
CORPORATIONS A PROBLEM APPROACH

SECOND EDITION

Larry D. Soderquist
A. A. Sommer, Jr.

CONTEMPORARY
LEGAL EDUCATION SERIES



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The persons and business entities in the situations in this book are fictional, as are the events described in the situations. Neither the persons nor business entities are intended to represent real persons or entities.

Preface to the Second Edition

Business lawyers are basically planners. Their viewpoint is prospective. It seems useful, then, to present corporation law from the same viewpoint. This book, and the accompanying statutory appendix, are designed to place students in the position of the business lawyer. Each chapter of the book begins with a situation involving one or more hypothetical clients, with later situations building on earlier ones. The book and the statutory appendix together provide references — including statutes, cases, articles, and other materials — that the business lawyer might consult before determining how to proceed. Although the materials were chosen with the presented situations in mind, they were also selected with a view to giving students a good background in the areas traditionally covered in a basic course in the field. Classroom work can involve the situations as much or as little as the teacher wishes. For example, the situations can simply be used, as part of assigned readings, to place the cases and other materials in an understandable context. The approach of the book, then, is not meant to dictate what is to go on in class.

The book is designed to be used in a three or four semester-hour corporation law or business associations course. It touches on general and limited partnerships and other forms of business organization, but focuses on corporations. Some of the securities related materials have been included simply to give students a first acquaintance with a few of the more common securities law questions likely to arise in a corporate practice. Teachers who wish to deal only selectively with these questions, or to save them for another course, will find no difficulty in doing so. Introductions to agency law and to the reading of financial statements are included in appendices. These were designed to be understandable to students with little or no help.

Citations of authority and references of various sorts have been omitted, as have footnotes, except where inclusion or partial inclusion has served a specific purpose. These deletions generally have not been indicated. Other deletions and revisions usually have been, except for the correction of typographical errors and the deletion of paragraph and longer portions of text appearing before or after excerpts from non-case materials, and except for a few miscellaneous deletions and revisions of a minor nature. Where footnotes have been retained, they have been renumbered.

The accompanying statutory appendix contains the various uniform partnership acts, the Model Business Corporation Act, the Revised Model Business Corporation Act, and the Securities Act of 1933 and selected rules, along with portions of the Securities Exchange Act of 1934 and selected rules. Since it is understood that some teachers may wish to focus on a particular state's corporation statute rather than on the Model Act or the Revised Model Act, the situations and reading materials were designed with this in mind. In addition to these statutes and rules, forms of articles of incorporation, by-laws, and minutes of a board of directors' organizational meeting, and a sample stock certificate, are included. An excerpt from a prospectus and various proxy materials also are provided.

Many people helped in the preparation of this book and the statutory appendix, and we gratefully express our thanks to all of them. Particularly, we first wish to thank the students of Professor Soderquist who provided helpful research assistance. We are also grateful to Professor Soderquist's research associate on the first edition, John A. Scanlan, who did a superb job in helping with various aspects of the project over a long period of time. Finally, our special thanks go to Professor J. Kirkland Grant, who read drafts of the manuscript for the first edition, offered numerous helpful comments and suggestions, and provided materials that have significantly enhanced the book and the statutory appendix.

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March, 1986

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CHOOSING THE BUSINESS ENTITY

Situation 1

A business client of yours recommended your firm to William Anderson and Linda Baker, who want to start a business. An appointment was arranged, and at the appointed hour Baker and Anderson enter your office. They explain that their associate, James Phillips, will be a little late. He has been tied up at a directors' meeting but should be arriving soon. Phillips, they say, is an investment banker and also an investor in several businesses.

Baker proceeds to give you some background and explain what she and Anderson have in mind. She is a molecular biologist and for the last several years has worked in a university research laboratory. During this period she has developed a rapid, efficient way to synthesize DNA. She is well known for this and is often asked for advice by other laboratories around the country. Considering the costs involved in tooling up to do DNA synthesis, Baker is convinced that many researchers would be interested in having this done for them under contract. Setting up and running a laboratory to do this work is the first stage in her and Anderson's plan. The second, with which they would proceed as time and money allows, is research toward perfecting a patentable process for introducing disease resistance into plants by means of DNA manipulation. Baker has done preliminary work toward this, but has not wanted to proceed further, since any resulting patent would be the property of her present employer.

She then asks Anderson to talk with you about the business details. Anderson, you learn, is the vice president for finance and administration of a small chemical supply company. As such he is in charge of an office staff and has primary responsibility for managing the company's finances. He expects to handle the business end of the new enterprise. Since Baker will need to spend her time in the laboratory, Anderson plans to handle most contacts with prospective customers, except when Baker's involvement is absolutely necessary. This will be like old times, he says, since his first job with his present company involved calling on customers. He explains that he and Baker will not be able to contribute to the new business anything like the required capital. Together they can raise only about \$75,000. Anderson has been busy searching for a prospective investor, however, and has found Phillips. Phillips is willing to contribute, or guarantee loans for \$200,000 to \$300,000 if the terms are satisfactory.

In the ensuing general discussion, Anderson and Baker also give you the following information:

1. Neither Anderson nor Baker expects to have any substantial source of income other than what they can earn from the new business. Each requires about \$30,000 per year to survive financially.
2. Estimated expenses, for the first year of operation, include:

Equipment and supplies		\$200,000
Salaries:		
Anderson and Baker	\$60,000	
Laboratory technician	20,000	
Clerical help	<u>12,000</u>	92,000