



## Tuck School at Dartmouth

### INTERNATIONAL CORPORATE GOVERNANCE Winter 2010

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#### **COURSE DESCRIPTION**

Since “finance without governance” is a near-impossibility, anyone interested in corporate finance and financial development needs to have a basic understanding of how corporate governance works in practice. The course defines a corporate governance system as the set of constraints on minority shareholder expropriation set by (1) internal corporate control mechanisms (such as the board), (2) external capital market monitoring and pricing, and (3) laws and regulations. Students learn how the design of the corporate governance system determines the ability of individual firms to attract capital on competitive terms. We discuss how and why governance systems differ across countries, and how large institutional investors such as pension funds and certain sovereign wealth funds actively work to increase shareholder rights and develop best governance practices. The course also taps into the latest U.S. debate on how the government, as “owner of last resort”, should exercise its share-ownership rights in companies like AIG, Citigroup, and GM.

#### **GRADING**

- Class Participation, six two-page Group Memos, and two paper presentations in class: 60%
- Group Project, 40%:
  - In-depth case study of a governance controversy set against the background of the governance system of a selected country. Due for presentation in sessions 17 and 18.

**INTERNATIONAL CORPORATE GOVERNANCE  
Professor B. Espen Eckbo, Winter 2010**

<u>Session #</u>	<u>Date</u>	<u>Topic</u>	<u>Class Visitor</u>
<b>THE INTERNATIONAL GOVERNANCE DEBATE</b>			
1	Tue 1/5	Introduction: U.S. Government as Large Shareholder	
2	Wed 1/6	Corporate Governance: A Global Perspective	
<b>THE EXECUTIVE COMPENSATION CONTROVERSY</b>			
3	Mon 1/11	Compensation Policies	
4	Tue 1/12	CEO Pay: A compensation consultant's view	<i>Stephen F. O'Byrne</i>
5	Tue 1/19	<u>No class</u> (Eckbo presenting to Norway's Sovereign Wealth Fund)	
6	Wed 1/20	<u>No class</u> (Eckbo presenting to Norway's Sovereign Wealth Fund)	
<b>THE SEPARATION OF OWNERSHIP AND CONTROL</b>			
7	Mon 1/25	Ownership Structure and Firm Performance Around the World - 1	
8	Tue 1/26	Ownership Structure and Firm Performance Around the World - 2	
<b>SOX AND ACCOUNTING ISSUES</b>			
9	Mon 2/1	Perspectives on Transparency and Ethics in Accounting	<i>Arthur Lindenauer</i>
10	Tues 2/2	Sarbanes-Oxley and the Cross-Listing Decision	
<b>INSTITUTIONAL SHAREHOLDER ACTIVISM</b>			
11	Mon 2/8	Governance Investing	
12	Tue 2/9	What do Large Institutional Investors Do?	
13	Mon 2/15	Negative Screening: The Case of Norway and Wal-Mart	
<b>TAKEOVER DEFENSES</b>			
14	Tue 2/16	Poison Pill Defense: The Case of the Circon Pill	
15	Mon 2/22	Takeover Defenses: Legal Issues	<i>John Gorman</i>
<b>SOCIALLY RESPONSIBLE INVESTING</b>			
16	Tue 2/23	Ethical Investments: Norway's Sovereign Wealth Fund	<i>Henrik Syse</i>
17, 18	3/1; 3/2	Term Project Presentations	

## INTERNATIONAL CORPORATE GOVERNANCE

Professor B. Espen Eckbo  
Winter 2010

### THE INTERNATIONAL GOVERNANCE DEBATE

#### Session 1: Introduction: U.S. Government as a Large Shareholder

- That Value-Maximization Criterion: The controversy over corporate objectives
- The government as large shareholder: What's different? When to exit?
- Director Election Reform

Jensen, Michael C., 2001, "Value Maximization, Stakeholder Theory, and the Corporate Objective Function," Pre-published Working Paper, Tuck School of Business at Dartmouth.

Eckbo, B. Espen, 2009, "The Government as Active Shareholder," Testimony to the Congressional Domestic Policy Subcommittee of the Oversight and Governance Reform Committee (December 16).

#### Session 2: Corporate Governance: A Global Perspective

- Law and financial development
- Investor expropriation technology
- Legal families and investor rights protection

Shleifer, Andrei, Robert W. Vishny, 1997, "A Survey of Corporate Governance", *Journal of Finance*, 52, 737-783.

Eckbo, B. Espen, 2005, "Strong Insiders Invite Weak Governance", *Financial Times, Mastering Series* (May 19).

Djankov, Simeon, Rafael La Porta, Florencio Lopez-de-Silanes and Andrei Shleifer, 2008, "The Law and Economics of Self-Dealing," *Journal of Financial Economics* 88, 430-465.

### EXECUTIVE COMPENSATION CONTROVERSY

#### Session 3: Compensation Policies

- Principal-agent paradigm and optimal contracting
- Pros and cons of bonus systems
- Did stock compensation cause the banking crisis?

Jensen, Michael C. and Kevin J. Murphy, 2004, "Remuneration: Where We've Been, How we Got to Here, What are the Problems, and How to Fix them", Working paper, HBS and USC.

Fahlenbach, Rudiger and Rene M. Stulz, 2009, "Bank CEO Incentives and the Credit Crisis," Working Paper, Fisher College of Business, Ohio State University.

#### **Session 4: CEO Pay: A Compensation Consultant's View**

- Stock option valuation parameters
- Accounting expense of performance incentives
- Cost-efficiency of retention incentives

O'Byrne, Stephen F. and S. David Young, 2005, "Top Management Incentives and Corporate Performance", *Journal of Applied Corporate Finance* 17, 105—114.

Class Visitor: Stephen O'Byrne, President, Shareholder Value Advisors, Inc.

#### **Session 5: No Class (Eckbo presenting to Norway's Sovereign Wealth Fund)**

#### **Session 6: No Class (Eckbo presenting to Norway's Sovereign Wealth Fund)**

### **THE SEPARATION OF OWNERSHIP AND CONTROL**

#### **Session 7: Share Ownership Structure and Firm Performance around the World -1**

- Facts on ownership structures in the U.S.
- Does ownership structures impact performance?

Holderness, Clifford G., 2003, "A Survey of Blockholders and Corporate Control," *Federal Reserve Bank of New York Economic Policy Review* (April), 51-64.

Holderness, Clifford G., 2007, "The Myth of Diffuse Ownership in the United States," *Review of Financial Studies* 22, 1377-1408.

Helwege, Jean, Hristo Pirinsky and Rene M. Stulz, 2007, "Why do Firms Become Widely Held? An analysis of the Dynamics of Corporate Ownership," *Journal of Finance* 62, 995-1028.

#### **Session 8: Share Ownership Structure and Firm Performance around the World -2**

- Facts on ownership structures around the world.
- Does ownership structures impact performance?

Claessens Stijn, Simeon Djankov and Larry H.P. Lang, 2000, "The Separation of Ownership and Control in East Asian Corporations," *Journal of Financial Economics* 58, 81-112.

Andres, Christian, 2008, "Large Shareholders and Firm Performance – An Empirical Examination of Founding-Family Ownership," *Journal of Corporate Finance* 14, 431-445.

## SOX AND ACCOUNTING ISSUES

### Session 9: Perspectives on Transparency and Ethics in Accounting

Class Visitor: Art Lindenauer T'59, Former Chairman of the Audit Committee of Schlumberger Technology Corporation

Burns, Natashe and Simi Kedia, 2006, "The Impact of Performance-Based Compensation on Misreporting," *Journal of Financial Economics* 79, 35-67.

### Session 10: Sarbanes-Oxley and the Cross-Listing Decision

- What are the costs of key provisions of the 2002 Sarbanes-Oxley Act?
- What determines the cross-listing decision?
- New Listings: Is the U.S. losing out to London?

"The Sarbanes-Oxley Act of 2002", Cooley Alert, August 2002, 1-11.

Fernandes, Nuno, Ugur Lei and Darius P. Miller, 2010, "Escape from New York: The Impact of Loosening Disclosure Requirements," *Journal of Financial Economics*, forthcoming.

Doidge, Craig, G. Andrew Karolyi and Rene M. Stulz, 2009, "Has New York Become Less Competitive than London in Global Markets? Evaluating Foreign Listing Choices over Time," *Journal of Financial Economics* 91, 253-277.

## INSTITUTIONAL SHAREHOLDER ACTIVISM

### Session 11: Governance Investing

- Strategies for institutional activism
- Empirical measures of the value of good governance
- Governance and stock returns

Gompers, Paul A., Joy L. Ishi and Andrew Metrick, 2003, "Corporate Governance and Equity Prices", *Quarterly Journal of Economics* (February), 107-155.

Johnson, Shane A., Theodore C. Moorman and Sorin Sorescu, 2009, "A Reexamination of Corporate Governance and Equity Prices," *Review of Financial Studies* 22, 4753-4786.

### Session 12: SRI and Negative Screening: The Case of Norway and Wal-Mart

- Strategies for institutional activism
- Empirical measures of the value of good governance
- Governance and stock returns

## Case Study: TBA

### **Session 13: What do Large Institutional Investors Do?**

- Strategies for institutional activism
- Does governance investing pay?

Del Guercio, Diane and Jennifer Hawkins, 1999, "The Motivation and Impact of Pension Fund Activism", *Journal of Financial Economics* 52, 291-340.

Becht, Marco, Julian Franks, Colin Mayer, and Stefano Rossi, 2006, "Returns to Shareholder Activism", ECGI Finance Working Paper no. 138.

Bradley, Michael, Alon Brav, Itay Goldstein and Wei Jiang, 2010, "Activist Arbitrage: A Study of Open-Ending Attempts of Closed-End Funds," *Journal of Financial Economics* 95, 1-19.

## **HOSTILE TAKEOVERS: LEGAL AND ECONOMIC ISSUES**

### **Session 14: Poison Pill Defense: The Case of the Circon Pill**

- Defensive strategies
- Use of governance provisions
- The Circon case

Comment, Robert and G. William Schwert, 1995, "Poison or Placebo? Evidence on the Deterrence and Wealth Effects of Modern Antitakeover Measures," *Journal of Financial Economics* 39, 3-43.

## Case Study

Circon Case (HBS 9-801-403 (A), 9-801-404 (B))

### **Circon Case Study Questions**

*Each group submits a spread sheet with the numerical answer to question 4 below.*

1. What motivated Circon Chairman and CEO Richard Auhll? Did he have financial incentives that strongly aligned his interests with those of the shareholders?
2. Put yourself in Auhll's shoes moments after receiving the telephone call from the U.S. Surgical CEO Leon Hirsch: how do you respond to the hostile bid? What factors would you consider? What factors should you consider (if different)?
3. Put yourself in the shoes of George Cloutier, moments after being asked by Richard Auhll to join the Circon board. Would you agree to be on the board? What role would you wish to play? Is your role consistent with your "duty of care" as member of the board?

4. If a hostile bidder had “broken through” (or triggered) the poison pill, what precisely would have happened to Circon’s capital structure and the hostile bidder’s stake in the company? What is the maximum cost of raising cash for (non-bidder) shareholders to be better off exercising the pill?
5. Put yourself in the shoes of Charles Elson immediately after getting elected to the Circon board. How do you assess your situation? What are your options? How do you achieve change within the board and/or within the company?
6. At the board meeting at the end of the (A) case, what options were available to the board? Which appears to have been the most attractive? How should the board have implemented this option?

### **Session 15: Takeover Defenses: Legal Issues**

- Case precedence for use of defensive actions
- Director fiduciary duties
- Shareholder rights and the “Just Say No” defense

Class Visitor: John Gorman, Luse Lehman Gorman Pomerenk & Schick Pc

### **Session 16: Ethical Investments: Norway’s Sovereign Wealth Fund**

- What are ethical theories?
- How do ethical theories map into investment strategies?
- How do you influence corporate social responsibility?

Class Visitors: Henrik Syse, Former head of Corporate Governance, Norges Bank Investment management (NBIM – manager of Norway’s Sovereign Wealth Fund)

### **Sessions 17-18: Student term paper presentations**