and *Bloomberg Business Week* (Kolhatkar, 2016) reported that the U.S. Department of Justice and the Securities and Exchange Commission (SEC) announced the commencement of legal proceedings against a corporate executive, a sports gambler, and the famous professional golfer, Phil Mickelson. The corporative executive is Thomas C. Davis, the former chairman of Dean Foods Co., as well as a retired investment banker from Credit Suisse, who was very heavily in gambling debt to legendary sports gambler, William "Billy" Walters, who is considered one of the most successful sports bettors in the country (Viswanatha, Hong, and Rothfeld, 2016; Goldstein, Protess, and Stevenson, 2016; Kolhatkar, 2016).

Phil Mickelson, who has a reputation for betting on sports, was also in debt to the gambler. Actually, as the *Wall Street Journal* (Rothfeld and Berzon, 2016) reported, Phil Mickelson likes to gamble; his gambling was "sizeable"; and he was a well-known figure at the Las Vegas betting scene, where he bet heavily at the tables and on football games. Moreover, twice in 2015, separate criminal charges were instituted

against people with whom Mickelson was involved in gambling transactions, and these charges included allegations of insider trading (Rothfeld and Berzon, 2016). To illustrate the extent of his gambling the *Wall Street Journal* (Rothfeld and Berzon, 2016) also noted that in an almost three year period between 2000 and 2003 Mickelson lost nearly $2.5 million gambling in Las Vegas casinos, which debt was paid. Mickelson should be able to repay his gambling debts as he has been said to have made almost $80 million during the course of his playing career as a professional golfer (Kolhatkar, 2016). Mickelson is regarded as a "preferred customer" in Las Vegas, meaning the casinos are willing to extend him credit, as well as occasionally to allow him to exceed his credit line (Rothfeld and Berzon, 2016). Mickelson did win $540,000 on a bet on the 2001 Superbowl; so he is not a "complete loser" (Rothfeld and Berzon, 2016). Nevertheless, the recent gambling and insider trading allegations are bringing unwelcome attention to Phil Mickelson as well as dredging up past gambling and gambling associations with people who apparently do not have, to say the least, the most stellar reputations, all of which and whom are being extensively reported in the *Wall Street Journal* (Rothfeld and Berzon, 2016).

In the current case, the government believes that Mr. Davis passed on inside information to Williams, who then passed the secret data on to Mickelson. Specifically regarding Mr. Mickelson, the complaint by the Securities and Exchange Commission states that he "received gains from trades based on material nonpublic information," that he had no legitimate right to these gains, that he received the gains as a result of the securities law violations of the other two defendants, and that under the circumstances it would "not be just, equitable, or conscionable" for Mr. Mickelson to retain those gains (Rosenfeld, 2016). The government apparently had been conducting an investigation for over two years. As a result of the charges, Davis has pled guilty to criminal charges and is cooperating in the case against Billy Walters. Davis has also pled guilty to perjury for initially lying to government investigators when he said that he had never given information to Billy Walters. Walters has been arrested and has been charged with 10 counts of securities fraud, insider trading, and wire fraud. His attorney said that any trading was based on mere speculation and not based on trading on sufficiently objective and factual information (Viswanatha, Hong, and Rothfeld, 2016; Goldstein, Protess, and Stevenson, 2016; Kolhatkar, 2016).

The government, however, is just proceeding civilly against Mickelson, who was not charged with any criminal wrongdoing. Mickelson has agreed to pay to the SEC more than $1 million, including interest, based on the trading he did based on a tip from Billy Waters, who is a long-time friend, a member of the same country club, and a golfing buddy of Mickelson. Actually, Billy Walters is an accomplished amateur golfer as well as a developer of golf courses. He also knows Davis well as he met Davis on a golf course when they both lived in Southern California. They have known each other for more than 20 years (Viswanatha, Hong, and Rothfeld, 2016; Goldstein, Protess, and Stevenson, 2016; Kolhatkar, 2016).

Apparently, Mickelson owed a gambling debt to Billy Walters, which was to be repaid in part from the profits Mickelson was to make from trading in Dean Foods' stock based on the tip from Davis given to Mickelson by Billy Walters. The government also said that Mr. Davis was "desperate for money" and thus sought financial help from Billy Walters. For example, Davis owed a casino debt of $100,000, which he paid by taking money from a Dallas charity for battered women and homeless children. Furthermore, in one instance, Billy Walters gave Davis $1 million to repay this amount and other obligations. In exchange for this help Davis regularly provided Walters with a large number of tips regarding Dean Foods' earnings and other market-moving information. Another alleged tip dealt with a plan by certain investors to take a stake in the restaurant conglomerate, Darden Restaurants, the parent company of Olive Garden

restaurants, and then break it up and spin-off certain divisions (Viswanatha, Hong, and Rothfeld, 2016; Goldstein, Protess, and Stevenson, 2016). Moreover, there was another supposed tip that Dean Foods was going to announce a spin-off and sale of its organic food unit (Kolhatkar, 2016).

Mr. Davis was under a confidentiality and non-disclosure agreement with the investment group at the time. The SEC says that as a result of this tip and others from Davis, Billy Walters made illegal profits and avoided losses totaling more than $6 million over a six year period. Moreover, the government alleges that Billy Walters instructed Davis to use the secret code term, "Dallas Cowboys," when referring to Dean Foods, and he also gave Davis a pre-paid cell-phone. As a result of the tips by phone or after personal meetings Billy Walters repeatedly called his Las Vegas broker to buy tens of millions of dollars in Dean Foods' shares (Viswanatha, Hong, and Rothfeld, 2016; Goldstein, Protess, and Stevenson, 2016; Kolhatkar, 2016). Mr. Walters has pleaded not guilty to the charges (Hong, 2016).

After Billy Walters learned of the planned Darden breakup and "spinoff" from Davis, Billy Walters then allegedly told Mickelson, who then purchased 240,000 shares of Dean Foods' stock in three separate brokerage accounts; and Mickelson then sold his shares, making a $931,000 profit when the stock rose 40% when news of the "spinoff" became public. Mr. Mickelson then paid his gambling debt to Billy Walters in part with those trading profits. Mickelson was then sued by the SEC to recover those profits, but he was not charged criminally with insider trading, which *Bloomberg Business Week* called a "seemingly miraculous escape" (Kolhatkar, 2016). Technically, Mickelson was named as a "relief defendant" in a civil case, wherein the government argued that Mickelson was "unjustly enriched" from the trades, and thus he must return his "ill-gotten" gains, which he did. Technically, being named as a "relief defendant" means that "Mr. Mickelson was not accused of any legal violations but was alleged to be in possession of ill-gotten gains to which he had no lawful claim" (Rosenfeld, 2016). Attorneys for Mickelson said that the golfer did not engage in any wrongdoing (Viswanatha, Hong, and Rothfeld, 2016; Goldstein, Protess, and Stevenson, 2016; Kolhatkar, 2016). And when the SEC's Enforcement Director was asked why Mickelson was not charged he said that charges have to be justified "based upon the evidence and the law" (Viswanatha, Hong, and Rothfeld, 2016). So, what precisely is the law that could apply in the "Mickelson case"?

3. THE LAW

This legal section to the case study is an examination of certain basic legal principles in the field of securities law and regulation, especially regarding insider trading. As emphasized by the authors, this legal section is not an exhaustive treatment of a very complicated and at times vague area of the law. Rather, the purpose of the authors has been to supply sufficient basic principles regarding securities regulation, particularly securities fraud and insider trading, to educate the reader and to allow the reader to make some principled and reasoned determinations as to the legality of the trading practices in this case study. Yet the "law is the law" and thus the starting point for analysis. The law, as underscored, tries to be just but at times fails in that laudatory goal. Accordingly, the law must be juxtaposed with, yet differentiated from, morality and ethics as well as concepts of social responsibility. And, most importantly, the reader must be made cognizant of the fact that there are many moral gaps in the law, meaning that an action might be legal but immoral based on ethics. Such a result very well may be the case when the discerning reader perceives the distinction between insider trading and trading on inside information. Attorneys, of course, will be ready, willing, and able to advise business people and others on the legality of their actions – stock

trading or otherwise – so as to avoid lawsuits and legal liability. Yet, "to be forewarned is to be forearmed"; and thus it is always good to learn some basic "preventative law."

There are three main security statutes in the United States: the Securities Act of 1933 (which is essentially a disclosure type statute for companies offering new or subsequent issues of securities to the public), the Securities and Exchange Act of 1934, and the Sarbanes-Oxley Act of 2002. There is also a very important agency rule made pursuant to the 1934 Act – Securities and Exchange Commission (SEC) Rule 10b5. The focal point of this study is the 1934 Act and Rule 10b5. The 1934 Securities Exchange Act is a very broad anti-fraud statute. Section 10(b) makes illegal – civilly and criminally – any knowing, intentional, and material misrepresentations, fraud, deceit, omissions, as well as manipulation regarding the purchase and sale of securities (Securities Act of 1934; Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). Manipulation can be in the form of "pump and dump" schemes, making false "tips" under aliases, and placing false orders (Patterson and Rothfeld, 2014). However, the wrongful conduct, it must be emphasized, must be knowing and intentional misconduct (to satisfy the "scienter" or "bad intent" requirement of the law) as opposed to just negligent or careless conduct in making "mere" misstatements or omissions (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). In addition to civil proceedings by the SEC and criminal prosecutions by the Department of Justice the courts have recognized a private cause of action pursuant to the 1934 Act whereby an aggrieved private party can institute a civil action for the rescission (that is, cancellation by the court) of the securities contract and transaction and for money damages (that is, restitution in the form of the return of the illegal profits made by the wrongdoer) (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012).

Pursuant to the 1934 Act, the SEC has promulgated Rule 10b5 which prohibits fraud regarding the purchase and sale of any security (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). Another principal purpose of Rule 10b5 is to prohibit and prevent "insider trading," which generally means a person is buying or selling securities based on the possession of information not yet available to the public. Also important to mention is SEC Rule 10b5-2 which prohibits people in a relationship of trust and confidence from trading on material confidential information received as part of this relationship. As such, pursuant to Rule 10b5-2 if one knows either explicitly or implicitly that information is delivered in confidence, or there is a pattern of sharing confidences between the parties, then the recipient cannot trade on the information (Yadav, 2015). SEC Rule 10b5, the prohibition against insider trading, and the critical distinction between insider trading and "merely" trading on inside information are the focal points of this case study. The 2002 Sarbanes-Oxley Act (SOX) statute was promulgated as a result of the Enron scandal. This statute is beyond the purview of this case study except to note that SOX materially expanded the criminal punishment for securities law violations, including insider trading, up to (what some might say as a draconian) 20 years of imprisonment (Sarbanes-Oxley Act of 2002, Section 1106; Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012).

A. SEC Rule 10b5 - Insider Trading vs. Trading on Inside Information

Pursuant to the power delegated to the agency by the 1934 Securities Exchange Act, the Securities and Exchange Commission promulgated Rule 10b5, which is the preeminent law in the U.S. governing insider trading. Insider trading is clearly illegal – civilly and criminally. Rule 10b5 holds that it is unlawful

for any person, directly or indirectly to use any device, scheme, or artifice to defraud, to make any untrue statement of material fact or to omit any material fact that are misleading, and to do any act, practice, of business that operates or would operate as a fraud or deceit on a person in connection with the purchase or sale of any security (17 *Code of Federal Regulations*, Section 240.10b5). Yet, though seemingly very broad in scope, as will be seen, the law is not a "blanket" prohibition on trading on inside information; rather, the courts have interpreted Rule 10b5 to allow trading in two narrow circumstances. First, though, it is necessary to establish the predicate for insider trading and next to determine who can be liable for insider trading. Finally, the two exceptional circumstances of legally trading on inside information will be explicated.

B. The Legal Foundation for Insider Trading

Insider trading is based on trading on material, nonpublic information. First, one needs "information," which is the predicate for the legal wrong. Pursuant to securities law, information is narrowly defined. Information for the purposes of insider trading is based on objective, factual, historical, and/or scientific information, for example, the earnings report for the last quarter, the merger plan, an impending takeover, or the geologists report on the discovery of natural resources. As such, rumors, speculation, opinions, predictions, and statements in the form of questions are not usually sufficiently factual to be construed as "information" (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). Yet a major problem emerges in security law and that is that people do not make predictions, give opinions, or for that matter ask questions, in a vacuum. That is, normally, opinions and predictions as well as questions are based on some facts. Consequently, the perplexing question emerges as to how many "facts" there have to be in a question or "opinion" or a "prediction" to turn it into a legal "fact," and consequently serve as the initial foundation for insider trading liability. The answer to that difficult question is beyond the purview of this case study; yet in one sense the answer is "simple" in that a jury would typically have the final say in making that critical determination. Assuming there is the necessary "information," the next step is to ascertain if the information is sufficiently "inside," that is, nonpublic.

Once there is "information" the second requirement for legal liability is that the information must be "inside"; that is, the information must be proprietary, confidential, secret, and private. The information must be nonpublic. Once information "goes public" it can be traded on. Moreover, the Securities and Exchange Commission maintains that investors must wait a "reasonable" amount of time after disclosing the information before trading (Schipana and Seyhun, 2016). Yet, "what constitutes a reasonable time depends on the circumstances of the disclosure" (Schipana and Seyhun, 2016). Examples of non-public inside information have been: earnings reports (United States v. Newman, 2014; SEC v. Dorozhko, 2009) natural resources discoveries (SEC v. Texas Gulf Sulphur Co., 1968) tender offers (United States v. O'Hagan, 1997) corporate mergers and takeovers (United States v. Salman, 2015; Chiarella v. United States, 1980) evidence of company fraud in the form of inflated asset prices (Dirks v. SEC, 1983) financial plans for funding the company (U.S. v. Cuban, 2010) the sale of the company to another company (United States v. McGee, 2014) a change in leadership (SEC v. Ingoldsby, 1990); the fact that the company was going to be sold at a much higher price than its market value (United States v. Chestman, 1991) the fact that the company would be receiving fewer orders from one of its largest customers (SEC v. Adler, 1998) the fact that the company had a list of companies it would not trade with

because the company was working on transactions with those companies (United States v. Teicher, 1993) and a reduction in earnings (Investors Management Co. v. SEC, 1971). However, even if the information is deemed to be legally "information," and even if it is deemed "inside" and "non-public," there is still one more step in determining liability – the "materiality" of the information.

The third and final foundation requirement is materiality. As such, in order to serve as the foundation for legal liability the non-public information must be "material." The U.S. Supreme Court in the case of Basic, Inc. v. Levinson (1988) emphasized that there are two requirements for materiality of information: 1) "a substantial likelihood that a reasonable shareholder would consider it important" in buying or selling securities; and 2) "a substantial likelihood that the disclosure of the omitted fact would have been viewed by the reasonable investor as having significantly altered the 'total mix' of the information available" (pp. 231-32). The Second Circuit Court of Appeals had previously stated the following factors: whether a reasonable person would attach importance to the information in determining his or her choice in the transaction in question; and whether the information under reasonable and objective contemplation would affect the value of a company's stock.

Materiality, in essence, is information which the reasonable investor might believe would be likely to cause an increase or decrease in the price of the shares of stock based on all the information available to him or her, for example, information regarding a merger or fundamental corporate change, a profit or loss announcement, a dividend change up-or-down, a new discovery of natural resources or a product or process, bankruptcy or reorganization, or lawsuits against the firm (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). A leading case as to "materiality" is the federal appeals court case of SEC v. Texas Gulf Sulphur Co. (1968) where the court held that the company's discovery of a rich ore deposit was "material," and thus several of its insiders, including directors, officers, and employees, could not trade on the information before an announcement of the discovery because the information would affect the judgment of reasonable investors. Other examples are the federal district court case of United States v. Corbin (2010) where information pertaining to numerous impending acquisitions of publicly traded companies was deemed to be material; and the Supreme Court case of Dirks v. SEC (1983) where the fact that the company had overstated its assets due to fraudulent accounting practices was also deemed to be material.

However, as with a great deal of securities law, the definition of "materiality" is not a precise one. As such, Anderson (2016) asks: "Who is the 'reasonable shareholder' or 'reasonable investor'? Is she small or institutional, a short-term speculator or a long-term investor? What constitutes a 'total mix' of information"? The Wall Street Journal (Chasan and Rubenfeld, 2015) notes that regarding "materiality", "There is a lot of gray area." Nevertheless, even if there is information which is nonpublic and confidential, if such information is deemed to be immaterial, then one can safely trade on it. Now, assuming that information is inside and material, the next step is to be aware of the two competing theories of liability for trading on such information – the broad theory and the narrow theory.

C. The Two Competing Theories of Liability

There are two competing legal theories pertaining to the legality of trading on inside information – the broad theory, also called the "level-playing-field" theory, and the narrow theory, also called the "insider" or "misappropriation" theory. Pursuant to the broad theory, anyone who knowingly trades on material, inside information, however acquired, commits a legal wrong, which is why the theory is at times called

the "level-playing-field" theory (Harasmimowicz, 2016; Klaw, 2016; Cheesman, 2016; Cavico and Mujtaba, 2014; Clarkson, Miller, and Cross, 2012; Coffee, 1990). However, the broad legal theory, though based on notions of fairness and equity, is merely the historical one, provided by the authors of this case study for comparison purposes. Rather, the prevailing legal theory is now the narrow or "insider" one, though from an ethical standpoint, it can be argued that the older, historical, broad theory is the moral one (Klaw, 2016). Yet, regardless of any moral or ethical debate, the narrow theory is the law today. Yet, as the discerning reader will soon see, the "narrow" theory is not quite that narrow.

The narrow theory encompasses three types of potential legal violators regarding trading on material inside information: "misappropriators," insiders, and tippees of insiders. Misappropriation of material inside information and then trading on the information is clearly a civil and criminal law wrong under securities law. "Misappropriators" are thieves who steal or "hack" (illegally accessing and stealing information from computer servers) inside information, or people who bribe insiders for the information, or who employ fraud, deceit, or trickery to obtain inside information. In addition to the securities law violations "misappropriators" would be liable for the theft, computer, bribery, and fraud offenses (Cheesman, 2016; Geiger,Riley, and Robertson, 2015; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012).

Secondly, corporate insiders may be liable. Corporate insiders who trade on their own company's inside information clearly commit a legal wrong. The disadvantages and harm to innocent and ignorant third parties - shareholders or members of the general public, who buy from or sell stock to the insiders under such circumstances are patent. Yet, the question arises as to who exactly is an "insider"? Moreover, here, one is confronted with a somewhat of a paradoxical situation in securities law; that is, the key foundational element of "information" is narrowly construed; whereas the definition of an "insider" is very broadly construed. Insiders include the company's directors, officers, and employees (though it is likely that only the higher level employees and their assistants) will have access to confidential information; but the term has been interpreted to encompass not only technical "employees" but also "outsiders" in the form of independent contractors, consultants, and agents, such as the company's non-employee sales force, lawyers, accountants, investment bankers, and stockbrokers (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012).

Now, a corporate insider is not going to be so stupid (Is s/he?) to personally trade on the company's confidential information. Rather, typically, the insider will pass the information along to a spouse, family member, friend, or trusted "outsider" in the form of "tips," and this person will do the trading. If the person who receives the information is deemed to be the "tippee" of the insider there is potential liability for both pursuant to insider trading law (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). So, tippees of insiders are the third category of people to potentially run afoul of securities law. However, the courts require that the tippee be in conspiracy with the insider, which is a difficult evidentiary burden for the government to surmount, especially if there is a long and attenuated communication chain between or among (multiple) parties (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). The courts also require as part of this insider trading conspiracy that the insider who tipped off the recipient tippee be in breach of a fiduciary duty as well as actually receive something of personal tangible benefit for passing along the information; and also that the tippee knew (or should have known) of the breach of the fiduciary duty, that the information was not public, and that the tippee received a benefit, typically monetary, from the information too (Stockman, 2015; Kendall,

2015; and Matthews, 2014; Protess and Goldstein, 2014). Assuming some sort of legally recognized "benefit" as well as the other legal requirements, the insider tipper, the tippee as well as any remote tippees (down-the-chain of communication) are thus potentially liable civilly for fines and restitution for any profits made from their illegal insider trading conduct (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). The aforementioned parties are also subject to criminal prosecution and punishment, which as noted as per SOX, can include lengthy prison terms. For example, a hedge-fund manager was given a six and one-half year sentence for being part of a "criminal club" of hedge-fund managers who tipped each other on non-public information about technology companies. An even more severe example is the case of another hedge-fund manager who was given an 11 year prison term for making more than $50 million in illicit profits from tips through insiders at tech companies and brokerage houses, though the government initially asked for a 19 year sentence (Popper and Hamilton, 2011). The general rule, therefore, is that misappropriators, insiders, and tippees in conspiracy with insiders commit serious legal wrongs – criminal and civil – for insider trading. So, then, who can trade on inside information? There are two "exceptional" situations for people legally trading on inside information – the "lucky" and the "smart."

D. Legally Trading on Inside Information

It's always good to be lucky, right? To have, as Machiavelli said, "the Goddess Fortuna to smile at you." So, perhaps such a "fortunate" person hears or sees something that he or she was not supposed to, for example, two CEOs loudly talking in the elevator about the planned merger (which obviously they should not be doing and very likely their corporate code of conduct prohibits this type of public discussion). Assuming there was no impermissible eavesdropping, hacking, monitoring, or surveillance, the recipient of the information merely happened to be "at the right place at the right time," and thus "stumbled" on the information. Accordingly, this "lucky" person, called in the law an "inadvertent tippee," can legally trade on the information, which technically is "inside" information (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). The inadvertent tippee exception, therefore, does provide some legal latitude for trading on inside information but only if one is "lucky" (and then knows how to intelligently "leverage" his or her luck!).

The inadvertent tippee rule, however, is constrained by one exception – well, technically, an exception-to-the exception – the "inadvertent tippee" in a fiduciary relationship rule. This rule holds that if one is a professional, for example, a doctor, lawyer, accountant, psychiatrist, psychologist, etc., in a fiduciary relationship (that is, one of trust and confidentiality) with a patient or client, and if the professional happens to hear or see something of a confidential nature, then the professional cannot trade on the information; and to do so would be a violation of the fiduciary relationship as well as a legal wrong under securities laws (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012).

The second category of people can legally trade on inside information – the "smart." These people are typically market professionals, that is, security analysts, who based on legitimate public sources of information, and using their own knowledge, skills, and intelligence make deductions (presumably correct ones!) that reflect certain information that is not yet public (Cheesman, 2016; Cavico and Mujtaba, 2014; and Clarkson, Miller, and Cross, 2012). The market professional is a very good "speculator" and makes a substantial profit – legally! Market professionals are not insiders; they do not

steal anything; no one tipped them off; they did not bribe insiders for information; rather, they are diligent, resourceful experts in certain sectors of the economy, and of course very smart (and hopefully a bit lucky too). Any person, theoretically, can be a market professional (assuming the time, effort, money, and education involved) or one can hire market professionals to do one's trading or simply read their views in publications or watch them on the media. This "smart" exception can be justified that it is good for the markets, the economy, and society as a whole to allow market professionals to "ferret out" and deduce by legitimate means information that is still technically "inside" (Coffee, 1990). The overall positive result is maintained to be a more efficient market (Epstein, 2016).

Therefore, assuming the predicate of non-public, material information has been established, and notwithstanding liability under the general rule, the law does provide legal latitude for trading on inside information in two exceptional cases – trading by the "lucky" and the "smart." One can be "lucky," as noted, as well as be "smart"; and thus use public information to deduce and to speculate as to the existence of information that is still confidential, and trade on that confidential information. Of course, the more speculation and the more of a substantial risk there are in the transaction, the less likely there will be any legal problems. However, if a case involves a corporate insider trading on his or her own firm's inside information, or the tippee in conspiracy with an insider doing the same, it is going to be, realistically speaking, exceeding difficulty for the insider and the tippee to claim that they were "merely" lucky or smart. That point is clear at least, that is, it is illegal for a corporate insider to use material, non-public information to trade in the shares of his or her company's stock. Yet, as underscored, that type of insider trading does not cover all that is potentially illegal.

In summary, this legal part to the case study was a succinct explication of legal principles governing trading on securities, particularly the legal wrong of insider trading. Yet as emphasized in the legal section to this case study, for any type of case the government needs evidence to satisfy its burden of proof and persuasion and to convince a jury of criminal guilt or civil liability. And as Epstein (2016) underscored: "To get evidence on particular transactions requires a massive inquiry." Consequently, the more lengthy, attenuated, stretched out, and convoluted the causation chain is between an insider and the ultimate recipient of the information the more difficult it is going to be for the government to persuade "beyond a reasonable doubt" a jury (a unanimous federal jury of 12 people) of a conspiracy between an insider and a tippee; rather, the eventual recipient of the information would contend that what was received was not technically "information" (and thus not illegal information, but just some rumors, speculation, or "loose talk" casually overheard (and thus legal to trade on). Moreover, the courts require that the government demonstrate that the tippee knew that the non-public information came from an insider and that the tipper-insider received a personal benefit or tangible reward. Therefore, the law of insider trading does have some latitude for trading on inside information for the "lucky" and the "smart." Moreover, the government, especially in a criminal prosecution does have a very difficult evidentiary burden to surmount. Consequently, it is possible to engage in legal trading on inside information. Yet is it moral to do so? Morality perforce brings one into the realm of ethics and philosophy.

4. ETHICS

Philosophy is the study and analysis of deeply problematical and fundamental questions, such as the nature of reality, thought, conduct, and morality. Ethics *is* a branch of philosophy. Moral philosophy is the philosophical study of morality; it is the application of philosophy to moral thinking, moral conduct, and

moral problems. Moral philosophy encompasses various theories that prescribe what is good for people and what is bad, what constitutes right and wrong, and what one ought to do and ought not to do. Moral philosophy offers ethical theories that provide a theoretical framework for making, asserting, and defending a moral decision. There is not one determinate set of ethical theories. Moral philosophy embraces a range of ethical perspectives and spends a great deal of time in analyzing the differences among these ethical views. Moral philosophy attempts to establish logical thought processes that will determine if an action is right or wrong and seeks to find principled ethical criteria by which to distinguish good conduct from bad conduct (Cavico and Mujtaba, 2013, 2016).

"Ethics" is the theoretical study of morality. Ethical theories are moral philosophical undertakings that contain bodies of formal, systematic, and ethical principles that are committed to the view that an asserted ethical theory can determine how one should morally think and act. Ethics is the sustained and reasoned attempt to determine what is morally right or wrong. Ethics is used to test the moral correctness of beliefs, practices, and rules. Ethics necessarily involves an effort both to define what is meant by morality and to justify the way of acting and living that is being advocated. Ethics proceeds from a conviction that moral disagreements and conflicts are resolvable in a rational manner. The purpose of ethics is to develop, articulate, and justify principles and techniques that can be used in specific situations where a moral determination must be made about a particular action or practice. When a decision involves a moral component, the decision necessarily encompasses ethical theories and principles (Cavico and Mujtaba, 2013, 2016). Accordingly, in this case study, the readers are being exposed to secular, Western-based ethics. Specifically, the four secular-based Western ethical theories that will be discussed in this case study are: Ethical Egoism, Ethical Relativism, Utilitarianism, and Kantian ethics (Cavico and Mujtaba, 2013, 2016).

A. Ethical Egoism

Ethical Egoism should be a very acceptable and accommodating ethical theory for anyone, especially a business person, because pursuant to that theory it is moral to advance one's self-interest, to prosper, and to make money. One does focus on the reasonably foreseeable consequences of an action; but with a narrow "selfish" perspective by ascertaining only how the consequences might impact oneself. However, an "enlightened" ethical egoist, such as Adam Smith, would counsel to take a long-term perspective as to maximizing self-interest, and thus one should be willing to undergo some short-term expense, sacrifice, and effort in order to advance one's self-interest in the long-term. Also, even if one has a big ego as well as a lot of power, the ethical egoists would advise that it is best to treat people well, and not necessarily because one loves them, or even likes them, but it will usually inure to one's benefit to treat people well and make them colleagues, allies, and part of the "team." So, in the case study herein one would ask pursuant to Ethical Egoism and seek to determine if Phil Mickelson was likely to advance his long-term self-interest by engaging in the trading activities under the circumstances presented.

B. Ethical Relativism

The second ethical theory is Ethical Relativism (Cavico and Mujtaba, 2013, 2016). "When in Rome, do as the Romans," as the old saying goes. Pursuant to this ethical theory, an action is moral if a society believes it to be moral. Consequently, societal norms become the standard for morality. All one has to do is to ascertain the moral norms of a particular society and adopt them and conform, and one will be acting

morally. Of course, one will need a definition of "society," which can be a challenge indeed. For example, is a minority group within a larger society a society? Is a minority group within a minority group a society? And what about a segment of society, such as, perhaps, the "corporate executive country club set" or the "world" of professional athletes or professional gamblers, are they, or any part or combination thereof, a society? Once one determines exactly what a particular society is and then what their moral norms are all one has to do is to conform and adapt and one will be acting morally in that society. However, it is important to underscore that just because a practice is deemed to be moral in a society the business person must be aware that there may be a superseding law that makes a culturally accepted practice, such as bribery in a society or as here giving stock tips to friends and associates, illegal. Ethical Relativism is not a defense to charges of illegality based on the law.

C. Utilitarianism

The third ethical theory is Utilitarianism, which is a relatively modern ethical theory created by the English philosophers and social reformers, Jeremy Bentham and John Stuart Mill (Cavico and Mujtaba, 2013, 2016). The core principle to this ethical theory is: "An action is moral if it produces the greatest amount of good for the greatest number of people." Accordingly, this ethical theory is a consequentialist ethical theory; one must predict consequences; one must ascertain whether the consequences are good or bad, cause pleasure or pain, happiness or dissatisfaction; and then must measure and weigh consequences. If there are predominant good consequences, the action is a moral action; and if there are predominant negative consequences the action is immoral. But it must be emphasized that even if an action is moral there still may be some pain, which means that "ends can justify means"; yet everyone got "counted," everyone's pleasure and pain was registered based on this egalitarian ethical theory. As a practical bit of advice, the authors would suggest that when predicting consequences one should make those determinations within separate and distinct stakeholder groups, as that approach would "channel" and thus make more manageable the predictive aspect of this ethical theory; and many readers of this case study should be familiar with stakeholder analysis too. For example, the consequences of the merger should be examined in the context of the following key stakeholder groups: shareholders, employees, unions, consumers/customers, suppliers and distributors, local communities, government, competition, and society as a whole. In the "Mickelson case" in order to determine if the professional golfer's actions were moral pursuant to the Utilitarian ethical theory would have to predict, measure, and weigh the consequences of the trading on Mickelson, of course, but also on all the other stakeholders directly or indirectly affected by his actions.

Utilitarianism does have several positive attributes: people should be used to its integral element of predicting consequences (as they do it for themselves); the theory takes a broad approach to ascertaining morality; all people and stakeholders directly and indirectly affected by an action are examined; everyone gets "counted"; there are no special and privileged people; everyone's pleasure and pain is registered; and thus the Utilitarian theory is a very egalitarian one. However, one big problem can arise when the "counting" is done since there may be a predominance of good consequences caused by the action, which means it is moral pursuant to this ethical theory; but there still may be some lesser bad, and perhaps very "painful," consequences to a minority of people affected by the action. Nevertheless, despite some negative consequences the action is moral pursuant to Utilitarianism.

D. Kantian Ethics

Finally, the fourth ethical theory is Kantian ethics, which is also a relatively modern ethical theory but one diametrically opposed to Utilitarianism (Cavico and Mujtaba, 2013, 2016). Regarding Utilitarianism, Kant condemned that ethical theory as being immoral because it could morally justify pain, suffering, and exploitation. That is, the problem of the "ends justifying the means." So, Kant declared that one should disregard consequences in making moral determinations. Thus, as the discerning reader can plainly see, a major problem emerges in Western ethics due to the conflict between the two modern ethical theories. So, how does Kant determine morality? Morality is based on a formal test that Kant called Categorical Imperative. "Categorical" because, according to Kant, this is the supreme, absolute, and only test for morality; and "Imperative" because at times one must compel oneself to be moral, that is, to do what one's reason tells one is the "right" thing to do, even though there may be some negative consequences to one personally (for example, "blowing the whistle" on one's polluting company and getting oneself fired). Have a "good will," declared Kant. That is, be morally strong, have a good moral character, do your duty – not necessarily to the law or to the state – but your duty to yourself - do what your mind tells you is the moral thing to do, regardless of consequences. Overcome fear, lust, greed, envy, an overarching ambition, go perhaps "above and beyond" the law, and do the "right" thing. So, what is the "right" thing to do pursuant to the Categorical Imperative?

Since Kant wants one to be very sure that one is acting morally, within the Categorical Imperative there are three main tests for morality that one must apply to the action itself to determine its morality; and all three tests must be passed; all these tests are interrelated. The first is the Universal Law test. Under this test one must ask if the action one is contemplating would be one that one, hypothetically, would be willing to make into a universal "law." That is, for example, take the actions of cheating, lying, and stealing. Would one want to live in a society where the moral norm is that it is permissible to cheat, lie, and steal? A rational person would of course say no; and would not want those actions to be done to him or her; and thus the actions are immoral. Now, people do cheat, lie, and steal, and Kant admits that, but he condemns them as "parasites" on an otherwise moral system where the vast majority of people do not cheat, lie, or steal. The second is the Kingdom of Ends test which holds that an action is immoral, regardless of consequences, if it is disrespectful and demeaning to anyone, if it treats anyone like an instrument or thing or mere means (even to achieve a greater good). Since a person knows that he or she is a human being, a worthwhile person deserving of dignity and respect, one thus should reason that other people feel the same too. In essence, for Kant, the core principle is for all people to treat all others with dignity and respect, and thus all will live in the Kingdom of Ends wherein all are treated as worthwhile ends and not as mere means. The third main part to the Categorical Imperative is the Agent-Receiver test (which actually is the Golden Rule of Bible made secular by Kant). Pursuant to this ethical principle, Kant would say to consider the contemplated action, but if one did not know if one would be the agent, that is, the giver of the action, or the receiver of the action, would one be willing to have that action done. So, using the Categorical Imperative and the example of the merger, if the merger produces greater good overall it is moral under Utilitarianism, but if any stakeholder group is disrespected or demeaned the merger is immoral. And to take a more dramatic illustration, what does one say morally about a legal but exploitative "sweatshop" in Asia or elsewhere? It certainly produces a lot of good inexpensive products, and thus good in the form of money for a lot of stakeholders, and perhaps more good than bad, which would be enough for a Utilitarian conclusion of "moral" for the 'sweatshop," but what would Kant say after seeing the

conditions of the "sweatshop" - the age of the young workers, their gender and perhaps harassment, their wages, the lack of safety standards? So, in the "Mickelson case" in order to determine if Phil Mickelson was acting morally in his trading activities pursuant to Kantian ethics one would "simply" apply the three tests of the Categorical Imperative to the actions of the professional golfer and make a principled and reasoned decision as to morality or immorality of those actions.

As a conclusion to the ethics part of this case study, was Phil Mickelson or any of the other parties involved in this trading situation acting morally? Well, the "easy" (perhaps too easy) answer is that it depends on the ethical theory that one applies to the particular facts of the case. The reader surely has heard of "situational ethics" which term has a dual meaning: first, signifying the particular facts and circumstances of a case; and second, referring to the fact that more than one ethical theory can be applied to a set of particular facts and circumstances, and, moreover, one can arrive at different, and conflicting, moral conclusions based on the ethical theory applied to the case. However, in addition to acting legally and morally there is another value that people, especially business people and leaders in all sectors, must be cognizant of – social responsibility.

5. SOCIAL RESPONSIBILITY

Another challenge today, especially for business people as well as for prominent people in the sports and entertainment business, is that they are expected to act in a socially responsible manner. This societal expectation of being socially responsible can be above and beyond the law and even morality and ethics. Businesses and business people, therefore, are expected to be "socially responsible" and good "corporate citizens" (even though there may be neither a legal nor a moral obligation to do so) (Cavico and Mujtaba, 2016). The World Business Council for Sustainable Development defines social responsibility in a business context as a company's continuing commitment to act legally and morally and also to contribute to the economic development of society while improving the quality of life of their employees and their families as well as the local community and society as a whole (Cavico and Mujtaba, 2013).

One dilemma when dealing with "social responsibility" is to precisely define the term. Legality is based on laws (though vague laws at times); morality is based on theories and principles (though perhaps even more vague); but social responsibility is based on current explanations of the term. Typically, the definition is a very broad one; and consequently "social responsibility" means that business is involved in charitable organizations and activities and philanthropy as well as civic and community activities (Cavico and Mujtaba, 2013, 2016). But social responsibility in the broad sense contains a sustainability element, that is, sustainability as a *means* in the form of environmental protection and conservation activities and "going green" endeavors, such as solar and wind projects, anti-pollution measures, and saving water. One thus sees under the rubric of social responsibility such "sustainability" slogans and notions as the "3 P's: People, Planet, Profits" and the "Triple Bottom Line" (Economic Prosperity, Environmental Stewardship, and Social Responsibility). Sustainability (as a "means" and also as an "ends") is thus an essential component to, as well as objective of, social responsibility (Cavico and Mujtaba, 2016). The goal, therefore, is to achieve long-term sustainable success for oneself and one's business or organization by making sound economic and policy decisions and acting in a legal, moral, and socially responsible manner. Accordingly, in the case herein one very well might ask if Phil Mickelson, the former CEO, his company, the PGA, the country clubs, or for that matter the Las Vegas casinos have been acting in a socially responsible and environmentally sustainable manner.

6. SUMMARY

This case study was about the so-called “Mickelson case” of alleged insider trading of stocks. This case has legal, ethical, and social responsibility consequences. In order to build a scholarly foundation for an analysis of the case the authors presented material of a legal, ethical, and social responsibility nature. Legal principles, ethical theories and principles, and definitions of social responsibility and sustainability were provided to educate the reader as to basic precepts and concepts. Overall, ethics, and concepts of social responsibility learned herein can be applied to the “facts” of this case by means of discussion questions in the specific context of the Phil Mickelson insider trading case. That is, since this article is in the form of a “case study” the authors will provide several detailed questions that can be used for academic educational and corporate training purposes. Then educators, students, trainers, and participants can themselves apply the aforementioned principles to the facts of the case; and next they can reason to rational conclusions as to legality, morality, and social responsibility, or the lack thereof of the “players” and other stakeholders in the case. The facts of the case study, as well as its prominence in the recent news, make it a very appropriate learning modality particularly for a college or graduate level sports law and ethics type course but the case involves broader issues and principles that make it useful to a general business law and ethics course as well as corporate law and ethics training. As such, in either context, a major purpose of the authors is to stimulate principled-based analysis and thought-provoking discussions on these important legal, ethical and social responsibility matters. The authors trust that the readers have found their explication of the laws, ethics, and social responsibility to be clear and informative, that the “Mickelson case” was an interesting and efficacious setting and modality for the presentation, and that the discussion questions forthcoming will be useful for analysis and discussion purposes.

7. DISCUSSION QUESTIONS FOR ANALYSIS

Based on the facts of this case as delineated in major media outlets and the succinct statement of the laws of insider trading, morality based on ethical theories and principles, and current definitions and concepts of social responsibility as explicated herein, the authors hereby provide the following questions for analysis and discussion, to wit:

1. Did Mickelson receive material, non-public information in the form of stock tips? Why or why not? Why is this determination critical?
2. Was the planned breakup and “spinoff” of Darden sufficiently factual and objective “information” or was it mere rumor, speculation, or “loose talk”? Why? And why is this determination critical?
3. Do you believe Mickelson was a tippee in conspiracy with the insider, Davis, by means of the sports gambler? Why or why not?
4. Criminal convictions require evidence of an “evil mind” or bad intent, that is, the wrongdoers knew what they were doing, knew it was wrong, and intentionally did the wrongful acts anyway. Was the fact that a secret code and pre-paid phone were used for Dean Foods’ trading sufficient evidence of bad intent? Why or why not?
5. And assuming that the answers to the preceding questions are “yes,” then why did the government proceed only civilly against Mickelson as a “relief defendant” and not criminally? Do you agree with the determination of the SEC’s Enforcement Director that charges were not warranted in Mickelson’s case? Why or why not? Was Phil Mickelson merely “lucky” or perhaps “special”? Why or why not?

6. David Rosenfeld, law professor and former head of an SEC enforcement division, writing in an editorial in the *Wall Street Journal* (Rosenfeld, 2016) called the SEC proceeding against Mickelson a "legal bogey" because of the SEC's apparent expansive definition of a "relief defendant" in this case. To wit, Rosenfeld (2016) explains: "The SEC appears to be taking the position that whenever there has been unlawful conduct by a tipper, any profits derived from trades by a tippee are ill-gotten gains, even if the tippee didn't have knowledge of a personal benefit, and even if the trades themselves violated no law." Do you agree with the SEC's interpretation of the "relief defendant" definition and its application to Mickelson? Why or why not?
7. Did Mickelson act morally based on the ethical theories of Ethical Egoism, Ethical Relativism, Utilitarianism, and Kantian ethics? Why or why not? Did the other two parties act morally? Why or why not?
8. As *Bloomberg Business Week* (Kolhatkar, 2016) asked: "Is it fair for rich, well-connected individuals with access to valuable corporate information to freely make money from it? Or is it deeply unfair"? Why or why not?
9. Phil Mickelson is a very successful and popular golfer who thus has many "big-time" (and "big-money") endorsers, including at one time a very large and prominent investment bank. How should an Ethically Egoistic endorser react to this latest gambling and insider trading "episode"? Explain.
10. What should a "socially responsible" professional athlete such as Mickelson, who is very famous and very wealthy, be doing for the local community and society as a whole? Provide specific examples.
11. What should a "socially responsible" as well as "sustainable" major golf country club be doing for the local community and society as a whole? Provide specific examples.
12. What should a "socially responsible" as well as "sustainable" PGA be doing for the local communities where it hosts tournaments and for society as a whole? Provide specific examples.
13. Phil Mickelson recently said that he was considering changing his residence from the high-tax state of California to Florida, a low-tax state without a state personal income tax. As a result, Mickelson was criticized by California community groups and others for being socially *irresponsible* for planning to leave the state? Do you agree with his critics? Why or why not?
14. Should professional athletes like Mickelson place bets with "professional" sports gamblers? Why or why not? Should they even associate with them? Why or why not? Actually, should they bet on sports at all? Why or why not?
15. *Bloomberg Business Week* (Kolhatkar, 2016) related an exchange at a news conference regarding the "Mickelson case" between a reporter and Mr. Preet Bharara, the U.S. Attorney for the Southern District of New York. The reporter asked Mr. Bharara the following questions: "Doesn't it undermine confidence in the markets to not charge the celebrity defendant and not explain why you are not charging the celebrity"? "What message do you think that sends to the American public"? According to *Bloomberg Business Week*, Mr. Bharara merely blinked. What do you think the answers to the reporter's questions are?

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