

**The University of Texas at Austin
McCombs School of Business**

**Managing Corporate Risk
RM 395.1**

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TEXT

- 1 *Risk Management and Insurance* by Scott Harrington and Greg Niehaus, Irwin McGraw Hill Publ. (required).
2. Class handouts (to be provided).

Overview

According to studies in the finance area, risk management activities run about 40% of the payroll of a typical firm, and health care medical benefits alone for employees account for over 25% of cash flow. There are various ways to look at these costs including: (a) are the firm's risk management investments supporting their business strategies in the most cost effective manner, (b) are corporate risk and employee risks being addressed most effectively, (c) how does management of these risks and costs impact global competitiveness. Already many corporations are spending in the six figures (or more) for insurance, which is just a small part of managing the risks faced by corporations. From a corporate perspective, one can expect the cost of risk management to rise even further with increasing corporate responsibility for products liability, employment liability, directors and officers' liability, and health care costs for their employees. For example, the Health Care Finance Administration actuarial studies unit that does statistical work for Medicare projects states that overall health care costs will increase at more than double the rate of inflation for the next five to seven years. General Motors, for example, has an annual \$2.8 Billion liability in health and pension benefits for their retired and active workers, which adds over \$1500 to the cost of each automobile sold. More and more corporations are dropping or freezing their pension plans to save money (IBM, HP, various airlines, and many others).

Congress is now considering bills to allow employees to sue their HMO health providers, which, since costs are borne by the employers, is an additional potential cost and liability for firms. All these issues are of great concern to corporate CEOs and CFO planners, as well as being relevant to individuals becoming informed voters in an election year. Corresponding to these financial and regulatory changes has been a general convergence in the financial intermediary industry and recognition of the enterprise wide nature of risk and its management. The global or integrated management of risk for an enterprise will be the subject of this class.

This course will cover various aspects of risk faced by corporations and the various methods (traditional and non-traditional) available to them for managing these risks. These risks will include managing usual physical risks of property damage and loss, but also include liability costs and management, employee costs and management, and crisis management and communication with the public in times of crisis to mitigate risk to brand value.

EVALUATION

Your final grade will be determined as follows:

<u>COMPONENT</u>	<u>PERCENT</u>
Homework and class participation	20%
Two Examinations worth 30% each	60%
Research Paper	20%

Homework will include a written summary of the guest speakers' presentations as well as assigned homework and group work. The homework assignments will be announced in class in advance and posted to Blackboard. **The first test will be on Monday February 26, 2007 and the second will be April 23. The research paper is tentatively scheduled to be due on April 30.** A brief descriptive presentation will be given by each student on the subject of their own research paper (part of homework/class participation grade) towards the end of the semester. Further information on the research paper, potential topics, and examples of previous "A" papers will be given class. **There will be no final exam.**

Actual letter grades for the course will be determined on the basis of (1) the performance of the student relative to the class, and (2) certain minimum standards.

My Teaching Style:

This course is taught as a combination of lecture and seminar. Readings accompany the course, and internet references will be given at still other times. I would prefer that each class be taught as a discussion, but I will find myself at the computer presenting material and trying to disseminate or reinforce textbook information, especially at first as we are developing the fundamentals and gaining experience in the risk management process and learning how to identify issues. Notwithstanding, I will still encourage discussion. Additionally, much of what you learn in the course will come from the efforts you make in preparing presentations, as well as from what I teach in class. My goal for each class is to make the material interesting enough that you actually *do* want to learn more. Since a discussion is a dialogue, your participation is vital. While I don't expect you to read my mind as to what business articles I use for class

examples, I do expect you to come to class with an understanding of the text reading that is sufficient enough to add cogent comments to anything we end up discussing. Though you may think you could save time by not reading the assignment until after we have discussed the important points in class, I encourage you to read the assignment before class so that you can contribute to a meaningful class discussion. Since your class participation has the potential for influencing my impression of your intelligence and since I assume that you *will* read each assignment beforehand, I would hate to have a misguided class comment wrongly influence my impressions. I will try *not* to put students "on the spot"--of course, reading the material beforehand will help us both save face.

Presentation and Paper:

At the end of the semester you will be required to submit an individual paper (15-20 pages), which will involve a topic in corporate risk and its management. Details are given later in this syllabus and will be discussed further in class.

In addition, you will have group presentations assigned. The presentations will allow you to explore a number a topics and acquire first hand knowledge (in academia, we call this process "research", but it is more sport than work) of the problem of managing risk. Accompanying each presentation will be a report submitted to me and presentation handouts (2 to 5 pages) for class members. But please don't spend \$10 to laminate your report--a single staple will suffice, preferably in the upper left-hand corner.

I reserve the right to grant additional credit for *extraordinary* circumstances.

The first presentation (and submitted paper) is due February 19th. You are to find an interesting court case that deals with a corporate risk management topic. Examples of such interesting cases include those below, but please do look for your own. Another source of interesting very large settlement court cases is <http://www.lawyersusaonline.com/topten2005.cfm>. A google search can yield still others. Make sure that the case you select involves issues of corporate risk (not just personal risk) management. You should analyze the case selected in terms of the corporate risk implications and lessons learned. Discuss how the risk might have been avoided or whether the risk could have been mitigated. You will get more credit for a novel case, or a novel approach to a case.

1. McDonalds being sued because of "excessive" fat content in their food.
2. Pharmaceutical companies being sued for pain reliever medicines.
3. Dow Corning being sued because of unsafe silicone implants.
4. Manville being sued because of asbestos safety concerns.
5. Cigarette companies being sued by state health departments.
6. Gun manufacturing companies being sued for damage or death caused by their product
7. Boards of directors being sued by shareholders because their investment values went down
8. Insurance companies in Mississippi being sued because their contract does not cover flood damage after hurricane Katrina
9. Farmers being sued because a patented gene from a genetically modified organism (GMO) has somehow found its way into their own seed stock, even though they have never used the GMO seed themselves (maybe a seed was carried by a bird, or blew off a passing truck, etc.).

10. GMO food producers being forced to label their food as GMO
11. Mercury amalgams in dental work

We will divide into groups at the beginning of the second week. For the case that you select, discuss in your group how RM topics (discussed in class and found in the readings) relate to the case. Determine which are the most important RM topics and the least important topics, and prepare a paper to submit that reports on your findings. Your research can include references from newspapers, magazines, congressional hearings, academic journals, books, etc., each of which should be duly referenced. As the paper is being finalized, prepare a 10 to 15 minute discussion to deliver in class. I would hate to have one group member's effort be nullified by another's. Consequently, you will have the opportunity to grade the members of your group as to their participation and effort, which will allow the grade to reflect the circumstance of each group member.

Term Paper Description

The term paper will be on a topic of your choice related to issues of concern in managing corporate risk management. The paper topic is not to be merely an "overview" or "encyclopedia" paper, but rather should address some issue of current interest or controversy (e.g. genetic testing use in employment risk management, privatization of social security, discontinuation of corporate pension plans, the role of health care costs paid by US corporations and its impact on the competitiveness of the USA industries, the impact of Sarbanes Oxley on corporate risk, etc). The topic you choose must be given to me for approval by February 27. The paper is due on April 19th.

The paper itself will be ten to 15 pages long with a minimum of eight references. References must include some that are from either academic journals or books, or from reputable newspaper magazines (Newsweek, Time, Business Week, etc.). Internet references are acceptable, but cannot constitute the bulk of your references.

The paper should be written as an academic research paper, with titles, section headings, appropriate paragraphing, an introduction (stating your thesis), and a conclusion section. Margins should be reasonable (1-1.25 inches). Look at articles published in a recent copy of the *Journal of Risk and Insurance* for examples of how to format and write your paper. **You will be graded down if there is inadequate sectioning and paragraphing, or if the English writing or style is inadequate.** This must be a professional paper. I recommend using the University's writing lab for assistance if there is any doubt. Don't wait until the last minute as they do fill up.

Any borrowed ideas, quotes or figures used in the paper must be referenced by authors' last names and year of publication. Any facts, figures or opinions which are not your own must be referenced (and your grade will suffer if you do not reference). For example, "RIDITs represent a very old idea and are closely related to distribution free methods" (Bross 1958, p19). **You will be graded down at least 5 points if you do not adequately cite references used within the text of your paper.**

The references in the reference section of your paper are to be listed alphabetically by the last name of the first author. Examples are given below.

- **Books**

One author:

Koerner, Joseph Leo. 1993. *The Moment of Self-Portraiture in German Renaissance Art*. Chicago: University of Chicago Press.

More than one author:

Cowlshaw, Guy, and Robin Dunbar. 2000. *Primate conservation biology*. Chicago: University of Chicago Press.

Editor(s) or compiler(s):

Panjer, Harry H., eds. 1998. *Financial Economics: With Applications to Investments, Insurance, and Pensions*. Schaumburg, Ill: The Actuarial Foundation.

Company or organization as author:

Blue Cross and Blue Shield of Michigan (BCBSM). 1987. "Participating Hospital Agreement." Detroit: BCBSM. [Citation would read: (BCBSM 1987)]

U.S. Prospective Payment Review Commission (ProPAC). 1991. *Annual Report to Congress*. Washington, DC: U.S. Government Printing Office. [Citation would read: (ProPAC 1991)]

Parts of books (articles in an anthology, chapters, introduction, etc.):

Twaddell, W. Freeman. 1957. A note on Old High German umlaut. In *Readings in linguistics I: The development of descriptive linguistics in America, 1925-56*. 4th ed. Edited by Martin Joos. Chicago: University of Chicago Press.

- **Journals**

Brown, Robert L., Robin Damm, and Ishmael Sharara. 2001. "A Macro-economic Indicator of Age at Retirement," *North American Actuarial Journal* 5(2): 1-10.

- **Magazines and Newspapers**

With an author:

Cynthia Schreiber, "Overture, EarthLink Decline in New-Stock Selloff," *The Wall Street Journal*, 11 July 2003, Money and Investing section.

Without an author:

Euroweek. 1997. "CSFB, Winterthur Storm Swiss CB Sector with First Catastrophe-Linked Bonds," (Jan. 17): 5.

- **Working Papers, Technical Reports, and Ph.D. Dissertations:**

Amundin, M. 1991. Click repetition rate patterns in communicative sounds from the harbour porpoise, *Phocoena phocoena*. Ph.D. diss., Stockholm University.

- **Personal Communications:**

Rich, Colonel William. Interview by author. Tape recording. Boston, Mass., 3 March 2001.

- **Online References (use date citation was found):**

Individual Life Insurance Experience Committee (ILFEC). 2001. "Report of the ILFEC: Mortality Under Standard Individually Underwritten Life Insurance between 1990 and 1991 Anniversaries," *Transactions of the Society of Actuaries*. Online at <http://www.soa.org/research/91ilreport.html>.

Note: When quoting material from another publication, you must include the page number(s) of the quote in the citation (Smith 2001, p. 20).

PAPERS WILL BE TURNED IN CLASS. I am also going to try to make arrangements to have you turn the paper in electronically to "Turn it in dot com", a service which checks for plagiarism. I will give you details on this aspect later.