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Testbank

to accompany

Contemporary Strategic Management 2nd edition

by Grant et al

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Chapter 2:
Corporate governance and sustainability

True/False Questions

1. Corporate governance is solely about overseeing internal operations of a company.
Reference: Also enables leaders to compete more effectively since a more responsible organisation is able to exercise rights to a voice in public policy

a. True
*b. False

General Feedback:
Difficulty: Easy

2. The Commonwealth Association of Corporate Governance aims to promote best international standards on governance on corporate governance on a country level.

*a. True
b. False

General Feedback:
Difficulty: Easy

3. The separation of ownership and management is the fundamentally necessary to create shareholder value

a. True
*b. False

General Feedback:
Difficulty: Medium

4. Corporate governance is about ensuring that companies act in the best interest of the nation they are part of.

a. True
*b. False

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General Feedback:
Difficulty: Easy

5. The CEO and the chairman of the governing board are usually the same person.

a. True
*b. False

General Feedback:
Difficulty: Easy

6. True commitment and personal identification of a manager with his company is the root of the principal-agent problem.

a. True
*b. False

General Feedback:
Difficulty: Medium

7. The networking role of the governing board is to ensure the functionality of the company's internal IT-networks and systems.

a. True
*b. False

General Feedback:
Difficulty: Medium

8. Governing boards are charged with making all major decisions, including strategic goals.

*a. True
b. False

General Feedback:
Difficulty: Medium

9. Anticipating industry movement and future customer preferences to create major profit growth opportunities is also known as managerial opportunism.

a. True
*b. False

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General Feedback:
Difficulty: Medium

10. Controlling managerial behaviour is a key responsibility of the governing board

*a. True
b. False

General Feedback:
Difficulty: Medium

11. To function most effectively, governing board members should have similar skill sets, backgrounds and not differ considerably in regards to demographic factors.

a. True
*b. False

General Feedback:
Difficulty: Hard

12. The size of governing board throughout the past 50 years has grown rapidly due to the increasing average size of multinational corporations.

a. True
*b. False

General Feedback:
Difficulty: Medium

13. The terms 'governing board', 'board of trustees' and 'supervisory board' are basically referring to the same group of elected individuals

*a. True
b. False

General Feedback:
Difficulty: Hard

14. The audit committee should assist the board of directors to ensure proper financial reporting.

*a. True

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b. False

General Feedback:
Difficulty: Medium

15. The audit committee is at the highest level of a company to make all major decisions with members appointed by shareholders at the annual general meeting.

a. True
*b. False

General Feedback:
Difficulty: Medium

16. Performance-based share bonuses can contribute to align employees' interests with those of shareholders.

*a. True
b. False

General Feedback:
Difficulty: Medium

17. In regards to executive compensations, a continuous salary is the only effective method to close the interest gap between a company's manager and the owners.

a. True
*b. False

General Feedback:
Difficulty: Medium

18. Ownership concentration, audit committees and corporate market control are all internal governance mechanisms.

a. True
*b. False

General Feedback:
Difficulty: Medium

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19. A situation in which managers do not need to take up the full consequences and responsibilities of their decisions and, therefore, may have a tendency to act less carefully than they should could be described as a case of moral hazard.

*a. True
b. False

General Feedback:
Difficulty: Medium

20. Agency costs are all costs that are related to the employment of an external manager.

a. True
*b. False

General Feedback:
Difficulty: Medium

21. Stakeholder analysis is a process of systematically gathering quantitative information about the ownership of an organisation in order to determine whose interests should be taken into account when developing and implementing policies and programs.

a. True
*b. False

General Feedback:
Difficulty:

22. The major objective of corporate governance isto increase the life and wealth of the society in total and the local communities a company is embedded in.

a. True
*b. False

General Feedback:
Difficulty:

23. In the context of strategic management, the terminologies governance and sustainability can be treated as synonyms.

a. True
*b. False

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General Feedback:
Difficulty: Easy

24. The separation of ownership and management in modern organisation is the root problem of corporate governance.

*a. True
b. False

General Feedback:
Difficulty: Easy

25. Good corporate governance is unlikely to increase a company's long-term performance, but it definitely helps to increase its reputation within its community.

a. True
*b. False

General Feedback:
Difficulty:

Multiple Choice Questions

26. The division of power in modern corporations means that:

a. Shareholders lack direct control of large, publicly traded companies
b. Shareholders cannot verify whether managers are behaving in the shareholders' best interests
c. Managers might pursue their own personal goals such as minising their pay
*d. All of the above.

General Feedback:
References: Chapter 2 page 49, Difficulty: Medium

27. What is corporate governance about?

a. Profit maximisation
b. Controlling decisions
*c. Meeting the needs of stakeholders
d. Compliance with human rights

General Feedback:
References: Chapter 2 page 41, Difficulty: Easy

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28. Ideally corporate governance does:

a. Establish a process for how important strategic decisions are made and controlled within organisations
b. Enhance disclosure and transparency
c. Provide an efficient legal and regulatory enforcement framework
*d. All of the above

General Feedback:
References: Chapter 2 page 41, Difficulty: Easy

29. Corporate governance is closely related to:

*a. The sustainability of an organisation
b. Manager's wealth
c. Human rights
d. The national government

General Feedback:
References: Chapter 2 page 42, Difficulty: Medium

30. The governing board of an organisation:

*a. Is under influence of owners, auditors, and other stakeholders
b. Is not influenced by any external party in order to act independently to advance the members interests
c. Is only influenced by the national government
d. May consist only of members that have been former employees of the organisation

General Feedback:
References: Chapter 2 page 44, Difficulty: Medium

31. The continuing commitment by business to behave ethically and contribute to economic development, while improving the quality of life of the workforce, the local communities and society at large is called:

a. Corporate governance
*b. Corporate social responsibility
c. Sustainability
d. Monitoring

General Feedback:
References: Chapter 2 page 44, Difficulty: Easy

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32. A socially responsible company:

a. Donates a major part of its profit to communities and charity organisations
b. Takes legal actions against competitors that have negative impacts on the society
*c. Makes profits in a legal and ethical way
d. Does not make employees redundant

General Feedback:
References: Chapter 2 page 45, Difficulty: Easy

33. Current trends in corporate governance are:

a. The extension of practices of corporate governance of private enterprises to the public sector
b. The international convergence of corporate governance practices
c. The establishment of labour unions
*d. Answers a and b

General Feedback:
References: Chapter 2 page 67, Difficulty: Medium

34. The provision of fair shares of wealth creation to the local and global societies is:

a. Bad for the organisation, but good for society
*b. Good for the organisation and good for the society
c. A major drawback of the idea of corporate social responsibility
d. Not offer the society for the organisation

General Feedback:
References: Chapter 2 page 44, Difficulty: Easy

35. The process of managing the expectations of people, groups or organisations that have an interest in a company and will be affected by its actions is called:

*a. Stakeholder management
b. Relationship-based management
c. Strategic management
d. Confucianism

General Feedback:
References: Chapter 2 page 46, Difficulty: Easy

36. Michael Porter is a:

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a. Representative of major stakeholder groups in the United States
b. Governor of the US Council on Competitiveness
*c. A well-known researcher in strategic management
d. All of the above

General Feedback:
References: Chapter 2 page 46, Difficulty: Easy

37. On the long-run, the objectives of an organisation can only be achieved by:

*a. Protecting and balancing the interests of different stakeholder groups.
b. Protecting an using relations to the local authorities to gain competitive advantage
c. Paying significant dividends to shareholders in order to meet their interests
d. All of the above

General Feedback:
References: Chapter 2 page 46, Difficulty: Medium

38. Incorporating the participations of major stakeholders at a company's governing board will most likely:

a. Reduce the profitability of the company
*b. Have an impact on the strategies adopted
c. Have no major impact on the organisation
d. Increase shareholder wealth

General Feedback:
References: Chapter 2 page 46, Difficulty: Medium

39. A major impediment to corporate governance effectiveness is has been found to be a disparity between:

a. Shareholder and stakeholder interests
b. Rich and poor
*c. Corporate directors' and managers' perception regarding stakeholder management
d. The strategic objectives of an organisation and its profit maximising motive

General Feedback:
References: Chapter 2 page 47, Difficulty: Medium

40. The process of systematically gathering and analysing qualitative information to determine whose interests should be into account when developing policies or programs is known as:

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a. Qualitative research method
*b. Stakeholder analysis
c. The Freeman-approach to interest policy formulation
d. Shareholder analysis

General Feedback:
References: Chapter 2 page 47, Difficulty: Medium

41. The design of a stakeholder approach to strategic management was first proposed by:

a. Kennedy
*b. Freeman
c. Porter
d. None of the above

General Feedback:
References: Chapter 2 page 48, Difficulty: Easy

42. Freeman proposed three levels of stakeholder analysis:

a. Organisational, public and traditional
b. Corporate, business-unit and functional
c. Internal, external and superior
*d. Rational, process and transactional

General Feedback:
References: Chapter 2 page 47, Difficulty: Medium

43. The identification, specification and analysis of interests of each stakeholder group linked to their relative power characteristics are at the core of which of Freedman's levels of stakeholder analysis?

*a. The rational level
b. The process level
c. The transactional level
d. All of the above

General Feedback:
References: Chapter 2 page 47, Difficulty: Hard

44. Corporate governance only became important in modern organisations, because:

a. Their size enabled them to tie closer relationships to politics

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*b. In the past, companies were managed by the owners and there was no problem of the conflict between ownership and management
c. Impacts from an increased competitive environment has required companies to become more efficient
d. The rising awareness of large organisations on global warming

General Feedback:
References: Chapter 2 page 48, Difficulty: Hard

45. In the context of strategic management, if we speak of residual income, we mean:

a. Consumers income that is available for purchasing the product or service of the company
*b. Income from the operations of the firm after all costs and expenses have been paid
c. Income that should be donated to charity and distributed to the society an organisation is embedded in
d. Income from financial assets in possession of the company

General Feedback:
References: Chapter 2 page 49, Difficulty: Medium

46. The agency theory explains:

*a. Potential conflicts arising between a shareholder and a manager over companies
b. The major efficiencies that can be achieved through the use of exclusive distribution agents
c. The negative implications of corporate governance mechanisms
d. The interference of political agents with the decisions of corporate managers

General Feedback:
References: Chapter 2 page 49, Difficulty: Medium

47. The difficulty for a single shareholder to monitor the company's business because this would require efforts over proportional to the value of the shareholding is the key issue of:

a. Corporate social responsibility
b. Residual income
c. Shareholder analysis
*d. Agency theory

General Feedback:
References: Chapter 2 page 49, Difficulty: Medium

48. Managers' own personal goals such as avoiding risk, maximising their pay and spending corporate money on prestige projects are in conflict with the organisations goals mainly due to:

*a. The separation of ownership and management

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b. Low moral standards in the management class
c. Poor organisational goals
d. A malfunctioning social and economic system with inherent corruption

General Feedback:
References: Chapter 2 page 48, Difficulty: Medium

49. Based on the assumption that the human being is rational, self-interested, and opportunistic, managers as agents are inclined to practice managerial opportunism if:

a. They previously worked for a competitor
b. Effective corporate governance mechanisms are in place
*c. No effective corporate governance mechanisms are in place
d. The prevailing legislation does not allow for such behaviour

General Feedback:
References: Chapter 2 page 48, Difficulty: Medium

50. Situations in which managers do not need to take up the full consequences for their decisions and, therefore act more risky or less carefully are also known as:

*a. Moral hazard
b. Managerial Opportunism
c. The principal-agent problem
d. Risk neutrality

General Feedback:
References: Chapter 2 page 48, Difficulty: Medium

51. Agency costs are incurred to:

a. Pay agents to manage the company
b. Distribute the company's products through exclusive sales agents
*c. Protect the principal's interests against the inappropriate actions of the agent
d. Compensate corporate managers

General Feedback:
References: Chapter 2 page 49, Difficulty: Medium

52. Controlling costs of managers related to the process of aligning their interests with those of shareholders are also known as:

a. Sunk costs

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b. Opportunity costs
*c. Agency costs
d. None of the above

General Feedback:
References: Chapter 2 page 50, Difficulty: Medium

53. There are two major types of governance mechanisms:

a. societal and political
b. managerial and operational
*c. external and internal
d. obligatory and voluntary

General Feedback:
References: Chapter 2 page 50, Difficulty: Easy

54. The following can be referred to as external governance mechanisms:

a. Societal pressures
b. Possible changes in the corporate ownership structure
c. Political pressures
*d. All of the above

General Feedback:
References: Chapter 2 page 50, Difficulty: Medium

55. In some cases, social, political, and institutional forces may not be sufficient to control corporate leaders. A good example for failure is:

a. Microsoft
*b. Enron
c. Fonterra
d. Toyota

General Feedback:
References: Chapter 2 page 62, Difficulty: Medium

56. Corporate market control mechanisms are most effective for companies that are:

*a. Publicly listed at the stock exchange
b. The market leader in their industry
c. Owned by a large variety and numer of shareholders

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d. Independent of external sources of funding

General Feedback:
References: Chapter 2 page 52, Difficulty: Hard

57. Corporate market control mechanisms are fundamentally based on:

*a. Modern economic systems allowing voting shares to be publicly bought or sold
b. Day-to-day operations
c. a. and b.
d. None of the above

General Feedback:
References: Chapter 2 page 52, Difficulty: Hard

58. An indicator of the extent to which managers are efficiently operating the corporation and maximising shareholder wealth can be:

*a. The share price of the company
b. The company's wealth in the long term
c. The company's number of shareholders
d. The average annual income of the company's shareholders

General Feedback:
References: Chapter 2 page 52, Difficulty: Hard

59. Internal governance mechanisms that oversee managerial activities and performance include:

a. closely monitor management activities
b. abuse their position of dominant control
c. reduce the likelihood that the firm becomes subject to a hostile takeover
*d. All of the above
b. Executive compensation
c. Audit committee
d. Governing board
*e. All of the above
65, Ownership concentration, or so-called blockholders, can:

General Feedback:
References: Chapter 2 page 53, Difficulty: Medium

Feedback:
*e) References: Chapter 2 page 53, Difficulty: Hard

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60. The following executive compensation instruments help to align the interests of managers with those of shareholders:

a. Share options
b. Performance-based cash boni
c. Fringe benefits
*d. All of the above

General Feedback:
References: Chapter 2 page 54, Difficulty: Hard

61. One of the responsibilities of the auditing board is to:

a. Control and monitor strategic management decisions
b. Listen to the concerns of shareholders at the annual general meeting
*c. Verify that the accounting records are kept in a proper manner
d. None of the above

General Feedback:
References: Chapter 2 page 56, Difficulty: Medium

62. In response to the Asian crisis in the late 1990s, many countries in the Asia-Pacific region came up with legislation that required larger firms to:

a. Form executive management boards
b. Get listed at the national stock exchange
*c. Form internal audit committee
d. To sell a majority share to the government

General Feedback:
References: Chapter 2 page 56, Difficulty: Medium

63. A group of elected individuals that acts in the owners' to formally monitor and control the company's top-level executives is also called:

*a. Governing board
b. Audit committee
c. Security and exchange commission
d. Employee committee

General Feedback:
References: Chapter 2 page 57, Difficulty: Easy

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64. A governing board is:

a. Responsible for setting strategic goals
b. Responsible for government organisations
c. Standing in place of shareholders in case of a business corporation.
*d. All except of b.

General Feedback:
References: Chapter 2 page 57, Difficulty: Hard

65. In regards to the composition of governing boards there are basically two types of board directors:

a. Practitioners and academic
b. Managerial and operational
*c. Internal and external
d. Compensated and voluntary

General Feedback:
References: Chapter 2 page 58, Difficulty: Easy

66. The recent debate about director independency in Australia and other developed countries is primarily concerned with the employment of:

a. Children
*b. Internal directors
c. Employees that previously worked for a competitor
d. Employees that previously worked for a government agency

General Feedback:
References: Chapter 2 page 58, Difficulty: Medium

67. Heterogenity in the composition of governing board often provides:

a. A fertile ground for destructive debates, personal arguments and intrigues between members
*b. A diverse and unique skill set that can be a potential source of expertise for the organisation
c. The precondition to quickly reach consensus on strategic decisions
d. All of the above

General Feedback:
References: Chapter 2 page 58, Difficulty: Easy

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68. From an academic perspective, three sets of interrelated roles played by governing boards can be identified:

*a. Strategy-making, controlling, networking and coordinating role
b. Advisory, monitoring and operating role
c. Accounting, auditing and resource allocation role
d. None of the above roles are found in governing boards

General Feedback:
References: Chapter 2 page 61, Difficulty: Medium

69. Linking the company with its external environment and securing critical resources is a role of the:

a. Audit Committee
b. Executive management team
*c. Governing board
d. Government

General Feedback:
References: Chapter 2 page 62, Difficulty: Medium

70. The CEO of a multinational enterprise is usually appointed by:

*a. The governing board
b. The shareholders
c. the stakeholders
d. The employee council

General Feedback:
References: Chapter 2

71. In its coordinating role, the governing board seeks to:

a. Coordinate managerial work load to achieve maximum management efficiency
*b. Balance the interests of stakeholder groups
c. Coordinate the supply chain and logistics to achieve superior efficiency
d. Maximise profits through synergies

General Feedback:
References: Chapter 2 page 62, Difficulty: Medium

72. Referring to governing boards, the formation of pricing cartels with competitors is also known as their:

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a. Strategy-making role
b. Networking role
c. Coordination role
*d. None of the above

General Feedback:
References: Chapter 2 page 62, Difficulty: Medium

73. A manager that has transcendent motives of having a strong personal identification with their company and therefore his commitments are characterised by honesty and decency can be referred to as a:

*a. Steward
b. Agent
c. Corporate social responsibility manager
d. Ethical manager

General Feedback:
References: Chapter 2 page 63, Difficulty: Medium

74. The corporate governance mechanisms of each country are shaped by the:

a. Political environment
b. Social environment
c. Economic environment
d. Legal frameworks
*e. All of the above

General Feedback:
References: Chapter 2

Short Answer/Essay Questions

75. Explain why the separation of ownership and management is the root problem of corporate governance?

Correct Answer:
Difficulty: Medium. In modern corporations, there is a division of power, duties and rights between shareholders and managers. Shareholders hold ownership rights (shares) that enable them to participate at the income of the company after all costs. Managers, on the other hand, are contracted to create income, but do often not own significant shares of the company they work for. The lack of ownership diverts managers' interest from those of shareholders. To align the interests of managers and

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shareholders, controlling and monitoring mechanisms are required. However, since single shareholders often lack the resources, expertise and insight into the company's internal practices, the so called agency problem arises.

76. A governing board is considered to be boundary-spanning control unit, which can have some important roles in regulating exchanges of information and resources internally and across organisational boundaries. Describe the four major roles of governing boards?

Correct Answer:
Difficulty: Medium. i) Controlling role: The board acts by ratifying managerial decisions and as a controller in monitoring the implementation and performance of these decisions. The two major vehicles are strategic control and financial control. Strategic control measures the firm's performance against strategic plans while financial control measures the firm against its financial targets.
ii) Strategy-making role: Is the responsibility to formulate corporate-level strategies. The board directors are supposed to use their expertise to advise on strategic decisions and help to build organisational capabilities.
iii) Networking role: Organisations depend on their external environment to build up new resource positions in order to achieve sustainable growth. Directors of a governing board should help their organisations deal with the environment, enhance their legitimacy and assist in achieving their goals of efficiency and performance, and act as a linking instrument of the organisation to the external environment.
iv) Coordinating role: Balancing of often conflicting interests of the various stakeholder groups.

77. Explain how good corporate governance can increase corporate performance?

Correct Answer:
Difficulty: Hard. Good governance, complemented by a sound business environment, enables companies to:
i) Access capital more easily due to increased credibility, thus lower the cost of capital
ii) Strengthen the corporate reputation in the general public, thus raise the trust of consumers and investors.
iii) Increase efficiency of operational activities and minimise risk through controlling managerial decision making.
iv) Enhance long-term sustainability and growth through the recognition of ethics, environmental protection, enhanced social responsibility in employment, protection of communities and social groups from exploitations, and the provision of fair shares of wealth creation at local, society and global levels.

78. One of the important questions regarding corporate governance is how the compensation of executive managers should be controlled. Suggest and explain incentives to align the interest of managers with those of shareholders?

Correct Answer:
Difficulty: Easy. i) Share options: Share options permit managers to purchase, by a certain date, shares at a fixed price. If the share price increases between the date when the option was granted and the date it

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is executed, managers can increase their personal wealth by buying the share at the pre-arranged price and selling at the market price.
ii) Performance-based cash bonus: Any cash reward that is contingent to achieving certain performance criteria. The key is the cautious selection of those criteria to reward the right behaviour. Therefore those criteria should be, of course, pre-established and substantially be market-based.
iii) Performance-based share bonus: Management incentive plans often include shares of the company that can only be sold by the recipient after a specified period of time. Thus, this type of deferred share bonus is a compensation vehicle that encourages managers to take a long-term perspective to the share price of their organisation.

79. Discuss and evaluate a situation where the CEO is also the chairperson of the governing board?

Correct Answer:
Difficulty: Hard. Several studies have shown that CEO/chairperson duality has adverse effects on organisational performance. The negative effects become apparent when considering that in such a duality situation the CEO controls management decisions and the monitoring and controlling function of those decisions. Governing boards are in charge to ensure management decisions are in best interest of shareholders. Therefore, the separation of the two roles is crucial to ensure efficient execution of the governing board's responsibilities.

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