

SYLLABUS
SPRING 2010

ECON 1790 **CORPORATE GOVERNANCE + MANAGEMENT**
Brown University

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<i>Lecture Time / Venue</i>	MWF 2:00-2:50 pm / Metcalf Chemical Laboratory 305
<i>Teaching Assistant</i>	John Wang E-mail: john_wang@brown.edu
<i>Conference Time / Venue</i>	M 12:00-12:50 pm / Wilson Hall 105 M 7:00-7:50 pm / Wilson Hall 205

About the Course

Corporate governance is concerned with mechanisms by which the owners of a public firm ensure that they earn an adequate return to their investments. Because self-interested managers control the firm's day-to-day operations, stockholders need to design monitoring devices and incentives for managers to act in their interest. We analyze the governance problem using the economic theory of contracts and discuss what the solutions look like in practice.

The first half of the course introduces the general contracting (or "principal-agent") problem and examines the management function in its light. We consider how organizations can be structured for optimal information flow and productivity. In the second half, we see how the financial structure of the firm affects the owners' ability to monitor management. We discuss how oversight can fail and how the legal framework is evolving to address the problems.

- Topics
1. The Contracting Problem (3 weeks)
 2. Employment and Management (3 weeks)
 3. Organization Design (3 weeks)
 4. Financial Structure and Control (3 weeks)
 5. Legislation (1 week)

Prerequisites ECON 1110 (Intermediate Microeconomics) or ECON 1130 (Intermediate Microeconomics, Mathematical); ECON 1720 (Corporate Finance).

Policies

Attendance While attendance is not specifically required, either in lecture or conferences, you will only be able to earn participation points in a given week if you go to one of the conferences and show that you have done the assigned exercises.

The purpose of conferences is to discuss weekly exercises and address questions you may have about lecture material. The role of the TA is not to work through exercises and directly answer every question. Rather, he will let students present their solutions and try to answer questions, and might only help out when needed.

Shopping You can enroll in the course at any point during the shopping period, but be aware that, from second week, you lose participation points if you do not attend conference.

Cell Phones They must either be switched off during lecture and conferences, or put on speaker when ringing. Do not let your phone ring in class without answering – it's impolite to the caller and leaves us all with a terrible impression of you.

Grading Assessment includes: in-class midterm and final exam (30% each), problem sets (30%) and weekly exercises (10%).

Three exercises will be assigned from the textbook every week, except in the first, fifth and sixth week. Exercises are announced one week in advance on the course website. They can be attempted in groups (if you like) and do not have to be handed in. However, you will be asked to indicate at the beginning of conference whether you solved the exercises fully, partially or not at all. If you sign in, then you need to attend conference and may be asked to present your full or partial solution.

Each set of weekly exercises counts for 1% of your final grade. (If you indicate every time that you have fully solved every exercise, you will get 10 points for participation in the end.) Intentional dishonesty, i.e. inability to produce your results, will trigger an automatic zero in participation for the entire course (you can get up to 90% after that).

In addition, three problem sets – each containing five exercises from the textbook – will be posted on the course website two weeks in advance of due date. Problem sets are to be done individually and handed in to the TA, either by e-mail or in hard copy, by noon on 2/15, 3/15 and 4/19. Every problem set counts for 10% of the final grade; each exercise is marked by the TA as “fully solved” (2 points), “partially solved” (1 point) or “not solved” (0 points). Late submissions incur a loss of 1 point (i.e. 1% of the final grade) per day, up to a maximum of 10 points.

Readings

Textbook Milgrom, P.; Roberts, J. (1992). *Economics, Organization and Management*. Prentice-Hall. ISBN: 978-0132246507.

Reference Tirole, J. (2005). *The Theory of Corporate Finance*. Princeton University Press. ISBN: 978-0691125565. (on library reserve)

A proper textbook on the economics of corporate governance does not exist. Two insightful expositions of organization theory come closest. Of these, Milgrom and Roberts is economics-oriented, while Brickley, Smith and Zimmerman, *Managerial Economics and Organizational Architecture*, balances economic and management perspectives. Kim and Nofsinger, *Corporate Governance*, describes the practical world of corporate governance; this little book makes great complementary reading.

Corporate governance is closely linked to the field of corporate finance. Tirole offers the most up-to-date economic treatment of corporate finance, often delving into corporate governance issues. Since Milgrom and Roberts cover the corporate finance aspect insufficiently for our purposes, you may wish to refer to Tirole for the relevant lectures, although the book is technically more demanding.

If you want to study principal-agent theory, which underlies the economic analysis of corporate governance, in more detail, take a look at Laffont and Martimort, *The Theory of Incentives: The Principal-Agent Model*. Again, this book is a formal treatment at the advanced undergraduate or graduate level.

Lecture and Readings Schedule

Week 1			
	Wed 1/27	Introduction to the Course	
	Fri 1/29	1.1 Contracts and Private Information	5: 126-140
Week 2	Mon 2/1	(1.1 cont'd)	5: 140-162
	Wed 2/3	1.2 Moral Hazard	6: 166-185
	Fri 2/5	(1.2 cont'd)	6: 185-196, 200-203
Week 3	Mon 2/8	1.3 Risk-Bearing and Risk-Sharing	7: 207-214, 246-247
	Wed 2/10	1.4 Incentives	7: 214-226
	Fri 2/12	(1.4 cont'd)	7: 226-241
Week 4	Mon 2/15	2.1 Employment	10
	Wed 2/17	2.2 Pay	12
	Fri 2/19	(2.2 cont'd)	8
Week 5	Mon 2/22	Long weekend (no class)	
	Wed 2/24	2.3 Careers	11
	Fri 2/26	2.4 Executive Monitoring and Compensation	13: 423-433
Week 6	Mon 3/1	(2.4 cont'd)	13: 433-445
	Wed 3/3	2.5 Leadership	
	Fri 3/5	Midterm Exam	

Week 7	<i>Mon 3/8</i>	3.1 Coordination and Efficiency	1, 2: 19-28
	<i>Wed 3/10</i>	3.2 Transactions	2: 28-52
	<i>Fri 3/12</i>	(3.2 cont'd)	9
Week 8	<i>Mon 3/15</i>	3.3 Information Flows, Complementarities and Strategic Objectives	4: 88-106
	<i>Wed 3/17</i>	(3.3 cont'd)	4: 106-118, 121-124
	<i>Fri 3/19</i>	3.4 Organization Structure	16: 538-552
Week 9	<i>Mon 3/22</i>	(3.4 cont'd)	16: 552-569
	<i>Wed 3/24</i>	(3.4 cont'd)	16: 569-583, 17
	<i>Fri 3/26</i>	3.5 Coordination through Prices	3
Spring Break			
Week 10	<i>Mon 4/5</i>	4.1 Financial Theory	14: 448-460
	<i>Wed 4/7</i>	(4.1 cont'd)	14: 460-477
	<i>Fri 4/9</i>	4.2 Trends and International Comparisons	15: 483-491
Week 11	<i>Mon 4/12</i>	4.3 Stakeholders and Their Conflicting Interests	15: 491-496, 15: 496-507
	<i>Wed 4/14</i>	4.4 Control	
	<i>Fri 4/16</i>	4.5 Monitoring	
Week 12	<i>Mon 4/19</i>	4.6 Takeovers	15: 507-520
	<i>Wed 4/21</i>	(4.6 cont'd)	
	<i>Fri 4/23</i>	4.7 Non-Corporate Forms of Ownership	15: 520-531
Week 13	<i>Mon 4/26</i>	5.1 Comparative Legal Environments	
	<i>Wed 4/28</i>	5.2 Crises	
	<i>Fri 4/30</i>	5.3 Shareholder vs. Stakeholder Interests	
Reading Period			