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What I Do When I Teach Business Associations, What Do I Do, Teach Business Associations, Teach, Business, Associations

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WHAT I DO WHEN I TEACH BUSINESS ASSOCIATIONS

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INTRODUCTION

For the last decade or so I have been teaching three different groups of students—American candidates for the J.D. degree, American candidates for the MBA degree (from the Kellogg School of Management at Northwestern University), and foreign lawyers who come to our law school for the LL.M. degree. These three groups of candidates have different experiences and different affinities for the law. The J.D. students know that some grounding in the law of business associations is indispensible to them, the Kellogg students have figured out that they cannot really attain C-suite status without some knowledge of the legal and regulatory environment in which they must move, and the LL.M. students have come to America to learn why we are, more or less, the leaders in business law. Because the LL.M. students are generally lawyers with several years of experience in their home countries, they are initially a bit skeptical that there is anything they can learn in a business law course that is comprised of law students who have never practiced and Kellogg students who have no legal training. In the past few years, this Business Associations course of mine, which we call "Corporations" in the law school and "Business Law" in the Kellogg class listing, is comprised of a roughly equal number of students in each of the three categories. In the first few sessions of what is a ten-session course (most sessions are comprised of two segments of one and one-quarter hours with a fifteen minute break in between the segments), the three student groups are rather wary of one another, and seem to be circling and sniffing one another out in the same manner as do unfamiliar dogs. By the middle of the course, though, after I have had them do some in-class projects together, they come to respect one another's particular experiences and accumulated wisdom, which makes teaching this class the peak academic experience of my career.

Because law students do not speak the language of managers and managers know virtually nothing of the law, I decided to write my own casebook designed to bridge the gap. My publishers at West Academic Publishing were bold enough to gamble on the possible demand for the casebook, which

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became *An Introduction to the Law of Business Organizations*.[1] The casebook has made it through three editions and was recently transformed into a basic business law textbook, which I wrote with a beloved former student who has spent his career teaching primarily in business schools.[2] I expect soon to switch to the new casebook (it will be published by the time this Article appears), but I do not expect to vary the content of the course I teach. I included in the new casebook the key materials from my original casebook.

The first session of the class, lasting only one and one quarter hours (the class is taught in the evening to accommodate the schedules of the Kellogg students, many of whom are employed full-time), is an introductory one, devoted to exposing the students to the basic doctrines of property, contracts, and torts, and also to defining what the law actually is and the goal of the rule of law. After a bit of intensive Socratic dialogue, I can usually manage to get the students to agree that the law is a set of rules for governing society that are administered by courts and agencies, behind which stands the force of the state. (This is not, of course, so very different from William Blackstone's definition of law as the command of the sovereign, specifying rights and prohibiting wrongs.[3]) I have the students read, for this first class, *Pierson v. Post*,[4] *Williams v. Walker-Thomas Furniture Co.*,[5] and *Lovelace v. Astra Trading Corp.*[6] in order to suggest that there are competing policies that the basic legal doctrines seek to implement. They learn, for example, that rules of property seek simultaneously to implement certainty and predictability and fairness and equity, and that the rules of contract seek to promote bargains struck by individuals but refuse enforcement of agreements that shock the conscience. This unsettles many students who come to my class believing, with regard to property, that "possession is nine-tenths of the law," and, with regard to contracts, that any signed writing ought to be enforceable. *Lovelace*, a torts case where the court holds that manufacturers ought to be liable for harm to foreseeable bystanders caused by products which leave the factory in an unreasonably dangerous condition,[7] alerts the Kellogg students to the manner in which issues of liability are crucial to business planning, and, in its rather

1. STEPHEN B. PRESSER, AN INTRODUCTION TO THE LAW OF BUSINESS ORGANIZATIONS (3d ed. 2010).

2. TIMOTHY L. FORT & STEPHEN B. PRESSER, BUSINESS LAW (2014).

3. 1 WILLIAM BLACKSTONE, COMMENTARIES *44 ("Municipal law, thus understood, is properly defined to be a rule of civil conduct prescribed by the supreme power in a state, commanding what is right and prohibiting what is wrong.") (internal quotation marks omitted).

4. Pierson v. Post, 3 Cai. 175 (N.Y. 1805).

5. Williams v. Walker-Thomas Furniture Co., 350 F.2d 445 (D.C. Cir. 1965).

6. Lovelace v. Astra Trading Corp., 439 F. Supp. 753 (S.D. Miss. 1977).

7. *Id.* at 761.

startlingly unpredictable standard, to the common law's leanings toward enterprise liability generally.

The second class begins with a one and one-quarter hours question-and-answer period, in which I allow the three groups to turn the tables of the Socratic method and ask me any question they wish about the law and legal institutions or about business generally. After one student poses a question, I often will offer another student the chance to answer the question first. This is a means of beginning to get the three groups to talk to one another. In that manner, I can show the business school students and the foreign lawyers how American law students instinctively are familiar with a legal system based on precedents, and how, for American lawyers, procedure may be even more important than substance. I seek, as well, to suggest to the American students the advantages of the statute-based civil law system with which my LL.M. students are intimately familiar. I am invariably asked to explain the hierarchical American court system and our system of dual sovereignty, whereby litigants might find themselves in state or federal court. I also make sure they all understand some of the curious aspects of American litigation, such as the fact that more than ninety percent of cases are settled before they reach a verdict, usually before the trial even starts. I also am invariably given the opportunity, in this question-and-answer session, to indicate the different tasks accorded to the judge and jury. I get to deal with the incredulity and apprehension that my civil law students have for American juries since most of their countries operate without that sacred American legal institution.

The second segment of the second class is an introduction to the doctrines of agency and partnership law. We explore the manner in which the law allows some persons to control the acts of others while at the same time creating liability on the part of the principals for the acts of the agent, and we explore further the manner in which a fiduciary responsibility is imposed on agents so that their principals' interests will be implemented.[8] Partnership law is explained as the creation of an elementary business organization in which the owners all act as agents for one another, and, of course, assume liability for one another's acts and undertake a concomitant fiduciary responsibility to one another.[9] In this class, I assign the famous *Meinhard v. Salmon* case.[10] I introduce this case both to expose the students to the fabulous purple prose of

8. *See* Croisant v. Watrud, 432 P.2d 799, 801–02, 804 (Or. 1967) (discussing the fiduciary relationship between a principal and his agent whereby the principal is liable for the agent's actions). *See also* Tarnowski v. Resop, 51 N.W.2d 801, 803 (Minn. 1952) (discussing an agent's liability to the principal for violations of fiduciary duties).

9. *See* Martin v. Peyton, 158 N.E. 77, 78 (N.Y. 1927) (discussing the creation of a partnership and the duties that partners owe to one another).

10. Meinhard v. Salmon, 164 N.E. 545 (N.Y. 1928).

Cardozo and further to impress them with American law's concept of fiduciary duty as requiring "the punctilio of an honor the most sensitive" and as encompassing conduct "higher than that trodden by the crowd."[11]

The third class is an introduction to the corporation, which I essentially present as the highest achievement of American law. I contrast the corporation with the partnership, the sole proprietorship, and the LLC, and we explore the question of whether the corporation should be simply a vehicle for return on investment for the shareholders, or whether the corporation, as a powerful actor in society, ought to assume some social responsibility beyond that of the duty it owes to its owners. In this case, I contrast two great old chestnuts of corporate law—*A.P. Smith Manufacturing Co. v. Barlow*, which allowed a corporation to make charitable contributions to Princeton University on the grounds that corporations owed a societal duty to preserve the capitalist system of private education,[12] and *Dodge v. Ford Motor Co.*, in which the Michigan Supreme Court essentially held that Henry Ford could not operate his automobile company as a semi-eleemosynary institution.[13]

In this third class, I also introduce the students to the "internal affairs doctrine," which is the doctrine whereby the internal affairs of American corporations—meaning the relationships among the shareholders, directors, and officers—is regulated by the state of incorporation, and, indeed, the basic doctrine of the American law of corporations is that it is the states—and not the federal government—that are the primary regulators of business organizations.[14] The law students are already somewhat sensitized to this notion since they have learned, to their own surprise, that state law and state courts are the primary enforcement mechanisms for the doctrines of property, contracts, and torts. Most American law students, and, to an even greater extent, most foreign lawyers and management students have been brought up thinking federal law is the only significant American law. My Business Associations class is one way of helping these three groups learn about Federalism, our system of dual sovereignty. Throughout the course, I seek to sensitize the students to the question of whether it is better to have one central system supervised by the federal government (which is, of course, the notion behind the federal securities laws, the Sarbanes-Oxley Act, and the Dodd-

11. *Id.* at 546.

12. A.P. Smith Mfg. Co. v. Barlow, 98 A.2d 581, 582, 590 (N.J. 1953).

13. Dodge v. Ford Motor Co., 170 N.W. 668, 671, 683, 685 (Mich. 1919).

14. *See* Edgar v. Mite Corp., 457 U.S. 624, 645 (1982) ("The internal affairs doctrine is a conflict of laws principle which recognizes that only one State should have the authority to regulate a corporation's internal affairs—matters peculiar to the relationships among or between the corporation and its current officers, directors, and shareholders—because otherwise a corporation could be faced with conflicting demands.").

Frank Act), or whether it is better to have fifty "social laboratories" competing to determine the best means of promoting and regulating business.

As an ongoing class exercise, I have the students "form" a business entity to market a new and promising microcomputer chip (one that, by hypothesis, will earn billions of dollars), and I ask them to choose a state in which to incorporate this new entity. We begin with a hypothetical and choose New York for incorporation, only to discover that the choice of this state could subject individual shareholders to liability since New York, in the case of certain closely held entities, makes some shareholders responsible for the salaries of employees[15] (presumably owing to the great sway labor organizations have in the Empire State). This leads to a comparison with Delaware, and I raise William Cary's classic assertion that the law of Delaware "water[s] the rights of shareholders vis-à-vis management down to a thin gruel."[16] Through an exploration of Cary's bill of indictment, including the assertions that Delaware makes it too easy to pay dividends, too easy to accomplish organic change, too easy to avoid cumulative voting, too difficult to gain a seat on the board of directors (because staggered boards are permitted), too difficult to maintain share ownership (because preemptive rights are not required), and too easy for managers to escape liability (because generous indemnity provisions exist), the students see that Cary is certainly correct that minority shareholders have less influence in Delaware.[17] This allows me to underscore the issue of whether corporations should exist simply to create a return on investment for shareholders (the orthodox position of Delaware law), or whether, instead, business organizations ought to be regarded as arenas for political participation, which should be more sensitive to minority ownership rights. The law students, procedurally oriented, tend toward sensitivity to minority participation, but the management students, with an eye toward the bottom line, intuitively see the wisdom in Delaware's approach, particularly when they are informed that the stock market appears to grant a premium for reincorporation in Delaware.

The fourth class begins with what I label a "dramatic reading" from the autobiography of famed New York trial lawyer Louis Nizer, *My Life in Court*.[18] It is his account of his work as counsel to Joseph R. Vogel, then the President of Loew's, Inc., who was engaged in a titanic struggle for control of

15. *See* N.Y. BUSINESS CORPORATION LAW § 630 (McKinney 2003).

16. William L. Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663, 666 (1974).

17. *Id.* at 669; *but see* Daniel R. Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware's Corporate Law*, 76 NW. U. L. REV. 913, 916–17 (1982) (writing a pungent criticism of Cary's thesis).

18. LOUIS NIZER, MY LIFE IN COURT (1961); *see also* Freeland T. Penney, Book Review, 11 U. KAN. L. REV. 191, 191 (1962) (reviewing LOUIS NIZER, MY LIFE IN COURT (1961)).

the corporation, and, in particular, its most important division, the Metro-Goldwyn-Mayer film studio.[19] Nizer was enlisted to help his client, Vogel, defeat a challenge from the deposed head of MGM studios, Louis Mayer, the Mayer in Metro-Goldwyn-Mayer and the legendary "king of Hollywood," and a couple of handpicked board members friendly to Mayer, including Joseph Tomlinson, a rough-hewn Canadian millionaire who, in the service of Mayer's plan for revenge, brought the operations of the corporation to a halt.[20] Nizer helped his client by getting the Delaware court, for the first time, to approve of shareholders removing directors for cause and to approve of the board members whom Vogel controlled staying away from board meetings to prevent a cabal without the best interests of the corporation at heart from forming within the quorum.[21] As well as outlining a story fit for a gripping Hollywood blockbuster, this episode introduces the students to the manner in which shareholders, directors, and officers interact to control a corporation. It also shows the students how important it is for the Delaware Court of Chancery to formulate these rules for American corporations.

The fifth class builds upon the introduction to the players in the corporation presented in the fourth class to underscore the fiduciary responsibility that state law imposes on directors and officers. I divide this fiduciary responsibility into three categories—nonfeasance, misfeasance, and malfeasance. *Francis v. United Jersey Bank*[22] is my vehicle for exploring nonfeasance—the penalty for failing to act when a similarly situated, reasonably prudent director would have acted, and this failure to act causes harm to shareholders, or, as in this remarkable case, creditors.[23] The characters in the case are straight out of a soap opera, and the students are generally touched by the insensitivity of holding a bereaved widow responsible for the acts of her miscreant sons. They also are struck by the necessity to enforce the monitoring duties of directors, lest the shareholders or creditors suffer. I also stress American law's rather harsh treatment of those who fail to act with the gentler requirements inherent in the business judgment rule. Under the business judgment rule, no liability is imposed, even if there are losses to the corporation, if a director rationally acts in good faith and in a manner he believes to be in the best interest of the corporation, so long as he is free from

19. NIZER, *supra* note 18, at 431, 435, 445. Nizer discusses the story of Vogel's struggle in chapter 6. *Id.* at 427–524.

20. *Id.* at 429–30, 437–38, 443, 445, 447. Mayer enlisted Tomlinson to help him retake control of MGM by attempting to slow business operations. *Id.* at 447–55.

21. *Id.* at 509; *see also* Campbell v. Loew's, Inc., 134 A.2d 852, 858, 862 (Del. Ch. 1957) (dicussing the analysis and rationle behind the court's ruling).

22. 432 A.2d 814 (N.J. 1981).

23. *Id.* at 824, 829.

conflicts of interest, even if the actions he takes are demonstrated to be unreasonable.[24]

After a tiny bit of prompting, the Kellogg students intuitively realize that this rule of law is in keeping with what they have learned since their first days at the School of Management, that the greater the risk the greater the eventual reward, and, therefore, the business judgment rule simply implements America's proclivity toward risk-taking entrepreneurs (as, indeed, does incorporation in Delaware generally, as the students learned in an earlier class).[25] But, as soon as this is grasped, I expose the students to the infamous *Smith v. Van Gorkom*[26] case and the Delaware Supreme Court's holding that businessmen cannot be shielded by the protection of the business judgment rule if they were not adequately informed before making the business judgment.[27] The law students are generally willing to accept this notion at face value, but the business school students are struck by the fact that the assessment of whether the information at hand is adequate is itself the quintessential business judgment. The students' understanding brings home the lesson that sometimes a majority opinion is incorrect, and the dissent has the better argument, as was doubtless true in that case. Consideration of *Smith v. Van Gorkom* (which at least one prominent business law teacher has suggested should no longer be taught)[28] also allows me to raise the possibility that the Delaware Supreme Court may be responding to the criticism of academic critics such as Cary, in an effort to demonstrate that the court is, indeed, committed to the protection of shareholders and not to the watering down of their rights to a thin gruel.

Still, by the time we are finished with *Smith v. Van Gorkom* (which I have used as a means of clearly distinguishing between the cases of nonfeasance (like *Francis*) and misfeasance (the classic business judgment rule situation)), the students conclude with the critics of *Van Gorkom* that the majority (who believed it was a case of nonfeasance) were incorrect, and the dissenters (who thought the case was one that called for the classic application of the business

24. *See* Smith v. Van Gorkom, 488 A.2d 858, 872 (Del. 1985). The Supreme Court of Delaware struggles with the application of the business judgment rule, as evidenced in the majority and dissenting opinions. *Id.* at 863, 893, 898.

25. *See* N.Y. BUSINESS CORPORATION LAW § 630 (McKinney 2003); Cary, *supra* note 16, at 669.

26. *Van Gorkom*, 488 A.2d 858.

27. *Id.* at 872.

28. Lawrence A. Hamermesh, *Why I Do Not Teach* Van Gorkom, 34 GA. L. REV. 477, 477–78 (2000).

judgment rule) got it right.[29] The law students are used to the byplay between majority and dissenting opinions, of course, but it is an eye-opener for both the Kellogg students and the LL.M. students. The former group is under the impression that the law ought to be clear and certain, and thus, something with which the United States Supreme Court justices should not disagree. The latter, as civil lawyers, are astonished by and unfamiliar with the disagreements that characterize our common law system.

As a last exercise in the fifth class, I divide the students into groups of five or six, requiring each group to appoint at least one Kellogg student and one LL.M. student who will draft a statute dealing with the problem of interested director transactions. This is my means of familiarizing them with a third aspect of fiduciary duty. The first two fiduciary duties are nonfeasance and misfeasance, both presumably products of inadvertence, but this third area, which I label "malfeasance," is the area of conflict of interest. This is a situation found not only in interested director transactions, but also, at least, in the areas of corporate opportunity, executive compensation, and sale of control by majority shareholders. The students have been exposed to some conflict of interest cases, particularly the wonderful *Cookies Food Products* case[30] and their statutes (which I have spokespersons for the groups read aloud to the other groups—encouraging appropriate positive or negative responses from the auditors). The students invariably recognize the importance of disclosure (both of the conflicts of interest and of material facts known to the party with the conflict of interest), the need for a disinterested corporate decision-maker, and the requirement that the transaction be in good faith and fair to the corporation.

The sixth class is an optional midterm, which the Kellogg school requires me to offer. For the students who take it, the midterm counts for one-third of their course grade, and the final counts for two-thirds of their grade. I give no points for class participation because I am an inveterate practitioner of the Socratic method (alarming to both the Kellogg students and LL.M. students who are used to lecturing), and I require uniform and enthusiastic participation. Our tradition at the law school is that of "sudden death" by which a student's grade depends on one final exam at the end of the course. The optional midterm, however, offers the LL.M. students and the Kellogg students an opportunity to spread the risk. While the Kellogg students generally appreciate American law's embrace of their perspective that the greater the risk the greater the reward, most of the Kellogg students tend to take the midterm,

29. *Van Gorkom*, 488 A.2d at 874; *id*. at 897 (McNeilly, J., dissenting). The dissenters of the Supreme Court of Delaware argue the board of directors did comply with the business judgment rule. *Id.* at 897–98.

30. Cookies Food Prods., Inc. v. Lakes Warehouse Distrib., Inc., 430 N.W.2d 447 (Iowa 1988).

while few law students do the same. I return the exams to them the next week, and I pick out one of the best (without revealing who the author is or the grade I have assigned) and have them all read it. Then, I call on a few students to suggest a grade and defend it. I then explain why I assigned the high grade I did. This, I think, relieves a bit of anxiety about the final both for those who have taken the midterm and the vast majority who have not.

Following this review of the midterm, in the seventh class, we proceed to examine an analogue to the state law of fiduciary responsibility (the subject of the fifth class), what I describe as a federal attempt to enforce fiduciary responsibility—the federal law of insider trading. After a quick review of the limited state law on forbidding insider trading without disclosure, we begin our examination of federal law, pursuant to my explanation that this is the federal government's way of attempting to protect shareholders, in the belief that state law does not do an adequate job. We concentrate on the Securities Exchange Act of 1934, primarily Sections 10(b), 14(e), and 16(b), and the related rules and regulations of the Act, in particular Rules 10b-5 and 14e-3.[31] I go through many hypotheticals with the students based on cases involving brokers, journalists, printers, and lawyers, attempting to draw distinctions between those who are under a fiduciary duty to disclose or abstain from trading and those who are not. The most important case is *United States v. O'Hagan*, where the United States Supreme Court made clear the extent of liability under both Rule 14e-3 and 10b-5.[32] I present three theories that lie behind the Court's decisions in this area—the equal playing field theory (which was put forward by the SEC and suggesting that no one should ever be permitted to trade on inside information without first disclosing it),[33] the misappropriation theory (which forbids trading on information for a particular purpose other than trading on the information—e.g. for printing documents or rendering legal counsel),[34] and the corporate fiduciary theory (which prohibits any corporate employee privy to inside information from trading without disclosure).[35] We explore the pros and cons of each theory. We also seek to understand how the Supreme Court could fully endorse both the misappropriation and the corporate fiduciary theories but only approve the equal playing field theory in

31. Securities Exchange Act of 1934 §§ 10(b), 14(e), 16(b), 15 U.S.C. §§ 78j, 78n, 78p (2006); 17 C.F.R. § 240.10b-5, .14e-3 (2006); *see also* United States v. O'Hagan, 521 U.S. 642, 651–52, 668–69 (1997) (discussing the scope of liability under Rules 10b-5 and 14e-3).

32. *O'Hagan*, 521 U.S. at 651–52, 669.

33. *See* 15 U.S.C. § 78p; *see also* Chiarella v. United States, 445 U.S. 222, 232–33, 235 (1980) (arguing against the equal playing field theory).

34. *See O'Hagan*, 521 U.S. at 652–54 (adopting the concept of liability as explained under the misappropiration theory).

35. *See Chiarella*, 445 U.S. at 227 (discussing the corporate fiduciary theory).

the narrow area of information regarding tender offers or takeovers (pursuant to Rule 14e-3).[36]

I finish our consideration of Section 10(b) and Rule 10b-5 by examining the "tippee" theory of *Dirks*.[37] I also explain how Martha Stewart was pursued by the SEC under a tippee-misappropriation theory because she acted on information wrongfully supplied to her by her broker regarding what other clients of Merrill Lynch were doing (here, Martha's friend Sam Waksal who was the CEO of the corporation in whose stock she was wrongfully trading).[38] This brings together all of our theories and brings home the problem by examining the misbehavior of a famous popular businesswoman, riveting both the managers and the lawyers.

I conclude the seventh session with an examination of the short-swing profit disgorgement provision, Section 16(b) of the 1934 Act, which is designed to prevent insider trading but, paradoxically, requires no actual insider knowledge.[39] In order to underscore the divergent jurisprudential philosophy of Sections 10(b) and 16(b),[40] I ask the class to consider two superheroes—Superman and Batman—and ask which one they prefer. This tangential discussion these days reveals a preference on the part of both law students and management students for Batman, although as recently as four years ago the Kellogg students preferred Superman by two-to-one, and the law students preferred Batman by two-to-one. I explain that Superman is like Section 10(b) and Rule 10b-5, provisions that the courts have expanded to give superpowers (broadly construing "manipulative or deceptive device or contrivance," "interstate commerce," and implying a private right of action (now express in the PSLRA of 1995)),[41] and that Batman is like Section

36. *See O'Hagan*, 521 U.S. at 672, 674 (examining how the equal playing field theory relates to tender offers).

37. Dirks v. SEC, 463 U.S. 646, 651 (1983).

38. *See* Michael L. Seigel & Christopher Slobogin, *Prosecuting Martha: Federal Prosecutorial Power and the Need for a Law of Counts*, 109 PENN ST. L. REV. 1107, 1110, 1114–15 (2005).

39. 15 U.S.C. § 78p (2006); *see also* Peter M. Dugré, *Securities Exchange Act Section 16(b): Fourth Circuit Harvests Some Kernels of Gold*, 42 FORDHAM L. REV. 852, 852–53 (1974) (discussing the application of Section 16(b) and the lack of a requirement of either actual use or intent to use inside information).

40. 15 U.S.C. §§ 78j, 78p; *see also* Craig M. Walker, *Accountants' Liability—The Scienter Standard Under Section 10b and Rule 10b-5 of the Securities Exchange Act of 1934*, 63 MARQ. L. REV. 243, 245, 250 (1979) (discussing the requirement that intent must be proven to bring a successful claim under Section 10(b) and Rule 10b-5).

41. 15 U.S.C. § 78j; 17 C.F.R. § 240.10b-5 (2014); Private Securities Litigation Reform Act of 1995 § 21D, 15 U.S.C. § 78u-4 (2006); *see also* Mark J. Loewenstein, *The Supreme Court, Rule 10b-5 and the Federalization of Corporate Law*, 39 IND. L. REV. 17, 19 (2005) (discussing cases in which the Court has expanded the reach of Section 10(b) and Rule 10b-5).

16(b).[42] Section 10(b) and Rule 10b-5 have a requirement of *scienter* and only punish actual wrongdoers,[43] much in the manner that Superman stands for truth, justice, and the American way, and would only act against evil. Section 16(b), on the other hand, requires no proof of evil intent and applies to anyone who falls into its rather arbitrary categories.[44] This is much like Batman, the Dark Knight, who occasionally seems to want to lash out in a manner that fails to distinguish between the good and the bad and "whack" people just for the sheer joy of it. This is probably something of a strained analogy, but it does at least highlight two different approaches to the legislator's art.

In the eighth session, we return to the topic of state law to study the legal problems of the close corporation. I explain that these problems are, essentially, the same as one encounters when thinking about the LLC. I explain that they can expect to be dealing with LLCs as the start-up vehicle of choice when they begin practice as lawyers or managers. Accordingly, my way of bringing this home to them is to devote about forty-five minutes of class to an in-class exercise in which the students are asked to write a shareholders' agreement for a drug store in which each of them is a part owner. The hypothetical is suggested by *Galler v. Galler*[45] and is done in the same small groups (including in each group a Kellogg student and a LL.M. student) that were employed when they drafted a statute in class five. This exercise is a means of once again bringing home to the managers and the lawyers the importance of careful drafting, and the means in which counsel can help managers plan strategically for conflict resolution, especially in a manner that avoids litigation. This exercise forces them to articulate rules of fiduciary responsibility and restrictions for transfer, buyback, and sales of shares (prompted by *Donahue v. Rodd Electrotype Co.*[46]), to consider the advantages and disadvantages of removing a board of directors (suggested by *Galler v. Galler*, itself[47]), and to create means of avoiding the majority oppressing the minority (the central problem of the close corporation), as was suggested by their previous reading in *Baker*[48] and *Cookies Food Products*.[49] I review with

42. 15 U.S.C. § 78p.

43. 15 U.S.C. § 78j; 17 C.F.R. § 240.10b-5; *see also* Walker, *supra* note 40 (discussing the requirement of scienter when applying Section 10(b) and Rule 10b-5).

44. 15 U.S.C. § 78p; *see also* Dugré, *supra* note 39 (discussing the lack of a requirement of intent to use inside information for Section 16(b)).

45. 203 N.E.2d 577 (Ill. 1965).

46. Donahue v. Rodd Electrotype Co. of New England, Inc., 328 N.E.2d 505, 515, 518–19 (Mass. 1975).

47. *Galler*, 203 N.E.2d at 584–85.

48. Baker v. Commercial Body Builders, Inc., 507 P.2d 387, 395–96 (Or. 1973).

49. Cookies Food Prods., Inc. v. Lakes Warehouse Distrib., Inc., 430 N.W.2d 447, 454 (Iowa 1988).

them the statutory set of solutions provided by the special provisions of the Delaware Corporations Code dealing with close corporations and suggest that all of these problems can be dealt with by shareholder agreements in the close corporation or by member agreements in the LLC.

The ninth class is the final substantive class for the course (there is one more session, devoted to review of each of the prior classes, and a Q & A period), which I call "Aspects of the Endgame." In that class, I explain that one way to conceptualize the course is a review of the life cycle of a business organization (reminding them that we formed our own entity in an earlier class and have been reviewing its operation in subsequent classes). I further explain that this last class is about what happens when you kill a business organization—how the law deals with organic change in a business organization. I begin by stressing that it is mandatory that the board and shareholders be given a vote. Then, I explain that where we are dealing with business organizations that are not publicly traded, in particular closely held corporations, dissenting shareholders have a right to have their shares valued and to receive cash for those shares.[50] This leads us to a discussion of valuation, and I stress that this is a topic that baffles lawyers. We explore the Delaware block method, as elegantly set forth in *Piemonte v. Boston Garden*,[51] and I do a hypothetical for the valuation of our imaginary corporation. In performing the valuation, I consider the vastly different figures that result from a consideration of asset value (based on the balance sheet), market value (based on a limited amount of data resulting from thinly traded stock), and earnings value (which generally results in a much larger figure).

In exploring valuation, I attempt to explain that the approach of lawyers is to try to take account of all available data (the Delaware block method, after all, is a marvel of lawyers' conceptualization, to try to take account of the three-dimensional temporal world of past, present, and future), while the approach of financial analysts is to determine simple and easily applicable tools such as discounted cash flow or comparative premium studies.[52] I end this exercise with a consideration of *Weinberger v. UOP, Inc.*,[53] the great case where the Delaware Supreme Court signaled a willingness to move from the highly artificial Delaware block method to any form of currently acceptable methods of valuation approved of by the financial community.[54] *Weinberger* is

50. See DEL CODE ANN. tit. 8, § 262 (2014) for a list of dissenters' rights in Delaware.

51. Piemonte v. New Boston Garden Corp., 387 N.E.2d 1145, 1148 (Mass. 1979).

52. These methods are discussed in Weinberger v. UOP, Inc., 457 A.2d 701, 712–14 (Del. 1983).

53. *Id.*

54. *Id.*

also splendid as a review of the rules that apply in conflict of interest situations in general and the profound importance of disclosure in particular.

Picking up another main theme in the course—Federalism—I move to a consideration of the Williams Act, suggesting that it—like the rules regarding insider trading—is another instance in which a perception that state law inadequately protects shareholders results in federal government oversight. I quote from Harrison Williams's comments on the floor of the Senate, where he railed against "White Collar Pirates," who have allegedly looted old established corporations, and we discuss whether it ought to be good public policy to encourage or discourage tender offers and takeovers.[55] The Kellogg students, steeped in the efficient capital market hypothesis, generally argue for the promotion of tender offers and takeovers, on the theory that targets are often depressed because of inefficient management, while the law students tend to worry about corporate looters, sensitized as they are to the possibility of miscreants among the practitioners of high finance. I review the empirical data on changes in share value following successful and unsuccessful tender offers. After reviewing this data, I argue that we can understand state and federal regulation as a search for a "sweet spot," in which tender offers are not completely frustrated but enough resistance is permitted either to encourage competing bids or otherwise to maximize the offers made to shareholders. This point, which the provisions of the Williams Act seem to illustrate, is strengthened by a consideration of the five great Delaware defensive tactic cases—*Unocal*,[56] *Moran v. Household International, Inc.*,[57] *Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc.*,[58] *Paramount Communications Inc. v. Time Inc.*,[59] and *Paramount Communications Inc. v. QVC Network, Inc.*[60] —in which the Delaware Supreme Court struggled to determine how much discretion to allow incumbent management to resist hostile bidders. The problem is brought home by demonstrating the manner in which Martin Davis, the CEO of Paramount, loses in *Paramount v. Time* when he is the bidder, and then again in *Paramount v. QVC*, in which he is the target. Then, I pose the question of whether or not the Delaware Court's goal is simply the frustration of Martin Davis, or whether there are, in fact, subtleties regarding the permissibility of defensive tactics that really do make good sense. Regardless,

55. For Williams's statement, see 111 CONG. REC. 28,257 (1965) (statement of Sen. Harrison Williams).

56. Unocal Corp. v. Mesa Petroleum Co., 493 A.2d 946 (Del. 1985).

57. Moran v. Household International, Inc., 500 A.2d 1346 (Del. 1985).

58. Revlon, Inc. v. MacAndrews & Forbes Holdings, Inc., 506 A.2d 173 (Del. 1986).

59. Paramount Commc'ns Inc. v. Time Inc. 571 A.2d 1140 (Del. 1989).

60. Paramount Commc'ns Inc. v. QVC Network Inc., 637 A.2d 34 (Del. 1994).

as the Delaware Court searches for the "sweet spot" to better protect shareholders, the "thin gruel" accusation levied by Cary is wrong

CONCLUSION

It is, of course, not completely possible to articulate exactly what happens in ten evening classes in a short article of this nature, but I hope enough has been said to suggest that what I am trying to do with a Business Organizations course (other than demonstrating to budding managers and lawyers that they need to understand the different perspectives the two groups bring to the exercise) is to demonstrate that the law of business organizations is, like all American law, a struggle to reconcile competing human desires and competing public policies. I stress personalities and passions, and wallow sometimes in betrayals and frustrations, emphasizing the foibles of actors such as Salmon (who slighted Meinhard),[61] Louis B. Mayer (who tried to crush his successor, Joseph Vogel),[62] Lillian Pritchard (whose stunning dereliction of duty permitted her malevolent offspring to loot a brokerage),[63] Martha Stewart (whose greed landed her in federal prison),[64] or Martin Davis (who could not get the wisdom of his "strategic plan" approved by the Delaware Judiciary).[65]

Teachers of the Business Organization course have an enviable opportunity. Students expect it to be boring, rule-obsessed, and dry, but they are utterly captivated when they discover that it is about nothing less than the ultimate realities of the human condition. Managed properly, and with the extraordinary tools that are now available,[66] Business Organizations can become an almost thrilling exploration of political science, financial planning, and human psychology.

61. Meinhard v. Salmon, 164 N.E. 545, 546 (N.Y. 1928).

62. JERRY W. MARKHAM, A FINANCIAL HISTORY OF MODERN U.S. CORPORATE SCANDALS FROM ENRON TO REFORM, 271–72 (2006).

63. Francis v. United Jersey Bank, 392 A.2d 1233, 1235 (N.J. Super. Ct. Law Div. 1978).

64. *See* Seigel & Slobogin, *supra* note 38, at 1114–15, 1117 (discussing the prosecution of Martha Stewart).

65. *QVC Network Inc.*, 637 A.2d at 49–50.

66. For examples, see two wonderful recently published collections of essays on the great cases in the law of business organizations: THE ICONIC CASES IN CORPORATE LAW (Jonathan R. Macey ed., 2008) and CORPORATE LAW STORIES (J. Mark Ramseyer ed., 2009).