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McGraw-Hill Corporate Finance
Application-Based Activities (ABA)
Implementation Guide

Table of Contents

- Please see additional links in the Connect Library > Instructor Resources > Application-based Activities site for a full list of ABAs and their descriptions, a McGraw Hill text and chapter key, and sample syllabi.

Overview of the Corporate Finance Application-Based Activities

McGraw-Hill's Corporate Finance Application-Based Activities (ABAs) are available in Connect for all McGraw-Hill Corporate Finance titles. The assignable and auto-gradable ABAs immerse students in an engaging and interactive learning environment, which simulates real-world scenarios in which corporate finance concepts are applied. The ABAs have been created by corporate finance experts and professors to address key corporate finance course challenges, including improving critical thinking skills; increasing the number of assignable materials for students to apply concepts; and improving the level of student engagement and motivation by showing relevance of the course content to real life.

Each ABA features a topic that is among the "most often taught" in the one- and two-semester corporate finance courses based on our extensive surveys related to the needs of corporate finance instructors. As students begin an ABA assignment, they become one of the characters in the ABA and take an active role in the simulation--asking and answering questions to make key decisions. Other characters in the ABA offer students background information about core concepts, provide relevant information and give feedback about the students' understanding of the topics. Each ABA was designed to take students approximately 10-15 minutes to complete.

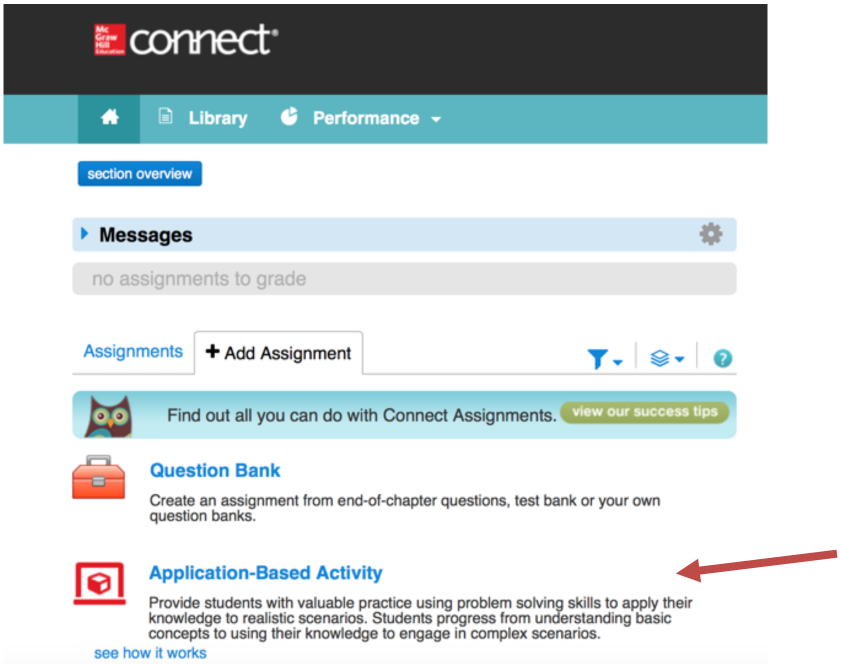
By applying their conceptual knowledge to real-world scenarios, students develop critical thinking and analytical skills. This practical application of corporate finance concepts helps engage students to achieve deeper understanding. The ABAs were also designed to connect students to the content through scenarios set in a context that is familiar to them like in a student project group, summer job, store, or concert.

McGraw-Hill's ABAs are easy to assign in Connect and are auto gradable, saving instructors time and providing students feedback on how well they're doing. ABA assignments are customizable so that instructors can select and organize them based on their own course learning outcomes and determine point values and due dates. Connect set-up policies, also determined by instructors, can allow students to have multiple attempts at completing the ABAs.

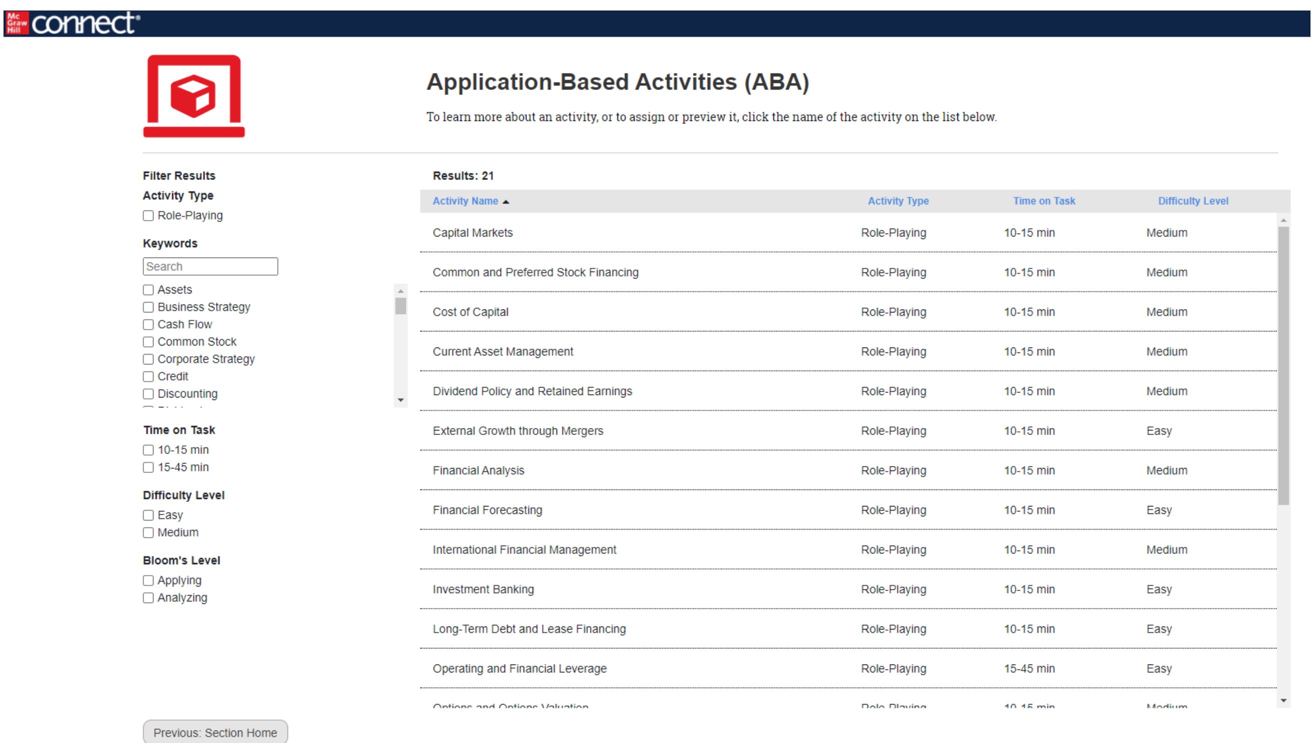
Assigning the Corporate Finance Application-Based Activities in Connect

1. Sign into your McGraw-Hill Connect Instructor Account
2. Access your McGraw-Hill Corporate Finance course
3. Click on Add Assignment

4. Click on Application-Based Activity



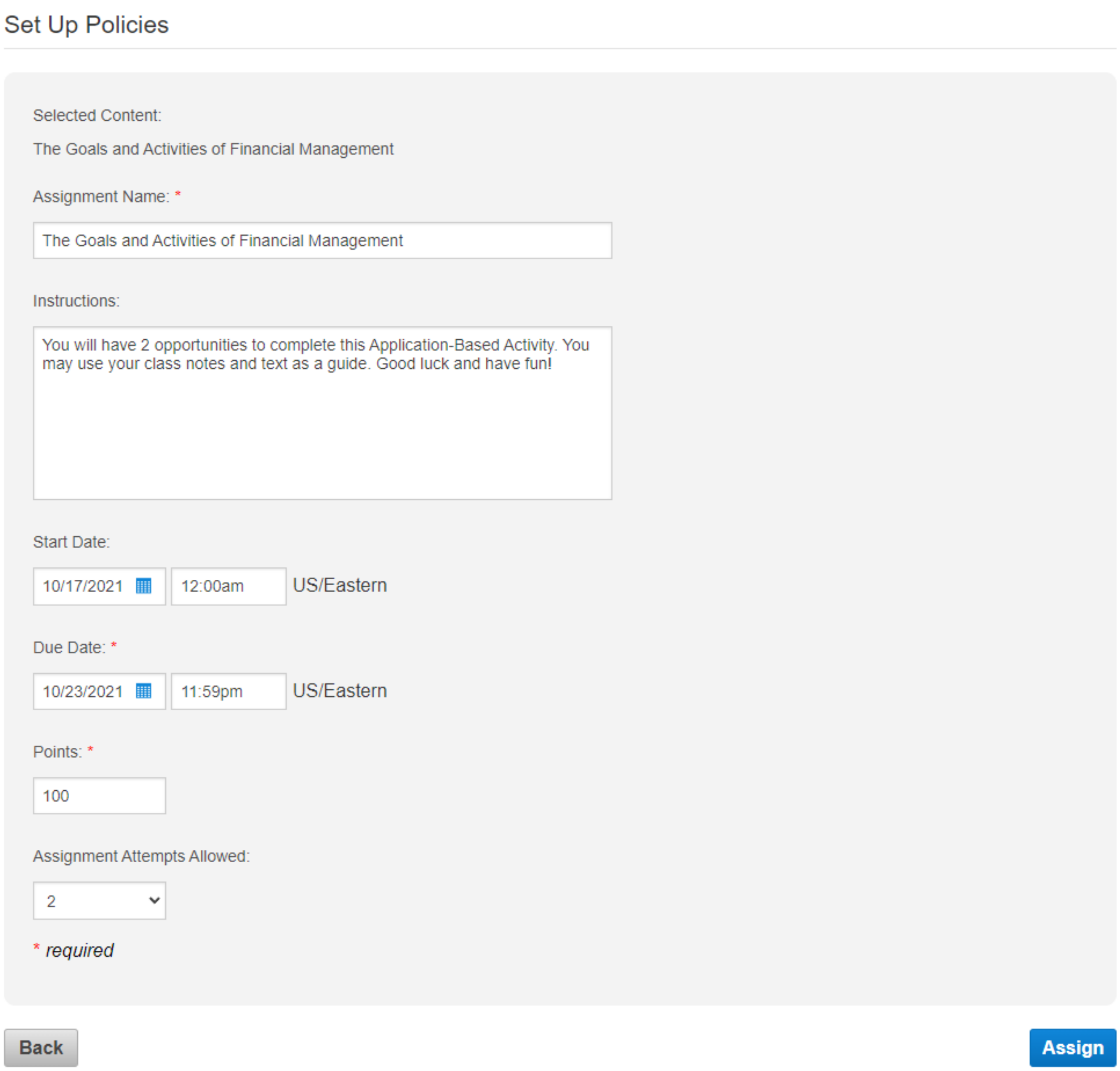
5. The next screen displays the list of available Application-Based Activities (screenshot below). Please note that the Corporate Finance ABAs are listed by topic.



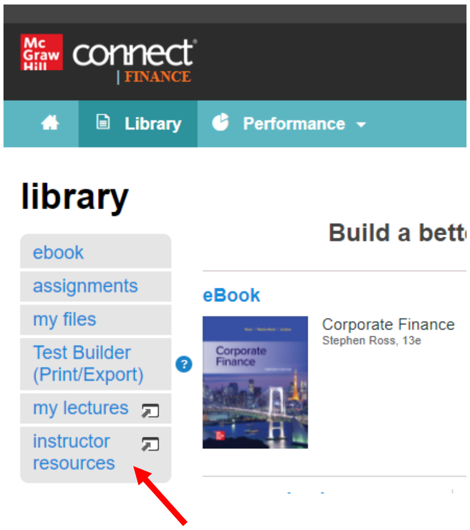
6. To preview an ABA select the activity name, then click the blue “**Preview**” button**.** Instructors may then click through the ABA experience. Please note that in Preview mode, the ABA is being previewed through the instructor Connect account and as such, progress on the ABA is not saved if the instructor exits the ABA. Instructors may create and register into the Connect course as a student using the 2-week free trial Connect access. Please contact McGraw-Hill’s customer service team or local McGraw-Hill representative if assistance is needed. (Contact information is below). Instructors may also click on the button to learn more about the activity.

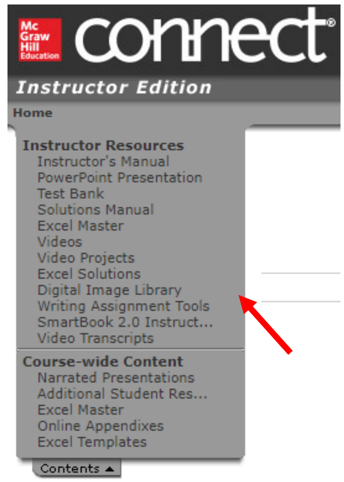
7. To assign the ABA, select the activity name, the section will expand then click the blue “**Assign**” button.

8. The next screen displays Connect’s Set Up Policies (screenshot below). Items marked with a red asterisk * are required before the assignment process is completed.



For easy access, this Implementation Guide and associated ABA resources are also available to instructors in the Connect Library > Instructor Resources.





Note for LMS Integrated Courses

For institutions using a Learning Management System (LMS), Connect and the Corporate Finance Application-Based Activities offer deep integration/single-sign on for most LMSs:

- **Blackboard**: deep linking, grade sync and single sign-on
- **Canvas**: deep linking, grade sync and single sign-on
- **Brightspace**: deep linking, grade sync and single sign-on
- **Moodle**: grade sync and single sign-on
- **Sakai**: grade sync and single sign-on

For more information on pairing a Connect course with an LMS, please contact the McGraw-Hill Customer Experience Group mpss.mhhe.com or access an online tutorial at http://createwp.customer.mheducation.com/wordpress-mu/success-academy/pairing-your-connect-course-with-your-lms/?page=Search&term=pairing%20LMS

Corporate Finance Application-Based Activity Walkthrough with Screenshots

Each ABA has a welcome screen with a description of the activity and information about the learning objectives, evaluation, and scoring.

connect

The Goals and Activities of Financial Management

The Goals and Activities of Financial Management

Activity Description

The CEO of a startup is meeting with her mentor. Her product is bringing in revenue but she's never managed a company before. She asks for your help. Help Kiara sort out the basics of financial management for her new company.

The estimated time to complete the activity is 15-20 minutes. You should start when you have enough time to critically think through the scenario. However, if you need to exit the activity before completion, you will return to where you left off when you re-enter.

Learning Objectives

After completing the activity, you will be able to:

- LO 1 Become familiar with the basic concepts of financial management
- LO 2 Identify the primary goal of financial managers
- LO 3 Understand the connection between financial markets and corporate finance

Evaluation and Scoring

You will be asked to respond to a variety of questions as you complete the activity, and your responses may impact both your score and what happens next.

You will not have the ability to go back and change your answer, so consider each answer option carefully.

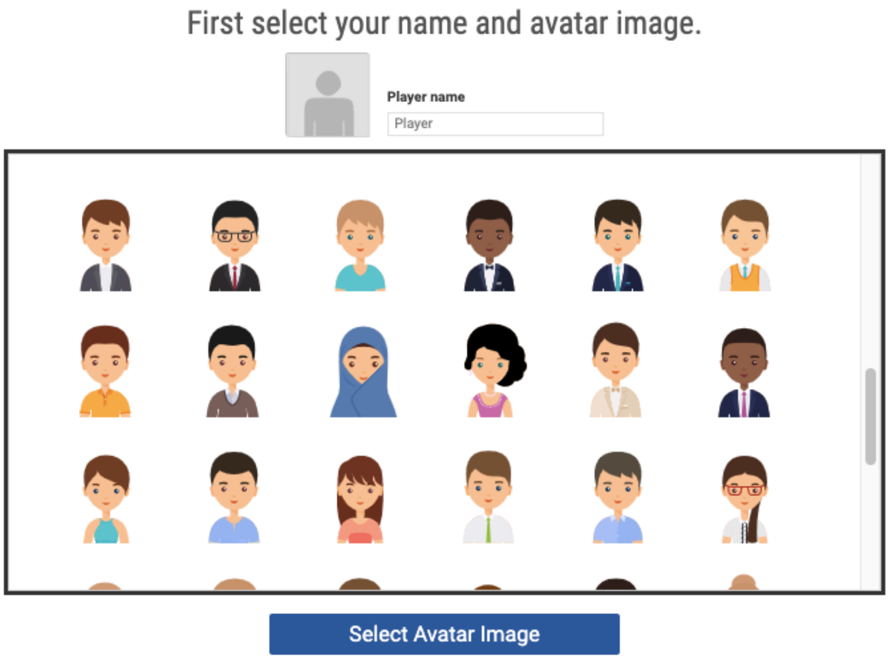
Scoring is calculated as follows:

1. Points are received based on the answer you select for each question, and questions are tied to multiple scoring categories associated with the learning objectives.
2. Your scores for each category are based on the total number of points you earn for the associated questions.
3. You will receive one final activity score at the end of the activity that combines your results from each category.

Your instructor has assigned a total point value for this assignment. Your assignment grade is calculated based on the final percentage score you earn at the end of the activity.

begin

After clicking “Begin” students can type in their names and select an avatar image to represent themselves in the ABA.

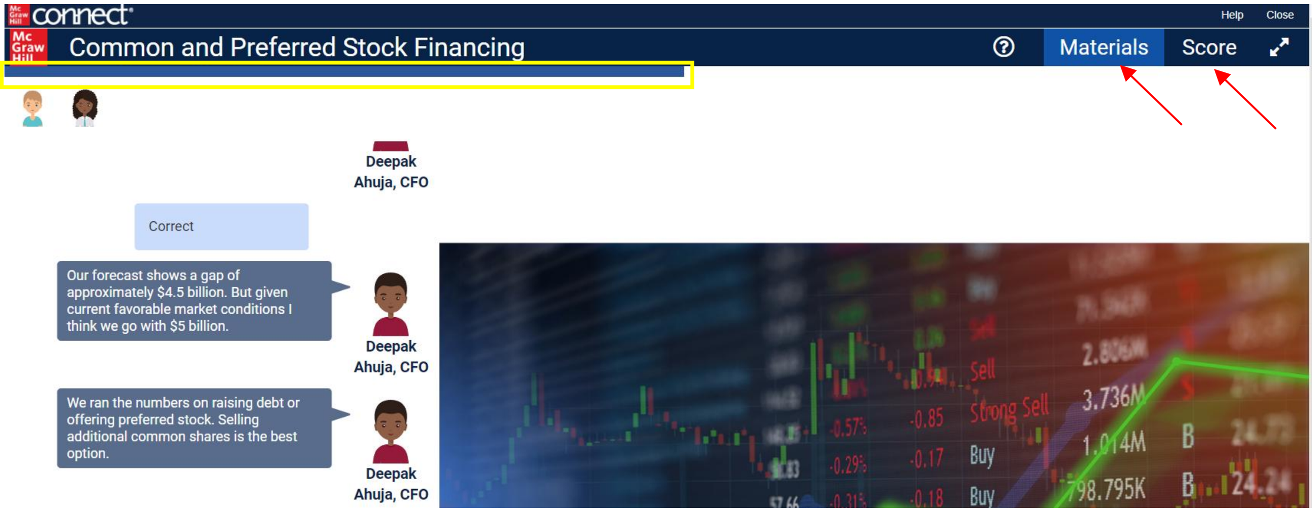


When students begin the ABA assignment, they will see two panels (screenshot below):

1. The left-hand panel is where students engage with various characters featured in the ABA. As stated previously in this Implementation Guide, these characters will offer students background information on core concepts and provide relevant information and periodic check-ins for understanding. Students click through the conversations, answer questions, and follow directions or click links to open a variety of resources.

2. The right-hand panel contains pertinent images, documents and other resources for students to interact with as they complete the ABA assignment.

Red arrows (screenshot below, top right) indicate boxes students click to open additional resources (Materials) or to check their Score at any point in the ABA assignment. Students can see their progress toward completion of the ABA by viewing the blue bar at the top of the ABA screen (outlined in yellow box in screenshot below).



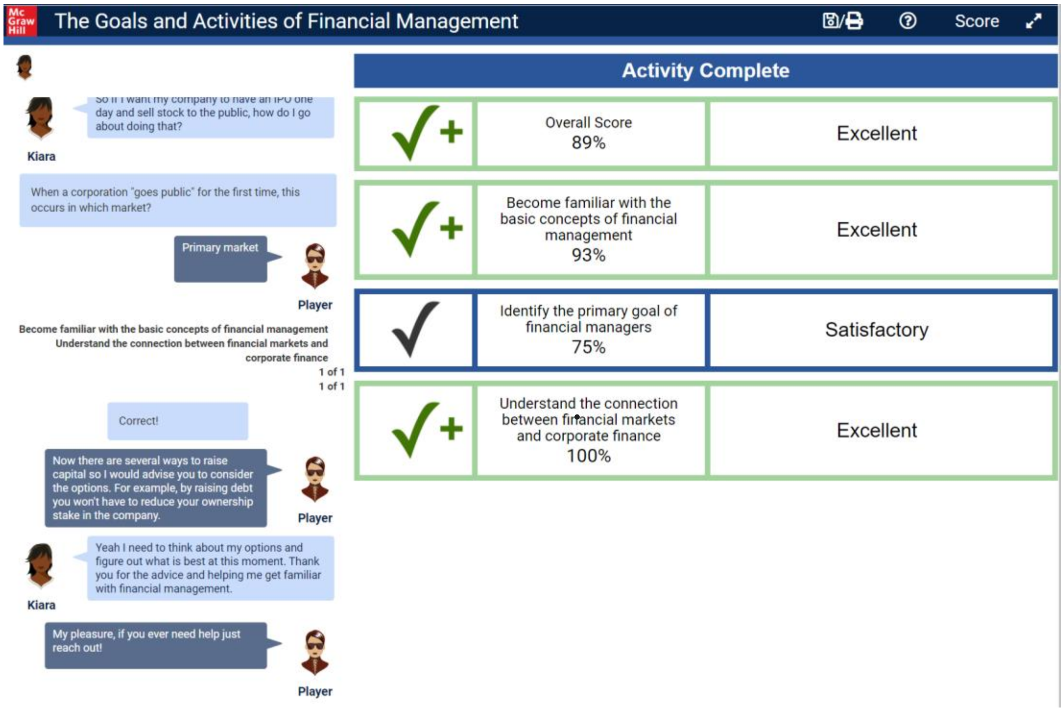
If a student starts an ABA assignment but clicks "Close" to exit out of that attempt, the student's progress on the ABA assignment *has been saved* up to the point where the student exited. They can reopen that attempt and pick up where they left off.

Scoring

When students complete the ABA assignment, they will receive their scores (expressed as a percentage) – an Overall Score for the entire ABA, and scores for each of the Learning Objectives contained within the ABA (screenshot below). Students will also receive feedback on their performance.

Scores are based on students' answers to the questions placed throughout the ABA. Those questions are tied to specific Learning Objectives. The score's percentage measures the students' correct answers during that attempt. If the instructor has allowed multiple attempts in the Connect Set Up Policies, students may re-launch the ABA and achieve a different score.

Students *cannot* change their responses to the questions during an attempt. Once a question response is submitted, it is locked in, so students should be very intentional in submitting their responses. An answer selection is considered final for that attempt and the conversation continues. Typically, ABA characters follow student's answers with feedback indicating whether the response is correct or incorrect. Locking the answers prevents students from easily "gaming the system" until they receive "correct" feedback. As mentioned in the previous section, an instructor may a allow multiple assignment attempts in the Connect Set Up Policies.



Grades appear in the Performance Section of the Instructor Connect Course under Reports.

Assignment Score Weight Distribution

Understand the connection between financial markets and corporate finance	**33** %
Identify the primary goal of financial managers	**33** %
Become familiar with the basic concepts of financial management	**34** %

Assignment Details

Activity: **The Goals and Activities of Financial Management**

Export Score CSV | Export Details CSV

Student	Score	Time Played	Become familiar with the basic concepts of financial management	Identify the primary goal of financial managers	Understand the connection between financial markets and corporate finance
John Smith		**0:02:03**			
Attempt 1	**89%**	**0:02:03**	**93%**	**75%**	**100%**

Suggestions for Using Corporate Finance Application-Based Activities in Your Course

Whether teaching in a face-to-face environment, an online environment, a flipped classroom, or a hybrid model, Corporate Finance ABAs can be used in a variety of ways in support of curriculum goals.

Stand-alone Assignments
Each topic covered by a Corporate Finance ABA focuses on a specific element of the Corporate Finance mix. If there is a topic that instructors feel students typically struggle with or may need additional practice on, a specific Corporate Finance ABA can be either assigned in Connect and/or worked through in real-time during class. The Corporate Finance ABAs can be assigned either in preparation for a topical discussion, as part of an in-class activity or discussion or can be assigned post-discussion.

Integrated with Other Connect Assignments
Corporate Finance ABAs are ideal to use in conjunction with other auto-gradable assignment types available in Connect. ABAs can be integrated into a full suite of weekly assignments that move students through basic understanding of concepts and definitions to higher-level critical thinking and analytical skills.

Connect offers

- Smartbook – McGraw-Hill's adaptive reading environment integrated with questions to reinforce conceptual understanding. Best practice tip – instructors assign Smartbook chapter modules to be due *before* they cover that chapter's material in the course. Attaching points to the reading assignments helps ensure students read the material and come to class prepared.
- Connect Interactives* – a variety of assignable questions in Connect reinforce course content through Comprehension Cases, Video Cases, Decision Generators, and more
- Case Repository**
- Quiz Questions and Testbanks

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For help connecting to the local McGraw-Hill learning technology representative
https://shop.mheducation.com/store/paris/user/findltr.html

* Check with your McGraw-Hill learning technology representative for more information on Connect Interactives availability for your McGraw-Hill text.

** Check with your McGraw-Hill learning technology representative for more information on Connect's Case Repository availability for your McGraw-Hill text.

*** Please see additional links in the Connect Library > Instructor Resources > Application-based Activities site for a full list of ABAs and their descriptions, a McGraw Hill text and chapter key, and sample syllabi.

Chapter 1
INTRODUCTION TO CORPORATE FINANCE

SLIDES

1.1 Chapter 1
1.2 Learning Objectives
1.3 Chapter Outline
1.4 Cash Flow and Financial Statements: A Closer Look
1.5 Corporate Finance and the Financial Manager
1.6 The Financial Manager
1.7 A sample simplified organizational chart - Figure 1.1
1.8 Financial Management Decisions
1.9 Forms of Business Organization
1.10 Sole Proprietorship
1.11 Partnership
1.12 Corporation
1.13 A Corporation by another name…
1.14 Goal of Financial Management
1.15 A More General Goal
1.16 The Agency Problem and Control of the Corporation
1.17 Do Managers Act in the Stockholders' Interests?
1.18 Stakeholders
1.19 Financial Markets and the Corporation 1
1.20 Cash Flows Between the Firm and the Financial Markets
1.21 Financial Markets and the Corporation 2
1.22 Selected Concept Questions
1.23 End of Chapter
1.24 Accessibility Content: Text Alternatives for Images
1.25 A Sample Simplified Organizational Chart - Figure 1.1 – Text Alternative
1.26 Cash Flows Between the Firm and the Financial Markets – Text Alternative

CHAPTER WEB SITES

Section	*Web Address*
1.2	*CFO:* ww2.cfo.com
1.3	www.kingarthurbaking.com
	www.kehe.com
	benefitcorp.net
1.4	*A Guide to the Sarbanes-Oxley Act:* www.soxlaw.com
1.5	*For more about RSUs, check out* www.investopedia.com/terms/r/ restricted-stock-unit.asp *Business Ethics Magazine:* www.business-ethics.com/ *Yahoo Finance:* finance.yahoo.com
1.6	*SEC:* www.sec.gov *NYSE*: www.nyse.com *NASDAQ:* www.nasdaq.com

SUGGESTED VIDEOS

- The Role of the Chief Financial Officer
- Financial Markets

CHAPTER ORGANIZATION

1.1 Finance: A Quick Look
- Finance: The Five Main Areas
- Why Study Finance?

1.2 Corporate Finance and the Financial Manager
- What Is Corporate Finance?
- The Financial Manager
- Financial Management Decisions

1.3 Forms of Business Organization
- Sole Proprietorship
- Partnership
- Corporation
- A Corporation by Another Name…
- Benefit Corporation

1.4 The Goal of Financial Management
- Possible Goals
- The Goal of Financial Management
- A More General Goal
- Sarbanes-Oxley

1.5 The Agency Problem and Control of the Corporation
- Agency Relationships
- Management Goals
- Do Managers Act in the Stockholders' Interests?
- Stakeholders

1.6 Financial Markets and the Corporation
- Cash Flows to and from the Firm
- Primary versus Secondary Markets

1.7 Summary and Conclusions

ANNOTATED CHAPTER OUTLINE

Slide 1: *Chapter 1*
Slide 2: *Learning Objectives*
Slide 3: *Chapter Outline*

1.1. Finance: A Quick Look

A. Finance: The Five Main Areas

Slide 4: *Cash Flow and Financial Statements: A Closer Look*

B. Why Study Finance?

1.2. Corporate Finance and The Financial Manager

A. What Is Corporate Finance?

Slide 5: *Corporate Finance and The Financial Manager*

Corporate finance addresses several important questions:

1. What long-term investments should the firm take on? (Capital budgeting)
2. Where will we get the long-term financing to pay for the investment? (Capital structure)
3. How will we manage the everyday financial activities of the firm? (Working capital)

B. The Financial Manager

Slide 6: *The Financial Manager*

The Chief Financial Officer (CFO) or Vice-President of Finance coordinates the activities of the treasurer and the controller.

The controller handles cost and financial accounting, taxes, and information systems.

The treasurer handles cash management, financial planning, and capital expenditures.

Slide 7: A sample simplified organizational chart - Figure 1.1

Video Note: The Role of the Chief Financial Officer - This video looks at the changing role of the CFO.

C. Financial Management Decisions

Slide 8: *Financial Management Decisions*

The financial manager is concerned with three primary categories of financial decisions.

1. Capital budgeting – process of planning and managing a firm’s investments in fixed assets. The key concerns are the

size, timing, and riskiness of future cash flows.

2. Capital structure – mix of debt (borrowing) and equity (ownership interest) used by a firm. What are the least expensive sources of funds? Is there an optimal mix of debt and equity? When and where should the firm raise funds?

3. Working capital management – managing short-term assets and liabilities. How much inventory should the firm carry? What credit policy is best? Where will we get our short-term loans?

1.3. Forms of Business Organization

Slide 9: *Forms of Business Organization*

A. Sole Proprietorship – A business owned by one person.

Slide 10: *Sole Proprietorship*

Advantages include ease of start-up, lower regulation, single owner keeps all the profits and taxed once as personal income. In addition, with the Tax Cuts and Jobs Act of 2017, up to 20 percent of business income may be exempt from taxation.

Disadvantages include limited life, limited equity capital, unlimited liability and low liquidity.

B. Partnership – A business with multiple owners but not incorporated.

Slide 11: *Partnership*

General partnership – all partners share in gains or losses; all have unlimited liability for all partnership debts.

Limited partnership – one or more general partners run the business and have unlimited liability. A limited partner's liability is limited to his or her contribution to the partnership, and they cannot help in running the business.

Advantages include more equity capital than is available to a sole proprietorship, relatively easy to start (although written agreements are essential), and income taxed once at personal tax rate. Similar to a sole proprietorship, with the Tax Cuts and Jobs Act of 2017, up to 20 percent of business income may be exempt from taxation.

Disadvantages include unlimited liability for general partners, dissolution of partnership when one partner dies or wishes to sell, low liquidity.

C. Corporation – A distinct legal entity composed of one or more owners.

Slide 12: *Corporation*

Corporations account for the largest volume of business (in dollar terms) in the U.S. Advantages include limited liability, unlimited life, separation of ownership and management (ability to own shares in several companies without having to work for all of them), liquidity, and ease of raising capital.

Disadvantages include separation of ownership and management (agency costs) and double taxation. The new tax laws reduce the level of double taxation, but it has not been eliminated.

Lecture Tip: *Although the corporate form of organization has the advantage of limited liability, it has the disadvantage of double taxation. A small business of 75 or fewer stockholders is allowed by the IRS to form an S-Corporation. The S-Corp. organizational form provides limited liability but allows pretax corporate profits to be distributed on a pro rata basis to individual shareholders, who are only obligated to pay personal income taxes on the income. A similar form of organization is the limited liability corporation, or LLC. LLCs are a hybrid form of organization that falls between partnerships and corporations. Investors in LLCs have the protection of limited liability, but they are taxed like partnerships. LLCs first appeared in Wyoming in 1977 and have skyrocketed since. They are especially beneficial for small and medium sized businesses such as law firms or medical practices.*

D. A Corporation by Another Name…

Slide 13: *A Corporation by another name…*

Corporations exist around the world under a variety of names. Table 1.1 lists several well-known companies, along with the type of company in the original language.

E. Benefit Corporation

1.4. The Goal of Financial Management

Slide 14: *Goal of Financial Management*

A. Possible Goals

Profit Maximization – this is an imprecise goal. Do we want to maximize long-run or short-run profits? Do we want to maximize accounting profits or some measure of cash flow? Because of the different possible interpretations, this should not be the main goal of the firm.

Other possible goals that students might suggest include minimizing costs or maximizing market share. Both have potential problems. We can minimize costs by not purchasing new equipment today, but that may damage the long-run viability of the firm. Many "dot-com" companies got into trouble in the late '90s because their goal was to maximize market share. They raised substantial amounts of capital in IPOs and then used the money on advertising to increase the number of "hits" on their site. However, many firms failed to translate those "hits" into enough revenue to meet expenses and they quickly ran out of capital. The stockholders of these firms were not happy; stock prices fell dramatically, and it became difficult for these firms to raise additional funds. Many of these companies have gone out of business.

B. The Goal of Financial Management

From a stockholder (owner) perspective, the goal of buying the stock is to gain financially. Thus, *the goal of financial management in a corporation is to maximize the current value per share of the existing stock.*

Lecture Tip: *The late Roberto Goizueta, former chairman and CEO of the Coca-Cola Company, wrote an essay entitled "Why Share-Owner Value?" that appeared in the firm's 1997 annual report. That essay is reprinted in full at the end of this material. It is an excellent introduction to the goal of financial management at any level. It may also be useful to discuss how Mr. Goizueta's vision transferred to the stock market's valuation of the company. The following article illustrates the difference in strategy between Coca-Cola and Pepsi-Co during Mr. Goizueta's tenure.*

"How Coke is Kicking Pepsi's Can," *Fortune*, *October 28, 1996.*

Coke focused on soft drinks while Pepsi-Co diversified into other areas. Pepsi-Co's goal was to double revenues every 5 years, while Mr. Goizueta focused on return on investment and stock price. The article states that Goizueta "has created more wealth for stockholders than any other CEO in history." In mid-1996, Pepsi-Co sold at 23 times earnings with return on equity of about 23% and Coke sold at 36 times earnings with a return on equity of around 55%. The article goes on to discuss the differing strategies in more detail. It provides a nice validation of Mr. Goizueta's remarks in his letter to the shareholders.

Lecture Tip: *The validity of this goal assumes "investor rationality." In other words, investors in the aggregate prefer more dollars to fewer and less risk to more. Rational investors will act as risk-averse, return-seekers in making their purchase and sale decisions. Given different levels of risk aversion and wealth preferences, the only single goal suitable for all shareholders is the maximization of their wealth (which is represented by the value of their holdings of the firm's common stock).*

Lecture Tip: *It may be worth to point out recent events about Shareholder Primacy. In 2019, the Business Roundtable redefined the purpose of a corporation to help promote an "economy that serves all Americans." The full statement can be found here (accessed on 3/20/2025: https://www.businessroundtable.org/business-roundtable-redefines-the-purpose-of-a-corporation-to-promote-an-economy-that-serves-all-americans)*

C. A More General Goal – To maximize the market value of owners' equity.

Slide 15: *A More General Goal*

Many students think that this means that firms should do "anything" to maximize stockholder wealth. It is important to point out that unethical behavior does not ultimately benefit owners.

Ethics Note: *Any number of ethical issues can be introduced for discussion – several of which are discussed in more detail in later sections. One particularly good opener to this topic is the issue of the responsibility of the managers and stockholders of tobacco firms. Is it ethical to sell a product that is known to be addictive* *and dangerous to the health of the user even when used as intended? Is the fact that the product is legal relevant? Do recent court decisions against the companies matter? What about the way companies choose to market their product? Are these issues relevant to financial managers?*

D. Sarbanes-Oxley

"Sarbox" or "SOX," as it is commonly referred to, was designed to reduce the likelihood of corporate scandals by increasing investor protection by limiting certain actions by executives and increasing overall reporting requirements. The latter in particular has increased the cost of incorporation and has led some firms to avoid going public or even to "go dark."

1.5. The Agency Problem and Control of the Corporation

Slide 16: *The Agency Problem and Control of the Corporation*

A. Agency Relationships – The relationship between stockholders and management is called the agency relationship. This occurs when one party (principal) hires another (agent) to act on their behalf. The possibility of conflicts of interest between the parties is termed the agency problem.

B. Management Goals

Agency costs
direct costs – compensation and perquisites for management
indirect costs – cost of monitoring and sub-optimal decisions

Ethics Note: *When shareholders elect a board of directors to oversee the corporation, the election serves as a control mechanism for management. The board of directors bears legal responsibility for corporate actions. However, this responsibility is to the corporation itself and not necessarily to the stockholders. Although the following happened several years ago, it still makes for an interesting discussion of directors' and managers' duties:*

In 1986, Ronald Perelman engaged in an unsolicited takeover offer for Gillette. Gillette's management filed litigation against Perelman and subsequently entered into a standstill agreement with Perelman. This action eliminated the premium that Perelman offered shareholders for their stock in Gillette.

A group of shareholders filed litigation against the board of directors in response to its actions. It was subsequently discovered that Gillette had entered into standstill agreements with ten additional companies. When questioned regarding the rejection of Perelman's offer, management responded that there were projects on line that could not be discussed (later revealed to be the "Sensor" razor, which was one of the most profitable new ventures in Gillette's history up to that time). Thus, despite appearances, management's actions may have been in the best interests of the firm. This case indicates that management may consider factors other than the bid when considering a tender offer.

C. Do Managers Act in the Stockholders' Interests?

Slide 17: Do Managers Act in the Stockholder's Interests?

Managerial compensation can be used to encourage managers to act in the best interest of stockholders. One commonly cited tool is stock options. The idea is that if management has an ownership interest in the firm, they will be more likely to try to maximize owner wealth.

Lecture Tip: *A 1993 study performed at the Harvard Business School indicates that the total return to shareholders is closely related to the nature of CEO compensation; specifically, higher returns were achieved by CEOs whose pay package included more option and stock components. (See The Wall Street Journal, November 12, 1993, p. B1). However, this may not be the best way to encourage managers to act in the stockholders' best interest.*

Stern Stewart & Company developed a tool called EVA®, discussed later in the text, which measures how much "economic value" is being added to a corporation by management decisions. According to Stern-Stewart's web site (https://sternvaluemanagement.com/economic-value-added-eva), companies that tie management compensation to EVA® significantly outperform competitors that do not. They are conducting ongoing studies to measure this performance, but data up through November 2004 indicate that the stock returns for these companies have outperformed their competitors by 84% over a five-year period.

Both of these examples illustrate that carefully crafted compensation packages can reduce the conflict between management and stockholders. It should be noted that in 2007 it was widely publicized that many firms had "backdated" options in *an attempt to provide "in-the-money" compensation to executives—does this system provide the desired incentive?*

Lecture Tip: *According to The National Center for Employee Ownership, broad based stock option plans have increased dramatically, not only for technology firms, but also for non-tech firms such as Starbucks and the Gap. They estimate that as of 2001, over 10 million employees in the United States will have received stock options. Some firms have found a way to provide stock-based incentive to employees without giving them equity ownership at all. As reported in the October 26, 1998 issue of Fortune, "phantom stock" is used by private companies such as Kinko's and Mary Kay, Inc., as well as public companies, to provide employees with an incentive to work harder. Generally, an employee is awarded "shares" on a bonus basis, and the share values increase if the value of the business increases. (For a private firm, this means obtaining outside appraisals of value based on earnings multiples, etc.) At some future point, the employee has the right to cash in his "shares."*

Stockholders technically have control of the firm, and dissatisfied shareholders can oust management via proxy fights, takeovers, etc. However, this is easier said than done. Staggered elections for board members often make it difficult to remove the board that appoints management. Poison pills and other anti-takeover mechanisms make hostile takeovers difficult to accomplish.

D. Stakeholders

Slide 18: *Stakeholders*

Stakeholders are other groups, besides stockholders, that have a vested interest in the firm and potentially have claims on the firm's cash flows. Stakeholders can include creditors, employees, and customers.

Ethics Note: *A discussion of stakeholder interests leads very nicely into a discussion of ethical decision making. Theories of ethical behavior focus on the rights of all parties affected by a decision, not just one or two. The "utilitarian" model defines an action as acceptable if it maximizes the benefit, or minimizes the harm, to stakeholders in the aggregate. The "golden rule" model deems a decision ethical if all stakeholders are treated as the decision maker would wish to be treated. Finally, the Kantian "basic rights" model defines acceptable actions as those that minimize* *the violation of stakeholders' rights.*

Ethics Note: *The antitrust case against Microsoft can generate a healthy discussion of ethical behavior, innovation, and the government's role in monitoring business practices. The basic idea behind the case is that: (1) Microsoft stifled competition by imposing stiff penalties on computer manufacturers that chose to install operating systems other than Windows on some of their machines; (2) Microsoft tried to put Netscape out of business by incorporating Internet Explorer into the operating system; and (3) Microsoft has an unfair advantage in the applications programming area because their programmers have access to the source code for the operating system. There were other issues as well, but these were the major ones. The Judge in the case originally found that Microsoft did violate antitrust laws and that they continued to operate in a monopolistic fashion. He ordered the break-up of Microsoft into an "operating system" company and an "applications" company. The Judge also ordered that Microsoft allow programmers from the Company's competitors to come to a secured location and view the source code for Microsoft Windows. Microsoft contended that this would allow other companies to determine the direction that Microsoft is moving with their software and eliminate the competitive advantage that their research and development has afforded the company. The case was appealed and Microsoft was still found in violation of antitrust laws, but not to the extent found in the original case.*

The Final Judgment was issued on November 12, 2002, and has the following components: (1) Microsoft cannot retaliate against an Original Equipment Manufacturer (OEM) if the OEM "is or is contemplating developing, distributing, promoting, using, selling, or licensing any software that competes with Microsoft Platform Software" or ships a computer with more than one operating system; (2) Microsoft must publish and use a consistent licensing agreement schedule with all covered OEMs; (3) Microsoft cannot restrict OEMs from selling computers that include competing products, display competing product icons on the desktop, and launch competing products when a Microsoft application would normally be launched; (4) Microsoft must allow Independent Software Vendors (ISVs), Independent Hardware Vendors (IHVs), Internet Access Providers (IAPs), Internet Content Providers (ICPs), and OEMs access to Windows Operating System Product source code as necessary to develop products that will work effectively with the operating system – these companies must demonstrate why they need access and they are limited to access to that code that is required for "interoperating" with the operating *system; (5) Microsoft is not required to disclose any intellectual property rights related to security or that is designed to prevent software piracy.*

The Final Judgment called for the appointment of a technical committee that will assist in the enforcement and compliance with the judgment and Microsoft was required to appoint an internal compliance officer to make sure that all employees of the firm understand and comply with the judgment. Reports on compliance are routinely filed with the Department of Justice and can be found, along with the Final Judgment at http://www.usdoj.gov/atr/cases/ms_index.htm.

1.6. Financial Markets and the Corporation

Slide 19: *Financial Markets and the Corporation 1*

A. Cash Flows to and from the Firm

Figure 1.2 provides a concise summary of the cash flows to and from the firm.

Slide 20: *Cash Flows Between the Firm and the Financial Markets*

A firm issues securities (stocks and bonds) to raise cash for investments (usually in real assets). The operating cash flows generated from the investment in assets allows for the payment of taxes, reinvestment in new assets, payment of interest and principal on debt, and payment of dividends to stockholders.

Video Note: Financial Markets – This video discusses how capital is raised in financial markets and shows an open-outcry market at the Chicago Board of Trade.

B. Primary versus Secondary Markets

Slide 21: *Financial Markets and the Corporation 2*

Primary market – the market in which securities are sold by the company. Public and private placements of securities, SEC registration, and underwriters are all part of the primary market.

Lecture Tip: *Students are often curious about the nature of the information that is made public at the time of a primary offering. An interesting example of full disclosure appeared in The Wall Street Journal several years ago in the form of excerpts from a prospectus for a company called Indian Bingo, Inc.*

> *"To hear Indian Bingo tell it, prospective investors should think carefully before deciding to shell out $1 per share for the company's proposed initial public offering of five million common shares."*
>
> *"Indian Bingo says in a preliminary registration statement filed with the Securities and Exchange Commission that it wants to get into the business of operating bingo games on Indian reservations. But, Indian Bingo points out that the company would be a 'high-risk' investment. Among the reasons: the company is a month old, such bingo games may be held illegal, third-party studies of such activities haven't been made, the company doesn't yet have any source of income, and the underwriter hasn't any experience as a securities dealer."*
>
> *Also, "one of [the firm's] main consultants has served time in prison for obstruction of justice, and another has served time for conspiracy and mail fraud. Both have also received civil sanctions from the SEC for allegedly fraudulent activities, according to federal court records and SEC documents. Together, the two consultants and their family will control more than 50% of Indian Bingo's stock."*

Secondary market – the market where securities that have already been issued are traded between investors. The stock exchanges, such as the New York Stock Exchange, and the over-the-counter market, such as the NASDAQ, are part of the secondary market.

Dealer versus Auction Markets – A dealer market is one where you have several traders that carry an inventory and provide prices at which they stand ready to buy (bid) and sell (ask) the securities. The Nasdaq market is an example of a dealer market. An auction market has a physical location where buyers and sellers are matched, with little dealer activity.

In the United States, larger firms that are publicly traded primarily list their shares on either the NYSE or NASDAQ, each of which has its own set of listing requirements.

1.7. Summary and Conclusions

Slide 22: *Selected Concept Questions*

Slide 23: End of Chapter

Why Share-Owner Value?

At The Coca-Cola Company, our publicly stated mission is to create value over time for the owners of our business. In fact, in our society, that is the mission of any business: to create value for its owners.

Why? The answer can be summed up in three reasons.

First, increasing share-owner value over time is the job our economic system demands of us. We live in a democratic capitalist society, and here, people create specific institutions to help meet specific needs. Governments are created to help meet civic needs. Philanthropies are created to help meet social needs. And companies are created to help meet economic needs. Business distributes the lifeblood that flows through our economic system not only in the form of goods and services, but also in the form of taxes, salaries and philanthropy.

Creating value is a core principle on which our economic system is based; it is the job we owe to those who have entrusted us with their assets. We work for our share owners. That is – literally – what they have put us in business to do.

Saying that we work for our share owners may sound simplistic - but we frequently see companies that have forgotten the reason they exist. They may even try in vain to be all things to all people and serve many masters in many different ways. In any event, they miss their primary calling, which is to stick to the business of creating value for their owners.

Furthermore, we must always be mindful of the fact that while a healthy company can have a positive and seemingly infinite impact on others, a sick company is a drag on the social order of things. It cannot sustain jobs, much less widen the opportunities available to its employees. It cannot serve customers. It cannot give to philanthropic causes.

And it cannot contribute anything to society, which is the second reason we work to create value for our share owners: If we do our jobs, we can contribute to society in very meaningful ways. Our Company has invested millions of dollars in Eastern Europe since the fall of the Berlin Wall, and people there will not soon forget that we came early to meet their desires and needs for jobs and management skills. In the process, they are becoming loyal consumers of our products, while we are building value for our share owners – which was our job all along.

Certainly, we – as a Company – take it upon ourselves to do good deeds that directly raise the quality of life in the communities in which we do business. But the real and lasting benefits we create don't come because we do good deeds, but because we do *good work – work focused on our mission of creating value over time for the people who own the Company. Among those owners, for example, are university endowments, philanthropic foundations and other similar nonprofit organizations. If The Coca-Cola Company is worth more, those endowments are similarly enriched to further strengthen the educational institutions' operations; if The Coca-Cola Company is worth more, those foundations have more to give, and so on. There is a beneficial ripple effect throughout society.*

Please note that I said creating value "over time," not overnight. Those two words are at the heart of the third reason behind our mission: Focusing on creating value over the long term keeps us from acting shortsighted.

I believe share owners want to put their money in companies they can count on, day in and day out. If our mission were merely to create value overnight, we could suddenly make hundreds of decisions that would deliver a staggering short-term windfall. But that type of behavior has nothing to do with sustaining value creation over time. To be of unique value to our owners over the long haul, we must also be of unique value to our consumers, our customers, out bottling partners, our fellow employees and all other stakeholders – over the long haul.

Accordingly, that is how the long-term interests of the stakeholders are served – as the long-term interests of the share owners are served. Likewise, unless the long-term interests of the share owners are served, the long-term interests of the stakeholders will not be served. The real possibility for conflict, then, is not between share owners and stakeholders, but between the long-term and the short-term interests of both. Ultimately, everyone benefits when a company takes a long-term view. Ultimately, no one benefits when a company takes a short-term view.

The creation of unique value for all stakeholders, including share owners, over the long haul, presupposes a stable, health society. Only in such an environment can a company's profitable growth be sustained. Thus, the exercise of what is commonly referred to as "corporate responsibility" is a supremely rational, logical corollary of a company's essential responsibility to the long-term interests of its share owners. A company will only exercise this essential responsibility effectively if it promotes that social well-being necessary for a healthy business environment. It is as irrational to suppose that a company is primarily a welfare agency as it is to suppose that a company should not be concerned at all about the social welfare. Both views sacrifice the long-term common good to short-term benefits – whether share-owner benefits or stakeholder benefits.

Certainly, harsh competitive situations can sometimes call for harsh medicine. But in the main, our share owners look to us to deliver sustained, long-term value. We do that by building our businesses and growing them profitably.

At The Coca-Cola Company, we have built our business and grown it profitably for more than 110 years, because we have remained disciplined to our mission.

Not long ago, we came up with an interesting set of facts: A billion hours ago, human life appeared on Earth. A billion minutes ago, Christianity emerged. A billion seconds ago, the Beatles changed music forever. A billion Coca-Colas ago was yesterday morning.

The question we ask ourselves now is: What must we do to make a billion Coca-Colas ago be this morning? By asking that question, we discipline ourselves to the long-term view.

Ultimately, the mission of this Atlanta soft-drink salesman – and my 26,000 associates – is not simply to sell an extra case of Coca-Cola. Our mission is to create value over the long haul for the owners of our Company.

That's what our economic system demands of us. That's what allows us to contribute meaningfully to society. That's what keeps us from acting shortsighted. As businessmen and businesswomen, we should never forget that the best way for us to serve all our stakeholders – not just our share owners, but our fellow employees, our business partners and our communities – is by creating value over time for those who have hired us.

That, ultimately, is our job.

Roberto C. Goizueta
Chairman, Board of Directors,
and Chief Executive Officer
February 20, 1997

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