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TEACHING BUSINESS ORGANIZATIONS FROM A TRANSACTIONAL PERSPECTIVE

WILLIAM K. SJOSTROM, JR.*

INTRODUCTION

Many lawyers have transactional, as opposed to litigation, practices. Instead of working on cases, transactional lawyers, also called corporate lawyers, work on transactions, or deals—mergers and acquisitions, public and private securities offerings, venture capital financings, business start-ups, etc. A corporate lawyer advises the client as to the best way to structure a deal, negotiates the legal terms of the deal, and drafts or reviews the contract(s) to document the deal.¹

Notwithstanding the fact that a plethora of legal work is transactional in nature, most doctrinal law school courses are litigation bent, even if the course's subject matter comes up routinely in deals. For example, every deal involves a contract, yet very little, if any, time is spent in first year contracts courses on how or what aspects of a deal should be reflected in a written agreement. Instead, the focus is on reading and discussing judicial opinions, a valuable endeavor but implicitly litigation oriented.

Business Organizations is typically taught the same way as contracts—but not by me. I, instead, teach the course from a transactional perspective largely, because I view Business Organizations as the foundational course for corporate lawyers. Thus, I want to impart on my students, many of whom will be transactional lawyers in one form or another, a strong transactional law

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1. The American Association of Law Schools Section on Transactional Law and Skills defines transactional lawyering in line with me as follows:

Transactional lawyering is a distinctive form of legal practice that focuses on the creation of “a law of the deal” rather than on the interpretation of legal texts, or the litigation and resolution of disputes. This sort of lawyering—often called “private ordering”—depends on the parties (not the government or the courts) to create the rules that will govern their relationship.

ASS'N AM. LAW SCH., PETITION FOR PROVISIONAL STATUS: PROPOSED SECTION ON TRANSACTIONAL LAW AND SKILLS (2011), *available at* <http://entrepreneurs.typepad.com/files/aalspetition-1.doc>.

foundation for them to build upon in advanced business law classes and in their legal careers. Below I describe my approach.

I. COURSE OBJECTIVES

My primary course objectives are as follows:

1. Teach students the basics of business organizations law.
2. Teach students the business concepts necessary for them to understand the business organizations law covered in the course.
3. Expose students to the business organization documents and provisions they will see in practice.
4. Teach students how to read and apply language from statutes, organizational documents, and contractual provisions.
5. Introduce students to the planning and problem-solving involved in a corporate law practice.

The above objectives are not radically different from those of most law school courses. Notice, however, that case analysis is not included in the list. We do perform some case analysis in my course, but it is not a primary objective. This is largely because case analysis is rarely required in transactional practice. Further, in my opinion, students do more than enough case analysis in other courses.

Objectives Four and Five are where my course departs the most from a traditional Business Organizations course. These objective are the keys to making my course transaction-oriented because reading and applying language from statutes, organizational documents, and contracts is something that corporate lawyers are called on to do daily. Similarly, planning and problem-solving are at the heart of a transactional practice.

I pursue Objective Four by having students work through numerous exercises requiring them to analyze contractual or organizational document language in light of statutory provisions and apply this language in various situations encountered by corporate lawyers. Many of these exercises involve reviewing a complete document, such as an LLC operating agreement, and answering questions regarding it. As a result, students learn how various provisions covered in the course fit together in a single document.

Students get a chance to work through the following documents/provisions in my course:

- Limited liability partnership agreement
- Limited partnership agreement
- Limited liability company agreement
- Articles of incorporation
- By-laws

- Certificate of designation
- Loan agreement representations and warranties and covenants
- Warrant agreement
- Indemnification agreement
- Shareholders' agreement
- Proxy statement

I pursue Objective Five by having students do exercises that require transaction-oriented planning and problem-solving. Here's an example:

Amin, Basu, and Cano are planning to open a flight training school in Tucson, Arizona, which they will own equally. Amin is the instructor and will largely run the operation. Amin intends to provide all his time, but no initial cash, to the venture. Amin's incentive is to use the flight time he accumulates to qualify for a commercial pilot's license. Basu is the technical engineer whose function will be to provide all the necessary aircraft maintenance. Basu intends to work only part time as she is currently taking classes at the University of Arizona. Both Amin and Basu will receive a salary. Cano will be a passive investor in the venture and does not intend to participate in the management or day-to-day operations unless things do not go well.

Cano is a very wealthy individual and, accordingly, has substantial passive income that she would like to eliminate or reduce with passive losses. Consequently, Cano has agreed to provide all funds necessary to purchase the aircraft and to defray the working capital needs of this venture provided that all losses generated by this venture be specially allocated to her. Additionally, Cano requires that no funds be distributed to Amin or Basu until she has recouped all of the money she has invested in the venture.

Under which legal form should the business operate?

This exercise requires students to identify and understand the objectives of each owner, to consider which legal forms meet all or some of these objectives, to formulate a recommendation, and to explain and defend the recommendation.

II. THE BOOK

Historically, a major impediment to teaching Business Organizations from a transactional perspective was the lack of a book designed for this purpose. I did not let this stop me, but it was always somewhat of a struggle. All of the books on the market seemed to be designed for the case method of teaching. Thus, they have lots of cases, but very few, if any, transactional documents or provisions. I remedied the situation by supplementing my chosen book with transactional documents, transactional provisions, and related exercises. The problem was that, since the book was composed mostly of cases, students had to spend a lot of preparation time reading cases, and I, in turn, had to spend a lot of class time discussing cases, leaving little time for working exercises.

Furthermore, invariably, the book lacked a critical concept or explanation for a transactional exercise that I wanted the students to do, forcing me to oversimplify the exercise.

After switching books frequently over my first eight years of teaching Business Organizations in search of the perfect book (I tried five different books in that timeframe), I gave up and decided to write my own. My book, *Business Organizations: A Transactional Approach*, was published by Aspen in 2013.² It is, of course, designed specifically for teaching Business Organizations from a transactional perspective.

The book's key attributes are as follows:

- *Content selected through a corporate lawyer lens*: I was a corporate lawyer for many years before entering the academy, both at a law firm and in-house, and have drawn on this experience in selecting the book's content and topic depth. The book covers the business organizations law that every budding corporate lawyer should know.

- *Emphasis on real-world provisions*: The book is loaded with actual provisions from various documents corporate lawyers draft and review so that students get to see how the covered legal concepts are documented. The provisions also give students a sense of what corporate lawyers do in practice. In addition to the documents mentioned above, my book also includes board and shareholder resolutions, board and shareholder written consents, meeting notices, legal opinion provisions, specialized organizational document provisions, charter amendments, and a promissory note, among other things.

- *Teaching through exercises*: The book includes numerous exercises, all of which require students to apply what they have learned from the readings. The exercises are designed to reinforce the covered material and help students develop the planning and problem-solving skills of a corporate lawyer, as well as expose students to the documents and issues at the heart of a transactional practice.

- *More narrative, fewer cases*: I cover many legal concepts through concise explanatory text instead of judicial opinions. This enables me to keep the book a manageable size while providing more depth in areas central to a corporate law practice. It also frees up student preparation and class time for focusing on the exercises instead of case crunching. Each case is followed by a series of straightforward questions to get students to zero in on the key aspects of the case, leading to efficient class discussion. Additionally, unlike most casebooks, the book does not include "notes." Instead, I have integrated the note-type material into the text, which enhances readability by making the book flow better.

2. WILLIAM K. SJOSTROM, JR., *BUSINESS ORGANIZATIONS: A TRANSACTIONAL APPROACH* (2013). The remainder of this Article discusses the different approaches and sections found in this book.

The book is divided into three parts: Prefatory Matters (Part I), Unincorporated Entities (Part II), and Corporations (Part III). Prefatory Matters is comprised of a chapter introducing the various business forms, a chapter on agency law, and a chapter on entity selection. Unlike many Business Organizations books, I did not start with agency law because I wanted to be able to discuss agency law in the context of the various entities. This necessitated introducing the entities first. Hence, Chapter One introduces the fundamental characteristics of the six most common business forms (sole proprietorship, partnership, limited liability partnership, limited partnership, corporation, and limited liability company). Most of the topics covered in the chapter are revisited in more depth later in the book.

Chapter Two covers agency law. The chapter is admittedly incomplete given that there is an entire Restatement devoted to the topic. In line with the theme of the book, the chapter focuses on what I consider the quintessential agency law issue for a corporate lawyer—when is a business bound on a contract with a third party that someone entered into on the business’s behalf? The chapter looks at this issue under the common law of agency and entity specific statutory rules. It also introduces students to legal opinions and secretary’s certificates.

Chapter Three addresses considerations that drive a business’s choice of legal form under which to operate. I view form, or entity, selection as a core competency of a corporate lawyer. Thus, I cover the topic in a fair amount of detail including special allocations, potential employment tax savings for Subchapter S businesses, the possibility of an LLC electing to be taxed under Subchapter S, charging order protection afforded by unincorporated entities, and venture capitalists’ preference for investing in C corporations. I like doing the chapter towards the beginning of the semester because it grabs students’ attention by demystifying the alphabet soup of business forms and really hits home with students who have started or are contemplating starting a business. As you likely surmised, the flight training school fact pattern from above appears in this chapter.

Part II on unincorporated entities starts with Chapter Four, which covers partnerships and limited liability partnerships. The chapter focuses on the Revised Uniform Partnership Act (RUPA), given 37 states base their partnership statutes on it. The chapter includes a series of exercises requiring students to analyze a limited liability partnership agreement included at the end of the chapter. Exercises involving review of a full organizational document, such as a LLP agreement, is an important feature of my book because, in practice, advising a business on a multitude of issues starts with a review of its organizational documents. Thus, I want students to have experience analyzing these documents, including how the documents interact with the relevant statute.

Chapter Five covers limited partnerships and limited liability partnerships. The chapter includes a venture capital fund limited partnership agreement and related exercises. This agreement is more complicated than the LLP agreement from Chapter Four so that students are exposed to agreements of differing complexity. I chose a venture capital LP agreement because investment funds comprise the principal area where the limited partnership form is still used. Doing so also has the added benefit of introducing students to VC funds, a prominent source of corporate law work.

Chapter Six covers limited liability companies. The chapter focuses on the Delaware Limited Liability Company Act (DLLCA) for two reasons. First, Delaware attracts the most LLCs formed outside of their home states,³ and second, the Uniform Limited Liability Company Act has not been widely adopted.⁴ Thus, I concluded that it is more beneficial for students to study the DLLCA because they are likely to run into Delaware LLCs in practice. Similar to the other Part II chapters, Chapter Six includes a complete LLC agreement and related exercises.

Part III is devoted to corporations. As I explain to students, the book covers corporations in much more depth than the other entities by design. Specifically, I use the corporate form to do the “heavy lifting,” in part because corporate law is the most developed category of business entity law. I explain that there is a lot of overlap in legal concepts between corporations and unincorporated entities. Given time constraints and to avoid boring students by seemingly repeating the same material numerous times, there are a number of concepts that the book covers only in the corporate form, although they apply with equal force to unincorporated forms. Basically, I assume that the students are smart enough to apply what they learn in the corporate context to the unincorporated context, if need be, in the future.

Chapter Seven gets into the nuts and bolts of incorporating a business. While this material is unsexy, I view it as another corporate lawyer core competency, and thus, I cover incorporation in a fair amount of detail. Hence, the chapter includes many sample incorporation documents. The chapter also contains one of my favorite exercises—a poorly drafted articles of incorporation that students have to pick apart. This exercise is the most salient example of two techniques I use in a number of exercises—including poorly drafted or statutorily prohibited provisions in a document and omitting from a

3. Jens Dammann & Matthias Schündeln, *Where Are Limited Liability Companies Formed? An Empirical Analysis*, 55 J.L. & ECON. 741, 745–46 (2012) (finding that 54.44% of out-of-state LLC formations in sample were done in Delaware).

4. See *Legislative Fact Sheet—Limited Liability Company*, UNIF. LAW COMM’N, <http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Limited%20Liability%20Company%20> (last visited Oct. 31, 2014) (noting that the revised Uniform Limited Liability Company Act has been enacted by twelve states).

document statutorily required or otherwise important provisions. I do this to get students to more carefully scrutinize documents and the relevant statutes and to reinforce statutory rules.

Chapter Eight is a lengthy chapter on corporate finance—the bread and butter of many corporate practices. One of my goals for this chapter is to give students a sense for what corporate lawyers actually do. Thus, the chapter includes two “lawyer role” sections that describe, in a fair amount of detail, the roles corporate lawyers play on a commercial loan deal and an angel financing deal. The chapter also contains the most challenging exercise in the book—applying the language of a preferred stock certificate of designation.

Chapter Nine is another nuts and bolts chapter covering the statutory rules for shareholder meetings and voting as well as board action and elections. Students get to work with a complete set of articles of incorporation and by-laws included at the end of the chapter as part of some exercises.

Chapter Ten is the most traditional chapter of the book in that it contains numerous cases. This is because the chapter covers corporate fiduciary duties, which are mostly judge-made under Delaware law. The chapter includes the iconic cases *Smith v. Van Gorkom*⁵ and *In re Caremark International Inc. Derivative Litigation*⁶ as well as some more recent Delaware fiduciary duty opinions. Students work exercises applying Delaware fiduciary duty common law and then rework the same exercises later in the chapter applying MBCA fiduciary duty provisions. The MBCA exercises are complicated because the relevant provisions span three different MBCA chapters (1, 2, and 8) and use numerous terms with lengthy definitions. As a result, the exercises provide a good gauge for students of how far they have progressed during the course in analyzing and applying statutory language.

Chapter Eleven is a short chapter covering return on investment. It delves into distributions, including statutory restrictions on a corporation’s ability to make them. It also introduces students to federal securities law restrictions on the transfer of private company shares.

Chapter Twelve addresses minority shareholder protections. It includes the most practice-like exercise in the book—one where, on behalf of a majority shareholder, students review and comment on a shareholders’ agreement proposed by a potential minority investor. By this point in the book, students have hopefully developed the skills to flag problematic provisions and omissions and suggest changes.

Chapter Thirteen covers public company regulation. Topics include disclosure requirements, proxy rules, Rule 10b-5, and the prohibition on insider trading. I believe it is less confusing for students to collect these topics in a single chapter instead of interspersing them throughout the book, as many

5. *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985).

6. *In re Caremark International Inc. Deriv. Lit.*, 698 A.2d. 959 (Del. Ch. 1996).

Business Organizations books do. The chapter includes exercises requiring students to search the SEC's website to review and answer questions about Facebook's latest Form 8-K and Apple's latest proxy statement.

Chapter Fourteen, provides an overview of mergers and acquisitions. My main goal with this chapter is to teach students the basic ways in which an acquisition can be structured and the primary considerations that drive the choice of structure. The chapter also covers some of the sexier hostile takeover related cases (*Unocal* and *Revlon*) and issues.

The book closes with an appendix that introduces students to financial statements. I put it here to give professors flexibility as to when, or if, to cover these basic accounting-related materials. I cover the Appendix before Chapter Eight because students will have an easier time with the corporate finance materials of that chapter if they know some basic accounting.

III. A TYPICAL CLASS

I begin a typical class by projecting the portion of the syllabus on the screen corresponding to the reading assignment. I then give a quick overview of what we are going to cover and how it fits in with what we covered in the previous class. My main goal here is to provide context and help students see the big picture. Next, I lecture on what I view as the more important points from the assigned readings assisted by PowerPoint slides.

If the assignment includes a case, after briefly describing why we are looking at it, I call on a student to give a quick overview of the facts and then engage him or her in a discussion about the case. As mentioned above, each case in my book is followed by a set of mostly straightforward questions. The questions are generally designed to serve as a guide to students while reading the case. Thus, I do not cover all these questions in class, usually just the trickier ones.

Most reading assignments include one or more exercises. The exercises are the heart of the book. I use a group approach for these. Specifically, I divide the class into groups of four or five students and assign each group a number. I then give the class roughly three minutes (sometimes more, sometimes less, depending on the complexity of the exercise) to caucus. My expectation is that students will have worked through the assigned exercises as part of preparing for class. Thus, the caucus is just for them to compare notes and decide who will be the spokesperson if I call on their group. I then use an online random sequence generator to choose which group to call on to discuss the exercise.⁷ If the exercise involves applying statutory, organizational document, or other language (as most of them do), I often project the relevant language on the

7. *Random Sequence Generator*, RANDOM.ORG, <http://www.random.org/sequences/> (last visited Oct. 31, 2014).

screen (I do this by taking an exact PDF snapshot from the book and pasting it into a PowerPoint slide). For more difficult exercises, I post sample answers after class to make sure everyone is on the same page, which I may review in the next class depending on my read of the class's grasp of a particular exercise.

Doing this group approach uses substantial class time, so I do not use it for all exercises. Sometimes, I just ask for volunteers or go over the exercise myself. For that matter, I do not cover all exercises in class. Some I view as less important and others I simply run out of time because class discussion is going well and I do not want to squelch it. I post answers to exercises not covered in class on the class website.

IV. FINAL THOUGHTS

I do cover litigation-oriented topics in my book and course (derivative litigation, for example), and, as indicated above, we do discuss cases (the book includes thirty-one cases). Certainly a corporate lawyer needs to know the basics of business entity litigation so that, among other things, he or she can help a client avoid litigation, and students get this in my course, notwithstanding its transactional focus.

As for students who are concerned about the focus of my course because they want to be litigators or otherwise have no interest in practicing corporate law, I tell them the following:

1. The provisions and documents students will learn about in my course are often at the center of business organization related disputes. Thus, familiarity with them, as well as the planning behind them, is invaluable to a business litigator.
2. The book covers most, if not all, of the Business Organizations topics tested on the bar exam. Thus, students should have no worries on that front.
3. The book will give students a good sense of what corporate practice is all about and may inspire them to become corporate lawyers after all.

Even though contract drafting is a critical skill for a corporate lawyer, I do not cover it in my course beyond pointing out drafting errors in some of the book's documents and throwing out a drafting tip from time to time. Given the breadth of substantive material I need to cover, there simply is not time. Fortunately, at my law school, students learn some contract drafting basics in their first year legal writing course,⁸ and we also offer an upper-level contract drafting course. Thus, it is not critical for me to cover contract drafting in Business Organizations.

8. Our legal writing program uses a different book I wrote to teach the subject, WILLIAM K. SJOSTROM, JR., *AN INTRODUCTION TO CONTRACT DRAFTING* (2d ed. 2013).

CONCLUSION

I teach Business Organizations from a transactional perspective because it is the foundational course for corporate lawyers. Many students end up as corporate lawyers, and most other doctrinal law school courses are taught from a litigation perspective. My overarching goal is for students to leave my course with a strong transactional law foundation. My book is designed with this goal in mind.