

### Application Questions:

1. A corporation that Jasmine forms with \$100 of capital hires an employee who commits a tort within the scope of employment. The victim seeks to recover from Jasmine.

- a) Jasmine is liable if the tort was foreseeable
- b) Jasmine is liable as the sole owner and controller of the corporation
- c) Jasmine is not liable unless she has given a guarantee to the victim
- d) Jasmine is not liable because this is an ultra vires transaction

2. A corporation is about to issue stock with a par value of \$10. The consideration for which the stock may be issued must be

- a) \$10 or more
- b) exactly \$10
- c) \$10 or less
- d) none of the above

3. Five law professors are the directors of a corporation. Because they must all often travel to conferences, there is a danger that the board may not be able to hold some meetings. Which of the following measures in the by-laws may remedy this?

- a) Low majority
- b) Low quorum
- c) Allowing meetings by conference call
- d) **b** and **c** but not **a**

4. Four friends started and incorporated a business together with equal contributions and share ownership. They enacted an 80% supermajority for shareholder and board decisions. A few years later, the corporation is only involved in running a successful restaurant, under the direction of one of them, who has developed a broad reputation as a restaurant manager. Unfortunately, the same one is voting against all resolutions as a shareholder and director. Why may dissolution be an inadequate equitable remedy?

- a) The manager-shareholder has a right to oppose resolutions
- b) The manager-shareholder's opposition is irrelevant
- c) Dissolution may destroy going-concern value
- d) The manager-shareholder is not truly extorting the rest

5. Leveraged Corp, has \$100 of debt (interest rate 10%) and produces annual profits of \$20, which at the appropriate valuation of 10 times earnings produces a value for the firm of \$200. The equity trades for a capitalization of \$100, the debt for \$100. Buyer Inc proposes the following transaction: Buyer will borrow \$120 from banks at 10% and \$10 from its shareholders (so the sum of its assets will be \$130 in cash) and purchase 100% of Leveraged's common stock for \$130 after which the two will merge.

Does this buy-out constitute a fraudulent transfer?

- a) The transfer to the original shareholders of Leveraged is fraudulent in every case.
- b) The transfer to the original shareholders of Leveraged is fraudulent if the managers of Leveraged do not think that Buyer can produce an extra \$2 or more in annual profit.
- c) The transfer to Buyer is fraudulent if Buyer's managers do not think that they will produce an extra \$2 or more in annual profits.
- d) The transfer to the original shareholders of Leveraged is fraudulent as the managers of Buyer do not believe they can extract an extra \$2 or more in annual profit.

6. Target Inc. has and is expected to continue to have profits of \$20 annually (before interest) and \$100 in debt (with a value on the market of \$100 and debt service payments of \$11 annually). Despite that its managers consider the appropriate P/E ratio for target to be 10, its stock trades for a capitalization of \$50. The management team of Target, Inc., proposes the following transaction. The management team will create Vehicle Corp., by contributing in sum \$5, and they will borrow \$70 from banks with an annual debt service payment of \$8. Vehicle will purchase 100% of Target's common stock for \$75 and the two will merge.

Is this a fraudulent transfer?

- a) Yes because the managers are violating their fiduciary obligations.
- b) Yes because the merged entity's debt is riskier.
- c) No because the merged entity can in good faith service its debt.
- d) No because the merged entity's debt is not riskier.

### **Theory Questions:**

51. Farmer makes \$10 with fences, \$5 without fences (because his farm is trampled by cattle). Rancher makes \$11 without fences, \$5 with fences. Coase would say:

- a) Regardless whether the rule is "owners may fence their land" or "owners may not fence their land," farmer's land will get trampled.
- b) If, in order to have a binding agreement, the parties must notarize it at a cost of over \$1, then the rule should be "owners may not fence their land."
- c) both of the above
- d) neither of the above

52. Dionysus' vineyard is expected to produce \$200 if the weather is outstanding, \$100 if the weather is good, and \$0 if the weather is bad. The weather is outstanding 25% of the time, it is good half the time, and bad the rest of the time. The expected value of the harvest is

- a) \$125

- b) \$100
- c) \$75
- d) \$50

53. Which of the following equations gives correctly the present value of \$85 to be received in 5 years discounted at 12% using annual compounding?

- a)  $85/(1+12)^{5 \cdot 12}$
- b)  $85/(1+.12)^5$
- c)  $85/(1+.12/12)^{5 \cdot 12}$
- d)  $85/(1+.12/2)^{5 \cdot (.12/2)}$

54. A manager in a legal system that has broad fiduciary obligations, compared to one in a system of narrow fiduciary obligations, is likely to

- a) be forced to make more disclosures to the corporation to avoid liability
- b) consider more of the businesses' needs and prospects when making decisions
- c) find it easier to finance corporate ventures
- d) all of the above

55. The traditional justification for par-value statutes was that

- a) it protected creditors by providing a cushion of equity that the shareholders could not distribute as dividends
- b) it protected creditors by clearly stating the value of the corporation's equity
- c) it protected shareholders by providing a cushion of equity that they could not distribute as dividends
- d) it protected shareholders by clearly stating the value of their shares (and equity)

56. The practical importance of par-value was circumvented by

- a) the popularity of stocks with very low par value
- b) the impossibility of compliance
- c) the appeal of stocks with high par-value to investors
- d) the passage of Fraudulent Transfer laws

57. What does the statement "Delaware won the race to the bottom" mean in corporate law?

- a) Delaware offers corporate law which favors managers who use the corporate machinery to have Delaware as their state of incorporation
- b) Delaware offers worse corporate law than other states and its popularity is a puzzle
- c) Delaware was the first to offer easy-going corporate law

d) Delaware's corporate law was the first clearly bad corporate law

58. If Meinhard and Salmon knew ahead of time that Andrews' view of fiduciary duties would apply to their arrangement, they would probably have:

- a) Given Salmon a greater than 50% stake in the partnership
- b) Given Meinhard a greater than 50% stake in the partnership
- c) Opted for a debt contract rather than a partnership to finance the business
- d) none of the above

Answers: cadcdccbbdaaab