Empire College School of Law Student ID_______
Professor McCann
Business Organizations
Final – Spring 2010
Monday, April 12, 2010

ESSAY QUESTIONS – 1 HOUR

1. Zero Corporation, a publicly traded corporation, manufactures pagers. On January 2, 2010, the chairman of the Board of Directors, Amos, learned from Zero's research director that there had been a breakthrough in a manufacturing technique and the production cost of their pagers would be reduced by 50%. That savings equated to an increase in corporation profit of 50%.

Amos shared this information that day with the Board of Directors at a weekly barbeque on the company patio. Martha, a gardener working for an independent landscape company, overheard Amos' revelation about the breakthrough. Martha did not buy stocks herself but she told her brother in law, Barney, what she had heard. Barney then bought 1,000 shares of Zero Corp. stock for $100 a share, its then price on the New York Stock Exchange.

Diane, also a director of Zero, was dating George, who was a director of a rival company, Pagico. She told George about the breakthrough and what it meant for profits at Zero. George then convened his fellow directors at Pagico and they decided to quietly start buying shares in Zero before news got out about the breakthrough. Their plan was to buy 51% of the stock of Zero on the stock exchange and then force a merger with Pagico. To avoid notice, they bought the shares at various brokerages in the names of the individual directors of Pagico and their relatives. Diane also bought 1000 shares at $100/share on January 2.

Larry is an investor. It so happened that he had been studying the pager market and had concluded Zero was a solid company in that industry and was worthy of investment. Like Barney, he bought 1,000 shares of Zero Corp. stock on January 2nd for $100 each.

As the directors of Pagico and their families starting buying the stock, the price began to climb. On January 5th it was selling for $115. On January 10th it was up to $125. At that point, Martha's friend Barney sold his shares, having made a 25% profit in 10 days. Martha got nothing.

On January 12th, the stock fell back to $120, probably as a result of an overall drop in the market that day. On January 13th, at a point when Pagico's directors had secretly bought about 35% of the stock of Zero, corporate counsel at Pagico learned of the plan to acquire Zero. He sent a memo to the directors saying he vaguely recalled from law school that there may be a legal problem with what they were doing. At that point, the directors and their families rushed to sell the stock before their scheme was discovered. Diane learned from George about the corporate counsel memo and she also immediately sold, making $20,000 on her investment. With so many shares of Zero coming on the market at once the price of the stock plummeted. By January 15th, the stock was at $ 50/share.

Larry Loser has lost half of his investment in 15 days. He has consulted you as to his legal options. Does he have any legal rights against Martha, Barney, Amos, Diane, George or the other Pagico directors? Did Pagico violate the law?

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QUESTION 2 – 1 HOUR

JohnCo Corp. is a public corporation registered with the SEC and in the business of manufacturing porta-potties. For 10 years company profits have been flat and Alex, the current president and chairman of the board, was hired to improve the company's return to its shareholders. When Alex was hired, on January 1, 2010, the stock was trading at $5/share.

Alex came up with a five-year strategic plan to increase profits. The plan involved developing a line of sidewalk "Freshen Up" facilities. Built on the porta-potty mold, the Freshen Up would be an oasis for the busy urbanite who could step in, check his or her appearance, apply makeup or whatever, buy cosmetics and such from dispensers and then rejoin the herd on the sidewalk. With the launch of Freshen Ups Alex was optimistic that he could get the stock price up to $10/share by the end of the five year plan.

On June 1, 2010, however, JohnCo. was notified that DeepDu, a competitor, had filed a notice with the SEC that it had acquired 10% of JohnCo and intended to make a tender offer for 42% more of the stock. The tender offer was to be at $6.50 per share.

Alex convened the directors to deal with the notification from DeepDu. JohnCo had three directors, Alex, Mary and Glenda. Alex was a 5% shareholder in the company. Mary and Glenda each owned 20% of the stock. In addition to Alex getting his salary, each director received $150,000 per year as a stipend for serving as a director.

The three believed in Alex's strategic plan and decided that they would try to keep the company out of DeepDu's hands. They sent a notice to their shareholders saying that they felt the offer was inadequate and they urged the shareholders not to tender their shares. Nonetheless, it was soon apparent that JohnCo's other shareholders were not as optimistic and they were selling shares in large numbers to DeepDu. The Board then voted to implement some defensive tactics. First, they declared a dividend of $5/share payable to shareholders of record the day before DeepDu bought its first shares of JohnCo. The dividend would not be paid to any shareholder that sold her or his shares to DeepDu. That dividend was to be financed with a $20,000,000 loan at high interest, creating a large liability for the company. Second, the Board gave themselves Golden Parachutes under which if any of them were discharged involuntarily from the Board, or if the Board was expanded beyond three persons, each of the three directors would receive $5,000,000. Finally, the directors voted to transfer ownership of the mould for the porta-potties to Alex personally, meaning JohnCo could not manufacture if Alex decided to remove the mould.

When DeepDu filed suit to try to enjoin some of the actions of the Board, the Board then decided that the directors themselves should just buy the company. While they litigated with DeepDu over the poison pill measures, Alex and the other directors sent their own tender offer. They were offering a two tier proposal. They would pay $8.00 per share to anyone who tendered their stock, up to 30% of the shares. Anyone who did not tender would be bought out in the second tier at $5/share.

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You have been contacted by Tom and Joan. Tom was one of the shareholders who tendered to DeepDu for $6.50. He had 100,000 shares of JohnCo at before he tendered. Because he was barred from the dividend of $5/share he lost $500,000. Joan has received the current tender offer from the directors and wants to know what to do. What rights does either of them have against the directors of JohnCo?