

FINAL EXAMINATION

General Instructions

1. This is a three-hour examination. It has twenty-two pages, with two essay questions and fourteen multiple-choice questions. Thirty-five percent of your examination grade will be based on Question I, thirty-five percent on Question II, and thirty percent on the multiple-choice questions.
2. The examination is open-book: you may use any books, notes, outlines, or other printed or written materials.
3. Please write your examination number above, and please enter it on the Scantron form both by filling in the boxes in the "I.D. NUMBER" field and by writing it where the form asks for your name.
4. Do not use examination books; the examination itself provides space for you to write your answers. Although the space provided should be ample, and I encourage you to remain within it, you may, if necessary, write on the back of the examination pages.

Essay Questions

5. Please write legibly. If I can't read it, you won't get credit for it.
6. Please take time to organize your answers, and remember to discuss only the issues raised by the questions and only issues of agency law, partnership law, and corporate law. Also, keep in mind that you will receive no credit for discussing law, even in these areas, that is not relevant to the questions, and you will receive no credit for discussing relevant law if you do not explain *how* it is relevant to the specific facts set out by the questions.
7. If you believe that an additional fact is needed to answer a question, describe the missing fact and its significance.

Multiple-Choice Questions

8. Please both circle the letter of the correct answer on the examination itself **and** enter it on the Scantron form. The duplicate answers on the examination will be used to resolve any questions, or to correct any errors on the Scantron form.
9. Although you should read and consider the questions carefully, there are no "trick" questions. Therefore, if you think that a particular answer is correct except under some strained interpretation of the question or answers, you should choose that answer.

QUESTION I

The *Wall Street Journal* of November 12, 1997, carried a front-page story about a practice apparently known in the investment-banking industry as “spinning.” The practice occurs in the context of initial public offerings (IPOs) of stock. As the *Journal* describes, “IPO shares are much sought-after, because a new stock frequently soars on its first day of trading, buoyed by buying from eager investors who didn’t get in on the ground floor. Then the shares often slip back as demand abates.” The practice of “spinning” involves the allocation by an investment bank of some of the shares of the IPO of one company, say company A, to executives of another company, say company B; the shares are allocated to the executives at the stock’s original price and are then sold at a higher price later on the day of the offer. This provides the executives of company B with a quick profit, in what the *Journal* describes as “an apparent bid [by the investment banks] for business from the executives’ firms.” Moreover, the article notes that these arrangements can be risk-free to the executives, because the investment banks in some cases do not allocate the shares until after they have begun trading and have gone up in price.

The *Journal* provided this description of how the process worked in one case:

Joseph Cayre was ecstatic.

Holding an investment “road show” [*i.e.*, an informational program for possible investors] for a firm he heads that was about to go public, Mr. Cayre reveled in the first-day stock surge of an unrelated company, Pixar Animation Studios, that had just gone public itself. He boasted that he had just turned a quick \$2 million profit on 100,000 Pixar shares, witnesses to the 1995 incident say.

Where did he get a huge chunk of one of the year’s most coveted initial public stock offerings, one that surged 77% on its first day of trading? Robertson Stephens Inc., Pixar’s lead investment bank, had allocated the shares to Mr. Cayre’s personal brokerage account.

Less than a month later, Mr. Cayre’s company used Robertson Stephens for its own initial public offering. After it had become publicly held, the company, GT Interactive Software Corp., hired Robertson Stephens to advise it on acquisitions. Robertson Stephens’s total fees: more than \$5 million.

As the *Journal* describes it, “Mr. Cayre says there was no *quid pro quo*,” and that “[h]e hired Robertson Stephens simply because he liked an investment banker at the firm.” But Mr. Cayre does say that he personally asked Robertson Stephens’s chairman, Sanford Robertson, for the 100,000-share Pixar allocation, and the *Journal* reports that “when an internal debate arose within the investment bank about making such a big Pixar allocation, Mr. Robertson recalls that Mr. Cayre threatened to take his business elsewhere if he didn’t get all 100,000 Pixar shares.”

“Spinning” is defended by the investment banks. The *Journal* quotes Cristina Morgan, a managing director at investment bank Hambrecht & Quist, as saying that she thinks the practice is no different from such perks as free golf outings. “What we’re talking about is trying to solicit business,”

QUESTION II

You are in-house counsel for the Adzeville-Angler Corporation. Adzeville-Angler has two classes of common stock, denominated A shares and B shares. Only the B shares vote, but the A shares have certain dividend and liquidation preferences that make them worth more than the B shares. The great majority of the B shares are owned by Pangalactic Corporation, a public corporation, which therefore elects Adzeville-Angler's board, and has in fact filled the board with its own employees.

Adzeville-Angler's A shares are redeemable by the corporation on two months notice for \$60 cash, and are convertible by the A shareholders into B shares. In light of current publicly available information about Adzeville-Angler, the A shareholders believe that the A shares are worth more than \$60, but that the B shares are worth less than \$60 (and would still be worth less than \$60 if all the A shares were converted to B shares). Unbeknown to those outside Adzeville-Angler's management, however, the corporation's assets have appreciated, and in fact both the A shares and the B shares are worth more than \$60.

Adzeville-Angler's board has decided to give the A shareholders notice that it will redeem their shares in two months. If the A shareholders knew the true value of the corporation's assets, they would of course convert their A shares to B shares (since the B shares are worth more than \$60). They do not have that information, though, and the board does not plan to give it to them. Without that information, the A shareholders will allow their shares to be redeemed for \$60, rather than converting them, and the B shareholders will benefit.

At the board meeting where this course of action is discussed, you acknowledge that the board has the right—even perhaps the duty—to redeem, or try to redeem, the A shares, but you suggest that it also has a duty to provide information about the corporation's true value to the A shareholders, so that they can make the decision to convert. The chair of the board responds that you must have taken the four-hour, rather than the five-hour, corporations class, and says,

I think that if you review your materials, you'll find that all of the cases that mention a board's duty to inform its shareholders do so in the context of shareholder votes. Of course we need to give shareholders information in that context, because we're asking for their votes. Here, though, we're not asking them for anything; instead, we're just doing something that the terms of their shares, as set out in our certificate of incorporation, give us the right to do. So we don't need to tell them anything. And anyway, if they want to know what the corporation is worth, they can just use their inspection rights.

You admit that you took only the four-hour class, but point out that you were on time for nearly every class, so that you might actually have gotten more class time than you would have in the five-hour class. You then point to *Speed v. Transamerica Corp.* (discussed in the third edition of our casebook at page 347, and in the second edition at page 352) as support for your position. The chair responds
