

Law 6060-01  
Business Associations  
Jonathan Klick

The Armageddon

April 30, 2007  
8:30-12:30  
Room 101

This final exam consists of four questions (with three subparts for each question, except for question #4 which does not have subparts). Each question will be given equal weight in determining your final grade.

This is an open book and open note exam. You may use your casebook, class notes, casebook supplements, commercial outlines, commercial supplements, lucky charms, and any other printed or written materials you believe will be helpful in completing your answers.

You will be given four hours to complete this exam, and you may allocate your time among the questions as you see fit. There is no answer sheet for this exam. You may write/type as long or as short an answer as you believe is necessary to completely answer the test questions. If you need extra bluebooks, please quietly request them from the proctor. If you finish early, please submit your bluebooks or computer disks to the exam proctor and quietly exit the room.

If you perceive an ambiguity or error in any test question, please proceed to answer it, noting the ambiguity/error and making any reasonable assumptions you believe are necessary to answer the question. Please state these assumptions in your answer and provide your justification for the assumption.

Since some students have arranged to take the exam at a later date, recognize that any information you provide them about the exam will adversely affect your own grade because of the law school's grading curve.

Good luck and have a nice break.

1. According to the New York Times, 1/3 of the initial public offerings launched this year have been for SPACs (i.e., Special Purpose Acquisition Corporations) which use the equity raised from the public offerings for the sole purpose of engaging in the acquisition of firms identified by the SPAC managers as being undervalued. In the prospectuses for these SPACs, it is not uncommon for the firm to describe the general industry or country in which the SPAC will specialize but to leave the specific targets of the acquisition plans unspecified. Assume you are the corporate counsel for a newly created SPAC called FSU and you are drafting the disclosures for FSU's prospectus that will be sent out in advance of the initial public offering to investors and the SEC. You know that FSU's managers have specifically identified a number of underperforming firms in the telecommunications industry and plan to use the funds from the IPO to acquire control or at least large blocks of shares in these firms.
  - a. In drafting FSU's disclosures, what concerns will drive the degree of specificity you use in describing FSU's business plans?
  - b. Prior to FSU's first annual meeting, one of FSU's shareholders, Warren Buffett (who manages his own investment portfolio, Berkshire Hathaway, that often targets under performing telecommunications firms for acquisition) requests that the following proposal be put up for a shareholder vote on the proxy statement: "During each annual meeting, the managers of FSU must disclose all firms they plan on targeting during the coming year." In your role as FSU's corporate counsel, what kind of advice do you give to FSU's board members in their decision about whether or not to include Buffett's proposal on the proxy statement.
  - c. Relative to hedge funds and private equity funds (which are generally not subject to the SEC's disclosure and reporting requirements) what are some of the pros and cons of organizing as a publicly traded SPAC?

2. Two economists, K & G, start a consulting partnership in which they provide expert witness services in cases involving claims that misleading statements on the part of a firm's management led to shareholder harm. K & G jointly developed a new method for performing the "event studies" that are generally used in such cases to isolate changes in stock prices attributable to the misleading statement independent from normal variation in stock returns and the variation that can be attributable to normal market movements. In their partnership agreement, K & G agree to share all profits and losses equally and they agree that the partnership will continue until they mutually agree to terminate it. In terms of capital structure, each provided an equal amount of start-up equity and they each generally spend an equal amount of time soliciting clients and performing the duties necessary for the consulting services. They published the details of their event study methodology in the academic journal *The Journal of Financial Economics*. The partnership employs one non-partner economist, F, to help in preparing analyses for K and G. F does not have a contract and is an at will employee.
  - a. K is approached by a hedge fund manager who offers K a substantial amount of money to perform event studies, using the K & G methodology, to aid in the development of investment strategies for the fund. K accepts, performs the analyses, and receives a hefty paycheck. G discovers what has happened and demands that K remit half of the fees he received from the hedge fund. K refuses. If the dispute goes to court, outline G's legal claim and K's defense against that claim.
  - b. Assume K ends up not having to pay damages to G in part a. This enrages G, who decides to stop soliciting new clients and performing analyses for existing clients, but he still demands his 50 percent share of the profits brought in by K's work, as per the partnership agreement. As K's legal counsel, what do you advise K to do and why? If you had been consulted before the drafting of the partnership agreement, what would you have suggested regarding the termination provision and why?
  - c. F quits working for K & G and the next day, he sets up his own expert witness business, offering to employ the K & G event study methodology for clients for a fee one half of that charged by K & G. A number of K & G's clients end their relationship with K & G and instead retain F. Do K & G have any claim against F for "stealing" their clients? Why or why not?

3. Agency costs constitute a (if not the) central concern in all of business law. Discuss how agency costs could provide the causal mechanism for the following empirical findings and discuss how one might be able to mitigate these agency costs in the given context.
  - a. After controlling for observable differences between the houses, when real estate agents sell their customers' houses (on a standard commission rate of about 6 percent of the sales price), the sales price is, on average, about 4 percent lower than the prices real estate agents get when they sell their own houses and the real estate agent-owned houses stay on the market (before selling) about 10 days longer than houses the real estate agents sell for their customers.
  - b. In the U.S. system, the presiding judge must OK the terms of any class action settlement (including the fees for the plaintiffs' attorney) since there is the worry that the plaintiffs' attorney and the defendant will devise a collusive settlement. This worry arises from the fact that the victims involved in a class action case (almost by definition) have no incentive to monitor "their" attorney, so there is the potential that the settlement will be constructed to maximize the plaintiffs' attorney fee while minimizing the amount the defendant must pay (which, in turn, substantially lowers the value received by the victim class itself). However, it has been shown that as judicial workload rises (i.e., the number of cases on a judge's docket) plaintiffs' attorney fees in class actions also rise.
  - c. There is evidence that cardiologists order fewer tests and perform fewer procedures on heart attack patients with insurance in states that implement medical malpractice damage caps (i.e., restrictions on how much money a plaintiff can receive if he is successful in medical malpractice litigation) relative to states that do not limit awards in medical malpractice cases. Further, there is no resulting difference in ultimate health outcomes between patients in states with and without medical malpractice damage caps (e.g., the 1 year mortality rates of patients in the two sets of states are very similar on average).

4. Choose one of the preceding questions (1, 2, or 3) to count double or choose to have each of the questions count for  $\frac{1}{3}$  of your total grade. Please be clear regarding which choice you hope to make. The default rule (i.e., what I will do if you do not make your choice clear) is that you simply lose 25 percent of the points available on the test.