

# **MGST 451**

## **Corporate Governance and Ethical Decision-Making**

**Lecture 1 – Winter 2019 L01-L03**

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1. Why a course on corporate governance and ethical decision making?
2. One key benefit for students
3. Review of course outline
4. MGST 451: kind of a finance course?
5. Review of key concepts and terminology

- Business education shall prepare students for a world in which private enterprises are being asked to be self-critical of their role in society and need to respond to changing social norms.  
([www.aacsb.edu/~media/AACSB/Publications/research-reports/ethics-education.ashx](http://www.aacsb.edu/~media/AACSB/Publications/research-reports/ethics-education.ashx))
- The Haskayne School of Business is committed to sustainability and ethics in the business world.
  - Became a signatory to the 'Principles for Responsible Management Education' in 2008 ([www.unprme.org/index.php](http://www.unprme.org/index.php)).
  - For the report of the efforts spent at Haskayne to implement these principles see [haskayne.ucalgary.ca/about/prme](http://haskayne.ucalgary.ca/about/prme).
- MGST 451 is one course through which Haskayne students learn something about global social responsibility (GSR).  
([https://en.wikipedia.org/wiki/Corporate\\_social\\_responsibility](https://en.wikipedia.org/wiki/Corporate_social_responsibility))

- Any organization needs to be governed.
- All organizations are actually governed.
- A well-governed organization is more likely to be successful and provide personal growth opportunities to its employees.
- A future manager with leadership ambitions would be well-advised to understand the decision making dynamics within the organization (or within a potential employer).
- A weakly governed organization encounters issues and occasional crises that impede the careers of its employees.
- A badly governed organization will likely fail, “it is only a question of time”, tainting the resume of all its ex-employees.
- Once you understand corporate governance, you can use such knowledge when choosing an employer and when at work.

- This is a required course in the Bachelor of Commerce program.
- Students will acquire knowledge of corporate governance systems and learn why and how strong ethical decision-making systems are critical in developing and sustaining successful business enterprises.
- The resolution of agency problems, the responsibilities and structure of the board of directors, the intricacies of compensation systems and financial modelling are reviewed.
- Given their central role in modern compensation systems for executives and employees, options and share ownership programs are also studied.

Upon successful completion of the course, the student will be able to:

- a) critically assess the **critical components of a corporate governance system** and how they relate to each other functionally;
- b) explain/calculate the profit or loss that could be earned in a **long or short position**;
- c) explain/calculate the profit or loss that could be earned by using exchange traded **options**;
- d) explain the advantages, disadvantages, and taxation of **employee stock option plans**, and their use in executive compensation plans;
- e) explain what are the **agency costs** resulting from using corporate debt;
- f) explain how markets, **mergers and acquisitions** as well as shareholder activism relate to and influence corporate governance;
- g) present and discuss examples of good (or poor) corporate governance scenarios;
- h) discuss the **ethical decisions** faced by corporate boards and executives.

- One introductory lecture
- Three lectures on corporate governance
- Four lectures on stock positions and options
- Two lectures on executive compensation
- One lecture on agency costs and benefits of debt
- Three lectures on mergers and acquisitions
- One lecture on ethical decision making
- Eight lectures for in-class learning activities
- One lecture to prepare for the final examination
- A total of twenty-four lectures of 75 minutes

## **Textbook**

- Is the same one used in the Finance 317 course: Corporate Finance Third Canadian Edition by Berk, DeMarzo and Strangeland. Published by Pearson Canada.
- If you do not have the third Canadian edition don't worry, any Canadian Edition will do... just the chapter and page numbers will be different.

## **Nametags (optional)**

- Please bring and display a name tag at each lecture.



Item	Number	Description	Item Weight	Total Weight
On-line Quizzes	10* *8 best count	Individual 12 questions each	2% each	16%
Case reports	4	Group	6% each	24%
In-class activities	8† †6 best count	Group/Individual	4% each	24%
Final exam 3 hours	1	Individual 60 multiple choice	36%	36%
Total				100%

***Starting Friday January 25***, students will be required to complete, **on an individual basis**, an on-line quiz on the information that will be discussed in lectures 1, 2, and 3.

- **No collaboration or conversation about the quiz is permitted! This is individual work.**
- Each Quiz (12 multiple choice or true and false questions) will be made available on D2L at 6:00 p.m. on the Tuesday evening after the relevant Monday/Tuesday lecture. This quiz will be available until 6:00 p.m. on Friday.
- There are 10 quizzes, the best 8 will count toward your final grade. If you miss writing a quiz for any reason, you will not be offered a deferral. This means that you should plan carefully to ensure you do not miss more than 2 quizzes.
- For your quiz to be graded you must click the SUBMIT button before the 36 minute time limit has passed.

- You are required to form a group of **five** members so that you may complete the case assignments.
- The choice of group members is completely up to the students, but **all group members must be in the same lecture section.**
- **By no later than** start of class Wednesday January 23 or Thursday January 24, 2019, you must complete and submit the group registration form found on D2L listing the names of the five members in your group to your instructor. Please be certain to circle/indicate your lecture number on the form.

- **Four case reports are** to be completed by your group (2-page executive summary, plus up to five pages of exhibits, if any).
- Submit your reports in the corresponding D2L dropbox. Any collaboration between groups will be considered plagiarism.
  - The file has to be in a pdf format.
  - The name of the file has to follow the format  
“MGST451\_W2019\_L0?\_Case\_?\_Group\_?”
- In addition to what is specified in the course outline, specific instructions will be provided for each case in D2L. Marks will be lost if the said instructions are not complied with.
- **Late submissions will be penalized by 10% for every hour that the group’s solution arrives beyond the deadline.**

- The course will provide students with experiential learning opportunities through structured classroom activities.
- In the context of the course, experiential learning is used to complement the lectures, allowing students to experience hands-on discovery and/or application of knowledge.
- To benefit fully from these activities, students not only have to be willing to participate fully, but also be pro-active, to adopt a ‘thought pattern of inquiry’, and be self-reflective.
- Students will not be penalized for making mistakes, as mistakes are learning opportunities in experiential learning.
- Some students might find these activities constitute a challenging learning process while others find them really enjoyable and highly valuable.

- There will be an in-class activity in most Wednesday or Thursday lectures (best 6 of 8 will be chosen worth 4% each).
- These may be mini-exams, brief presentations by groups, debates, individual assignments or other class participation techniques.
- Students will be reminded in the preceding Monday or Tuesday lecture that the following Wednesday or Thursday lecture will have an in-class activity.
- **Being absent or not participating fully will count as a zero for the final course grade, and no deferral will be granted.**

- Registrar scheduled during the official final exam period (Monday April 15 to Thursday April 27, 2019).
- The final exam will comprise **60 multiple choice questions** covering all material presented in the lectures, including cases and the in-class activities. The time allowed is 180 minutes.
- A **sample final exam will be posted to D2L** to give students an idea of what the final exam may look like. Please, not copy, print, screen capture or electronically store this sample exam.
- You can bring **one 8.5” by 11.0” inch paper** (both sides allowed, but your own handwritten or typed ‘cheat sheet’ with your name – not a photocopy and no post-it notes). It must be submitted along the examination booklet and the scantron at the end of the examination.

## **Study early !**

- Instructors will not answer questions from students on the day of the examination. This means both in person and via email.
- Students are encouraged to prepare early and, given it is impossible to see all students on the day of the exam, it may be argued that those who did get to visit, might have received an unfair advantage.

## **During the exam**

- There are no penalties for incorrect answers, so (in the absence of knowing the answer for sure) make an 'educated guess' and never leave a blank answer for a question
- If you are a leisurely exam writer, be sure to watch the time carefully. You will not receive any extra time to complete the scantron (bubble) sheet during the examination. If your scantron (bubble) sheet has not been completed in the allotted time, your score will reflect the number of correct answers you recorded on the incomplete scantron (bubble) sheet.



- The Haskayne School of Business endeavours to ensure consistency of final grades across courses and sections. Variations in distribution will be considered by the instructor where called for by the performance in each individual class.

A+ $\geq$ 95%	B+ $\geq$ 80%	C+ $\geq$ 66%	D+ $\geq$ 56%
A $\geq$ 90%	B $\geq$ 75%	C $\geq$ 62%	D $\geq$ 50%
A- $\geq$ 85%	B- $\geq$ 70%	C- $\geq$ 58%	F < 50%

- Instructors **will not** curve the grades. To determine your letter grade, calculate your final percentage and then refer to the table above to locate your letter grade.
- Your final percentage equals the sum of the relative weight of the course component multiplied by your performance (as a percent) on each component.

- There are no “do-overs”
  - You have flexibility in managing your time for the on-line quizzes and in-class activities. You should plan to complete all these quizzes and activities but can miss up to two of each of these without impacting your grade
  - You are restricted to the original writing of the case analyses and final exam.
  - The rules have been stated and the rules will be followed. Be warned - no exceptions will be made!
- Regarding students who are close to a particular cut off point, for the same reason someone who gets 90.0 will not have their A grade removed, someone who gets 89.9 will not be “bumped up” to an A grade.

- Come to class prepared
  - Consult D2L regularly and read your emails;
  - Read the slides and other material provided.
- When in class, focus your attention on the lecture, think, try your best to assimilate the material, and if there is something you do not understand, ask questions.
- Attempt completing each quiz after having read the material and consult the material while doing the quiz.
- When working in group, adopt a positive and constructive attitude: come prepared, be willing to listen to what other team members have to share, etc.
- Please note that ability to communicate effectively and work well in diverse teams is highly valued by employers. People with a bad attitude are not hired, or when hired get fired.

## The two perspectives on corporate governance

- Law

- Since corporate governance is heavily regulated, the legal and compliance aspects can be studied from a legal perspective, for example by law students in a law school.
- It consists in a careful review and analysis of the applicable laws and regulations, often one law article at a time. The jurisprudence (court decisions) would also be reviewed.

- Finance

- Finance academics have researched corporate governance issues, in particular since “Theory of the Firm: Managerial Behavior, Agency Costs, and Ownership Structure” Jensen and Meckling (JFE 1976; 77,149 citations). Solutions to corporate governance issues are often finance-driven.

- Governance
  - Processes by which decisions are taken and implemented in the collective realm (i.e. to govern).
  - Process by which a decision maker become enabled to make decisions that affect the lives of many.
- Example: a democratic process used to elect a legislative assembly is generally viewed as providing better governance and therefore better laws and regulations than a dictatorship.
- Also, what checks and balances mechanisms are in place to ensure good decisions are taken and prevent abuse of power.
- Example: fixed terms for elected officials, as it encourages them to act in a responsible manner since otherwise they are likely not re-elected. But is there a cost for such mechanism?

- Corporate governance: how a corporation is governed.
  - Involves the interplay between three key stakeholders: the shareholders, the board of directors and management.
- ‘Good governance’ is assumed to provide for a greater likelihood of sustained corporate success (by having the required mechanisms to make sure management internalizes the welfare of shareholders/stakeholders of the firm).
- ‘Bad governance’ has often been found to be a key enabler of major corporate disasters (large losses for shareholders and other stakeholders like employees, banks, suppliers).
- In most countries, corporate governance of publicly-owned firms is heavily regulated, notably to protect shareholders from abuse to the hands of management.

- In a business context, compliance usually refers the firm complying with its obligations arising from various laws and regulations that legislators and regulators have enacted.
- Often viewed by firms as costly, being found to be in breach of your legal duty can lead to a mundane fine up to a complete loss of reputation and even firm managers being jailed.
- Management knowingly not complying with applicable laws and regulations has been found to be a key enabler of major corporate disasters (e.g. Enron).
- Management 'not paying enough attention' to compliance (i.e. 'playing dumb') has also been found to be a key enabler of major corporate disasters.

- Ethics attempt to delineate what is right or wrong behaviour in human affairs from a philosophical perspective.
- Business ethics refer to how ethics shall affect the conduct of a business enterprise.
- While firms sometime decide to achieve technical compliance with the 'letter of the law' (as opposed to the 'spirit of the law'), such behavior is viewed by many as unethical and might result in a loss of reputation.



- Human beings have a strong preference to live well rather than being confronted to scarcity.
- For example, people like to be well fed rather than go hungry.
- Good governance at the governmental level (public sector) and at the individual firm level (private sector) is critical to achieve and maintain a high standard of living.
- The credo of Canada is often referred to “peace, order and good government”. Good government by extension nowadays also refers to “the notion of appropriate self-governance by civil society actors”.
- A breakdown of good governance can lead to a rapid decline of standard of living (e.g. Venezuela).