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.
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<td>Introduction: U.S. Government as Large Shareholder</td>
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<td>Corporate Governance: A Global Perspective</td>
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<td>CEO Pay: A compensation consultant’s view</td>
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<td>Perspectives on Transparency and Ethics in Accounting</td>
<td><strong>Arthur Lindenauer</strong></td>
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<td>Mon 2/15</td>
<td>Negative Screening: The Case of Norway and Wal-Mart</td>
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<td>Tue 2/16</td>
<td>Poison Pill Defense: The Case of the Circon Pill</td>
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<td>Mon 2/22</td>
<td>Takeover Defenses: Legal Issues</td>
<td><strong>John Gorman</strong></td>
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<td>16</td>
<td>Tue 2/23</td>
<td>Ethical Investments: Norway’s Sovereign Wealth Fund</td>
<td><strong>Henrik Syse</strong></td>
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<td>17, 18</td>
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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


Session 2: Corporate Governance: A Global Perspective

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


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.

Session 4: CEO Pay: A Compensation Consultant’s View

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


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?


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

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


SOX AND ACCOUNTING ISSUES

Session 9: Perspectives on Transparency and Ethics in Accounting

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


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?


INSTITUTIONAL SHAREHOLDER ACTIVISM

Session 11: Governance Investing

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


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?


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


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

Circon Case Study Questions

Each group submits a spreadsheet 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**