**CORPORATE FINANCE**

**Learning Outcome 1: ACTIVITY 6**

**The agency problem**

For larger businesses, there is often a separation between the owners or shareholders (the principals) and the managers (the agents). An agency problem can occur when the managers of a business make decisions that are not consistent with the primary objective.

#### Required: In small groups

Using your chosen business from previous Activities, where relevant:

1. Identify the three factors that contribute to the existence of the agency problem in most businesses.
2. Explain the factors that might contribute to the agency problem in your chosen business.
3. Discuss the effects of the agency problem in your chosen business.
4. Discuss the agency problem that is particular importance to financial management.
5. Explain how restrictive covenants might be used to address the problem that you identified in (4).
6. Prepare a short presentation on your findings.