

Session 3a: Post class test solutions

1. **d. All of the above.** If any of the assumptions breaks down, you could take actions that increase stock price but don't increase the value of the business. Thus, you could rip off your bondholders/bank to make stockholders better off, lie to financial markets or have markets misread your results.
2. **c. They are counted as votes for incumbent management.** That makes the system tilt towards incumbents and makes it difficult for you to challenge managers at annual meetings.
3. **b. They tend to go along with incumbent managers and if they are unhappy, they sell their shares.** Institutional investors have neither the stomach nor the resources to involve themselves in fights with managers, partly because they are spread too thin (it is tough to fight battles with 100 companies) or because they have other interests that may be threatened by the activism.
4. **c. The primary mission of the board of directors is to ensure that top managers act in the best interests of stockholders.** They can always play the other roles as well, but they are secondary.
5. **d. Pay "greenmail" to a hostile acquirer.** While any of these actions can sometimes be examples of managerial interests at play, the clearest example is to pay "greenmail" to make a hostile acquirer go away. Since stockholder money funds the greenmail, and the only interests that are served are those of incumbent managers, there is no conceivable rationale that can be offered for paying greenmail. (I know that the anti-takeover amendments come close, but there are two reasons I feel less strongly about them: first, stockholders get to vote on them (they did not on greenmail) and second, value seeking managers can sometimes use anti-takeover amendments to extract higher prices from acquirers for their stockholders.