CHAPTER 1

Law, Value Creation, and Risk Management

TRUE FALSE QUESTIONS

1. Private law provides the legal rules within which firms compete.

   ANSWER: False
   SKILL LEVEL: Analytic
   OBJECTIVE: AIPCA: Legal

2. Managers can make their own "public" law.

   ANSWER: False
   SKILL LEVEL: Analytic
   OBJECTIVE: AICPA: Legal

3. Insurance policies may help firms manage risk.

   ANSWER: True
   SKILL LEVEL: Analytic
   OBJECTIVE: AICPA: Legal

4. Researchers have determined that Fortune 500 firms convicted of illegal conduct earned significantly lower returns on assets than firms that had not been convicted of wrongdoing.

   ANSWER: True
   SKILL LEVEL: Ethics
   OBJECTIVE: AICPA: Legal

5. Lobbying legislators is one method by which managers can help shape the environment in which they do business.

   ANSWER: True
   SKILL LEVEL: Communication
   OBJECTIVE: AICPA: Critical Thinking

6. Laws enacted in response to corporate misdeeds often impose fewer restrictions and costs on business than would have been imposed had firms as a whole acted more responsibly at the outset.

   ANSWER: False
   SKILL LEVEL: Analytic
   OBJECTIVE: AICPA: Legal

7. Promoting economic growth is one of the primary public policy objectives of laws and regulations applicable to business.

   ANSWER: True

SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

8. Worker protection is one major public policy concern underlying U.S. business law.

ANSWER: True
SKILL LEVEL: Ethics
OBJECTIVE: AICPA: Critical Thinking

9. Researchers found a statistically significant inverse relationship between a country's economic prosperity, as measured by the per capita gross domestic product, and the country's judicial independence.

ANSWER: False
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

10. As used in the text, the term "legal astuteness" refers to the ability of a manager to avoid situations making consultation with legal counsel necessary.

ANSWER: False
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

11. The entering into of nondisclosure agreements is an unethical practice that should not be tolerated by a legally astute manager.

ANSWER: False
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

12. A legally astute manager would wait as long as possible to consult legal counsel once a problem arises in order to keep legal fees to a minimum.

ANSWER: False
SKILL LEVEL: Communication
OBJECTIVE: AICPA: Critical Thinking

13. A legally astute manager understands that legal analysis is often ambiguous.

ANSWER: True
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

14. Each activity in regard to "law and the value chain" referenced in the text has legal aspects.

ANSWER: True
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

15. The European Union's center of operations is in Brussels, Belgium.

ANSWER: True
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

16. Under the resource-based view of a business firm, a firm's resources can be a source of sustained competitive advantage if they are valuable, rare, and perfectly imitable by competitors.

ANSWER: False
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

17. Self-regulation within the advertising industry has been largely successful in reducing the number of fast-food commercials directed at children.

ANSWER: False
SKILL LEVEL: Ethics
OBJECTIVE: AICPA: Legal

18. Law is dynamic as opposed to static

ANSWER: True
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

19. The Election Act of China gives businesspeople the right to be elected as congresspersons.

ANSWER: True
SKILL LEVEL: Diversity
OBJECTIVE: AICPA: Legal

20. The protection of private property rights is one way to promote economic growth within a society.

ANSWER: True
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

MULTIPLE CHOICE QUESTIONS

1. Which of the following is <u>not</u> one of the four primary public policy objectives furthered by laws and regulations applicable to U.S. business?
A. Promoting economic growth
B. Protecting workers
C. Promoting consumer welfare
D. Promoting governmental regulation
E. Promoting public welfare

ANSWER: D
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

2. Managers can make their own ______ law by entering into contracts and crafting certain governance structures.
A. Public
B. Primary
C. Cohesive
D. Private

ANSWER: D
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

3. The ______ approach recognizes that “business decisions consist of continuous, interrelated economic and moral components.”
A. Procedural
B. Systems
C. Conciliatory
D. Mandated

ANSWER: B
SKILL LEVEL: Ethics
OBJECTIVE: AICPA: Legal

4. Which of the following is a theory that recognizes that firms have relationships with many constituent groups which both affect and are affected by the actions of the firm?
A. Stakeholder
B. Stockholder
C. Relational
D. Cohesive

ANSWER: A
SKILL LEVEL: Ethics
OBJECTIVE: AICPA: Legal

5. Which of the following was enacted after widespread abuses in the subprime mortgage market?
A. The Walsh-Healy Mortgage Reformation and Consumer Protection Act of 2009
B. The Mortgage Lending and Financial Reform Act of 2009
C. The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
D. The Financial Institution Regulatory Pronouncement and Consumer Revision Act of 2010

ANSWER: C
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

6. Which of the following is true regarding legally astute management teams practicing strategic compliance management?
A. The cost of complying with government regulation is viewed as an investment, not an expense.
B. The cost of complying with government regulation is viewed as an expense which should be avoided until legal action is threatened.
C. Only the minimum necessary to comply with any applicable law should be done.

D. Both that the cost of complying with government regulation is viewed as an expense which should be avoided until legal action is threatened and that only the minimum necessary to comply with any applicable law should be done.

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

7. Through which of the following can managers help shape the legal environment in which they do business?
A. By lobbying legislators
B. By forming coalitions
C. By refusing to follow laws viewed as unneeded by company officials
D. By lobbying legislators and by forming coalitions, but not by refusing to follow laws viewed as unneeded by company officials

ANSWER: D
SKILL LEVEL: Ethics
OBJECTIVE: AICPA: Legal

8. Which of the following is a type of law referencing formal rules embodied in constitutions and statutes enacted by legislatures?
A. Public
B. Private
C. Substantive
D. Remedial

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

9. Which of the following is a type of law referencing formal rules embodied in judicial decisions rendered by courts?
A. Public
B. Private
C. Substantive
D. Remedial

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

10. Which of the following is NOT a way in which U.S. law protects workers?
A. Through regulating certain terms and conditions of employment
B. Through requiring the employer to provide certain benefits
C. Through protecting civil rights in the workplace
D. Through requiring the provision of educational opportunities to workers

ANSWER: D
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

11. Which of the following is an advocacy group that has lobbied against marketing to children?
A. The Alliance to Ban Advertising Targeting Children
B. The Protect the Children Foundation
C. The Center for Science in the Public Interest
D. The Group for Ethical Marketing Practices

ANSWER: C
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

12. Which of the following is true regarding a comparison of the law of the United States and the law of the European Union?
A. Laws of the United States and the European Union differ in regard to consumer privacy and emissions standards but are similar in regard to chemical usage and accounting standards.
B. Laws of the United States and the European Union differ in regard to consumer privacy, emissions standards, and chemical usage but are similar in regard to accounting standards.
C. Laws of the United States and the European Union differ in regard to consumer privacy, emissions standards, chemical usage, and accounting standards.
D. Laws of the United States and the European Union are similar in all significant areas involving business regulation and vary in only minor respects

ANSWER: C
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

13. Which of the following is true regarding typical requirements placed on employers mandating the provision of employee benefits?
A. Employers are typically required to provide workers' compensation, to pay unemployment insurance, and to pay social security and Medicare taxes.
B. Employers are typically required to pay unemployment insurance and to pay social security and Medicare taxes, but employers are not required to pay workers' compensation insurance.
C. Employers are typically required to pay workers' compensation insurance and to pay social security and Medicare taxes, but employers are not required to pay unemployment insurance.
D. Employers are typically required to provide workers' compensation and to pay unemployment insurance, but employers are not required to pay social security and Medicare taxes.

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

14. U.S. business law promotes consumer welfare through which of the following?
A. By encouraging the sale of safe products at a fair price
B. By preventing deceptive practices
C. By refusing to recognize consumer privacy
D. By encouraging the sale of safe products at a fair price and by preventing deceptive practices, but not by refusing to recognize consumer privacy

ANSWER: D
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

15. The "systems approach" to business and society builds on which of the following stakeholder theory insights?
A. That firms have relationships with many constituent groups, which both affect and are affected by the actions of the firm.
B. That firms have relationships with many constituent groups, and that these groups must be managed to best promote value to stockholders.
C. That although firms have relationships with many constituent groups, these groups have little impact on the ongoing management of business firms.
D. That firms have relationships with only a few groups, such as employees, that are directly connected with business operations.

ANSWER: A
SKILL LEVEL: Ethics
OBJECTIVE: AICPA: Critical Thinking

16. Which of the following is a term addressing the ability of a manager to communicate effectively with counsel and to work together to solve complex problems?
A. Legal astuteness
B. Conciliatory interaction
C. Mediation
D. Arbitration

ANSWER: A
SKILL LEVEL: Communication
OBJECTIVE: AICPA: Legal

17. Which of the following has the responsibility for deciding which allocation of resources and rewards in a business makes the most business sense?
A. The general manager
B. The in-house lawyer
C. An independently retained lawyer
D. An independently retained law firm, not just one lawyer

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

18. Which of the following is <u>not</u> a component of legal astuteness as referenced in the text?
A. A set of value-laden attitudes about the importance of law to the firm's success
B. A practice of leaving the resolution of legal issues to outside counsel
C. The ability to exercise informed judgment when managing the legal aspects of business
D. Context-specific knowledge of the law and the appropriate use of legal tools

ANSWER: B
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

19. Which of the following is listed in the text as a component of managing risk when assembling a team in business development?
A. Analyzing any covenants not to compete

B. Purposefully refusing to address issues such as sexual harassment
C. Informing employees that e-mail communications are not discoverable
D. Ignoring whistleblower protection

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

20. The ______ approach to business and society introduced in the text is a descriptive framework that integrates legal and societal considerations with mainstream theories of competitive advantage and social responsibility.
A. Integrative
B. Systems
C. Proactive
D. Economic

ANSWER: B
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

21. Which of the following is true regarding laws and practices of the European Union and its members?
A. European antitrust regulators are often more sympathetic to competitors than are U.S. authorities.
B. European antitrust regulators lack the authority to block mergers.
C. European antitrust regulators have the authority to block only foreign mergers, not mergers of companies located within the European Union.
D. It is expected that the impact of the European Union on corporate planning and strategy will become less, not more, evident in the future.

ANSWER: A
SKILL LEVEL: Diversity
OBJECTIVE: AICPA: Legal

22. Which of the following is a type of relationship building lobbying prevalent in China?
A. Xantu
B. Olaying
C. Guanxi
D. Quinta

ANSWER: C
SKILL LEVEL: Diversity
OBJECTIVE: AICPA: Legal

23. Which of the following is true regarding the criminal law in China?
A. It prohibits businesses from paying bribes to government officials, but a payment of money is not considered a bribe unless the amount is significant.
B. It prohibits businesses from paying any bribes to government officials, regardless of amount.
C. It allows the payment of bribes in any amount to government officials.
D. It allows solvent business to pay bribes in any amount to government officials, but prohibits the payment of bribes by insolvent businesses.

ANSWER: A

SKILL LEVEL: Diversity
OBJECTIVE: AICPA: Legal

24. Which of the following is a Chinese law applying to corporate political activities in China?
A. The Election Act of China
B. The Criminal Law of China
C. The Lobbying Law of China
D. The Election Act of China and the Criminal Law of China, but not the Lobbying Law of China

ANSWER: D
SKILL LEVEL: Diversity
OBJECTIVE: AICPA: Legal

25. As the public has become more concerned about childhood obesity, which of the following is a government agency referenced in the text that is considering a ban on certain types of children's advertising?
A. The American Consumer Agency
B. The Federal Communications Commission
C. The Federal Trade Commission
D. The Federal-State Advertising Coalition

ANSWER: B
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

26. Congress rescinded the jurisdiction of which of the following agencies over advertising to children?
A. The American Consumer Agency
B. The Federal Communications Commission
C. The Federal Trade Commission
D. The Federal-State Advertising Coalition

ANSWER: C
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

27. Which of the following was created by food advertisers in an attempt to halt government regulation aimed at stopping marketing preying on children's vulnerability?

A. The Children's Advertising Review Unit
B. The Minor's Board Unit
C. The Minor Protection Review Unit
D. The Children's Enhancement Board

ANSWER: A
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

Fact Pattern 1-1 (questions 28-31 apply)

Susan, the CEO of ABC Company, which was involved in the production and sale of hair care products, decided to hire new employees to develop new product lines for a planned expansion into the dog shampoo arena. She was concerned, however, that the employees specializing in canine products might leave at some point, taking company secrets with them for use in competition with ABC. She, therefore, required that the employees sign contracts containing covenants not to compete. Susan also consulted her in-house counsel, Sam, regarding the effect of some new regulations involving the use of certain chemicals in shampoo and conditioner. Sam told her, however, to ignore the regulations until some type of investigation of the company was started. Sam says that more than likely no one will ever check to see whether or not ABC is in compliance. Susan disagrees with his advice and decides to seek other counsel.

28. Refer to fact pattern 1-1. The covenants not to compete involved which of the following types of law?
A. Public
B. Private
C. Circumscribed
D. Tangent

ANSWER: B
SKILL LEVEL: Reflective Thinking
OBJECTIVE: AICPA: Critical Thinking

29. Refer to fact pattern 1-1. The use of covenants not to compete involves which of the following forces identified by Michael Porter and referenced in the text?
A. Supplier power
B. Threat of entry
C. Substitution
D. Buyer power

ANSWER: C
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

30. Refer to fact pattern 1-1. The government regulations pertaining to the use of certain chemicals involved which of the following types of law?
A. Public
B. Private
C. Circumscribed
D. Tangent

ANSWER: A
SKILL LEVEL: Reflective Thinking
OBJECTIVE: AICPA: Critical Thinking

31. Refer to fact pattern 1-1. Assuming that Susan seeks to be a legally astute manager, which of the following is true regarding the advice given by Sam to ignore the regulations pending an investigation?
A. Sam is correct that it is unlikely that any investigation will ever occur and that the regulations may be safely ignored.
B. Sam is correct only if ABC has not had past investigations because if past investigations have occurred, it is more likely that the company will be the target of future investigations.
C. Sam is incorrect but only because safety regulations are concerned.
D. Sam is incorrect because a legally astute manager will take a proactive approach to regulations.

ANSWER: D
SKILL LEVEL: Reflective Thinking
OBJECTIVE: AICPA: Critical Thinking

32. Molly, the CEO of a corporation owning a number of pet stores, calls you for advice. She tells you that she received inside information that the stock of the company was going to go down because of reports that a number of dogs sold by the store had become ill and that she, therefore, immediately sold all her stock in the company before the information became public. She tells you that she has been advised that she is going to be charged with a securities violation involving insider trading. Which of the following is true regarding her situation?

A. Corporate executives may be fined but may not be sent to jail.
B. Corporate executives may be sent to jail, but only for offenses endangering others.
C. Corporate executives may be sent to jail, but only for fraud involving banks.
D. Corporate executives may be sent to jail for violation of criminal laws.

ANSWER: D
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

33. Which of the following was the result in *Sorrell v. IMS Health Inc.*, the case in the text in which drug manufacturers challenged as unconstitutional a Vermont statute prohibiting pharmacies form selling prescriber-identifying information for marketing prescription drugs without the consent of prescribers?

A. That although speech promoting marketing was not protected by the First Amendment, the law was unconstitutional based on the due process clause.
B. That the statute regulated commercial speech which was evaluated under an “intermediate” standard and that the law was, therefore, constitutional.
C. That the statute did not involve constitutional issues and was, therefore, a permissible type of regulation.
D. That the conduct prohibited by the law was protected by the First Amendment and that the law was unconstitutional.
ANSWER: D
SKILL LEVEL: Reflective Thinking
OBJECTIVE: AICPA: Critical Thinking

ESSAY QUESTIONS

1. Under the resource-based view of a firm, when can a firm’s resources be a source of sustained competitive advantage?

ANSWER: When they are valuable, rare, and imperfectly imitable by competitors and have no strategically equivalent substitutes.
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Critical Thinking

2. What are the four ways referenced in the text by which U.S. law promotes public welfare?

ANSWER: By promoting effective administration of justice, by collecting taxes and spending money, by protecting fundamental rights, and by protecting the environment.
SKILL LEVEL: Analytic
OBJECTIVE: AICPA: Legal

3. Assume that after paying a large fine, a company survives charges of illegal activity. In what ways does illegal conduct put a company at a competitive disadvantage?

   ANSWER: Illegal conduct can put a firm at a competitive disadvantage by diverting funds from strategic investments, tarnishing the firm's image with customers and other stakeholders, raising capital costs, and reducing sales volume.
   SKILL LEVEL: Reflective Thinking
   OBJECTIVE: AICPA: Critical Thinking

4. Discuss ways in which laws and regulations promote economic growth.

   ANSWER: Laws and regulations promote economic growth by protecting private property rights; enforcing private agreements; allocating risks; facilitating the raising of capital; creating incentives to innovate; promoting liquid and skilled labor markets; providing subsidies, tax incentives, and infrastructure; and promoting free trade in global markets.
   SKILL LEVEL: Reflective Thinking
   OBJECTIVE: AICPA: Critical Thinking

5. How does U.S. business law provide worker protection?

   ANSWER: By regulating certain terms and conditions of employment, by requiring the employer to provide certain benefits, and by protecting workers' civil rights.
   SKILL LEVEL: Reflective Thinking
   OBJECTIVE: AICPA: Critical Thinking