

# **BUSINESS ASSOCIATIONS**

## **ANSWER PART A (both questions) AND PART B (1 question).**

Try to show thought and critical analysis of the materials and issues dealt with in the course.

DO read the questions carefully and think about your answers before beginning to write.

DO refer to statutory provisions, cases and other materials where appropriate. If you make general statements, try to back them up with specific references.

DO NOT use abbreviations unless you explain what you are using them to stand for.

DO NOT make assumptions in answering the hypothetical.

DO explain what further information you might need in order to answer the question properly.

DO write clearly.

**You will get credit for following these instructions, and may be penalized for failing to do so.**

## PART A

Xcorp and Zedcorp are corporations incorporated in Arcadia, a state in the US. Arcadia's corporations statute is modeled on the Delaware General Corporation Law.

Xcorp's main line of business is the operation of an online marketplace which originally focused on second-hand clothing, responding to a growing interest in sustainability among consumers. Xcorp now sells a substantial amount of clothing marketed as "vintage," which means it is at least 20 years old, as well as recycled and visibly mended clothing. A growing community of artisans who like to develop new items from recycled clothing and old textiles has joined Xcorp's marketplace. Xcorp has never been involved in the production of any of the items sold through its marketplace. Xcorp's advertising campaigns emphasize its commitment to sustainability and protecting people and the planet.

Xcorp was founded 5 years ago by Arya, Bran, and Cersei, who got to know each other 10 years earlier through their mutual interest in promoting sustainability. They are all shareholders, directors, and officers of Xcorp. Each owns 15% of the common stock, which is the class of stock with voting rights in shareholder meetings. Arya is the CEO; Bran is the Chief Information Officer (CIO) responsible for issues relating to cybersecurity and privacy; and Cersei is the Chief Sustainability Officer.

Three years ago, Yfund invested in preferred stock in Xcorp, and has the right to appoint two directors to the Xcorp Board as a result. Yfund appointed Daenerys and Euron to the Xcorp Board. Both have worked at Yfund for a number of years and are directors of other companies in which Yfund has invested. Gilly, the President of the Arcadia Sustainability Institute, and a long time friend of the Xcorp founders, is the other member of the Xcorp Board. Xcorp has a number of other shareholders who bought their shares in exempt offerings under the Securities Act 1933. There is no public market in Xcorp's common or preferred stock.

At a conference about sustainable fashion, Arya learned about a number of designers who were making beautiful clothing creations from pre-worn designer clothing and surplus fabrics that were never before used in production. Without telling anyone at Xcorp about her new idea, Arya decided to implement the idea for her own benefit and asked Hodor to work with some of these designers to develop clothing items which Arya

planned to sell through Xcorp's marketplace and other similar marketplaces. Arya gave Hodor specific instructions about the criteria she expected the clothing items to meet; Hodor was to report back to her regularly on the progress of the work, and Hodor would arrange to sell the items through the marketplaces Arya designated in return for receiving 15% of the profits generated by the sales. Arya has made significant profits from the sales of these items.

An Xcorp employee informed Cersei that she believed that a substantial amount of the clothing sold through the Xcorp marketplace was not in fact vintage clothing but newly manufactured clothing. Cersei began to investigate and consulted an expert on clothing supply chains who told her that the clothing that is being sold through online marketplaces as vintage clothing is often recently manufactured using chemicals that can cause serious allergic reactions for wearers of the clothing, and in factories where the workers are subject to human rights abuses. The expert identified some competing marketplaces where these problems were significant, including Zedcorp. Cersei informed the Board of Xcorp of what she learned from the Xcorp employee and the expert, but the Board members said they had no reason to believe that these problems affected any of the products sold through their marketplace.

Yfund owned shares in Zedcorp, and these shares are traded on the Arcadian Stock Exchange. Daenerys and Euron informed their colleagues at Yfund of what they learned as a result of Cersei's presentation about her conversations with the supply chain expert, specifically mentioning the issues at Zedcorp. Arya also informs Hodor about Zedcorp's issues. Yfund sells its Zedcorp shares. Hodor passes the information on to his brother, Jon, who sells the Zedcorp shares he owns.

A number of purchasers of clothing through the Xcorp and Zedcorp marketplaces complained to the Arcadian Consumer Protection Authority (ACPA) about allergic reactions they have suffered from contact with allegedly vintage clothing. ACPA began an investigation, and discovered that the firms that manufacture the fake vintage clothing are responsible for inadequate safety controls and also human rights abuses in their workplaces. ACPA found that much of the clothing sold through the Xcorp and Zedcorp marketplaces is affected by these problems and imposes substantial fines on Xcorp and Zedcorp for their false claims about sustainability and protecting people and

the planet. When these fines are announced, the price of Zedcorp's shares declines significantly.

**Answer the following questions, explaining what further facts you would need to know and giving reasons for your answers:**

1. [50 points] What liability do Arya, Bran, Cersei, Daenerys, Euron and Gilly face, based on these facts? If unhappy Xcorp shareholders would like to sue them, what difficulties would they face?
2. [ 25 points] What liability do Yfund, Hodor and Jon face with respect to their involvement in sales of Zedcorp shares?

**PART B** [25 points]

**Answer 1 of the following questions, using examples from the course materials to illustrate your arguments:**

1. Do you think that corporate law should emphasize the establishment of clear standards for directors and officers or the ability to provide remedies for the benefit of shareholders where necessary? How effectively do you think Delaware corporate law achieves either objective?
2. Do the rules of corporate law encourage good business judgment, and/or profit maximization for the benefit of shareholders?
3. Discuss the advantages and disadvantages of treating business organizations as essentially contractual arrangements among their participants.

**Case List**

Gorton v Doty

A. Gay Jenson Farms v Cargill, Inc.

Mill Street Church of Christ v Hogan

Ackerman v Sobol Family Partnership LLP

Watteau v Fenwick

Botticello v Stefanovicz

Hoddeson v Koos

Atlantic Salmon v Curran

Humble Oil v Martin

Hoover v Sun Oil

Murphy v Holiday Inns

Miller v McDonald's

Ira S Bushey & Sons v US

Manning v Grimsley

Arguello v Conoco

Majestic Realty v Toti Contracting

Reading v Regem

Rash v JV Intermediate

Town & Country House & Home Service v Newbery

Fenwick v Unemployment Compensation Commission

Martin v Peyton

Southex Exhibitions v Rhode Island Builders Association

Young v Jones

Meinhard v Salmon

Sandvick v LaCrosse

Meehan v Shaugnessy

Lawlis v Kightlinger & Gray

In Re Fulton

National Biscuit Company v Stroud

Summers v Dooley

Day v Sidley & Austin

Giles v Giles Land Company

Kovacik v Reid

G&S Investments v Belman

In Re El Paso Pipeline Partners LP Derivative Litigation

Duray Developments LLC v Perrin

Elf Atochem North America Inc. v Jaffari

Fisk Ventures LLC v Segal

Netjets Aviation Inc. v LHC Communications LLC

McConnell v Hunt Sports Enterprises

Racing Investment Fund 2000 LLC v Clay Ward Agency, Inc.

VGS v Castiel

Reese v Newman

Haley v Talcott

Walkovsky v Carlton

Sea-Land Services Inc. v Pepper Source

[Frigidaire Sales Corp. v Union Properties Inc.]

A.P. Smith Manufacturing Co. v Barlow

Dodge v Ford Motor Co

Shlensky v Wrigley

Boilermakers Local 154 Retirement Fund v Chevron Corp

Salzberg v Sciabacucchi

Kamin v American Express Company

Smith v Van Gorkom

Francis v United Jersey Bank

Bayer v Beran

Benihana of Tokyo v Benihana

Broz v Cellular Information Systems Inc.

In Re eBay Inc. Shareholders Litigation

Sinclair Oil Corp. v Levien

Zahn v Transamerica

Fliegler v Lawrence

In re Investors Bancorp, Inc. Stockholder Litigation

In Re the Walt Disney Co. Derivative Litigation

Stone v Ritter

Marchand v Barnhill

In re McDonald's Corporation Stockholder Derivative Litigation

Brookfield Asset Management v Rosson

United Food and Commercial Workers Union v. Zuckerberg

Auerbach v Bennett

Zapata v Maldonado

Delaware County Employees Retirement Fund v Sanchez

City of Birmingham Ret. and Relief System v Good

Weinberger v UOP

Kahn v M&F Worldwide

Corwin v KKR Financial Holdings LLC

In Re Mindbody, Inc. Stockholders Litigation

Robinson v Glynn

Doran v Petroleum Management Corp.

Escott v Bar-Chris Construction Corp.

SEC Memorandum of Law in support of Motion for Summary Judgment in SEC v  
Terraform

Halliburton Co. v Erica P John Fund, Inc

West v Prudential Securities, Inc.

Santa Fe Industries v Green

Deutschman v Beneficial Corp

Goodwin v Agassiz

SEC v Texas Gulf Sulphur

Dirks v SEC

Salman v US

US v O'Hagan

Amicus Brief by ICAN in SEC v Panuwat.