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Frey, Morris, Jr. & Choper: Cases and Materials on Corporations

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RECENT BOOKS

CASES AND MATERIALS ON CORPORATIONS. By *Alexander H. Frey*, *C. Robert Morris, Jr.*, and *Jesse H. Choper*. Boston: Little, Brown. 1966. Pp. xlv, 1405. \$13.50.

I

This book is one of two new casebooks on corporations to appear since 1959.¹ It will of course, provoke comparison with earlier books, particularly the *Baker & Cary* text,² which has been widely used and has been viewed by some as definitive.³ However, the law of corporations today is sufficiently different from the law of the 1950's to make a new teaching tool essential.

In evaluating this new casebook, it is relevant to note a few of the important recent developments in corporation law. Since 1959, the corpus of "federal corporation law," and the commentary thereon, has grown at an increasing pace. The recognition of private remedies under the federal proxy rules and Rule 10b-5 not only increases the impact of federal regulation, but also reduces the importance of the common-law actions. In addition, the courts recently have begun to re-examine the traditional concepts of corporate control⁴ which were articulated in the classic study by Berle and Means.⁵

Recent years have also brought a rapid and highly significant change in the investing habits of the nation's shareholders.⁶ Shareholdings of mutual funds and pension plans have so increased that fund and plan managers may exercise enormous power not merely over the corporation whose shares they hold, but over the entire economy.⁷ Moreover, in the course of the past seven or eight years,

1. The other is STEVENS & HENN, *CORPORATIONS AND OTHER BUSINESS ENTERPRISES* (1965).

2. BAKER & CARY, *CASES ON CORPORATIONS* (3d ed. 1959).

3. See, e.g., Coker, Book Review, 60 COLUM. L. REV. 747 (1960).

4. E.g., *Perlman v. Feldmann*, 219 F.2d 173 (2d Cir.), cert. denied, 349 U.S. 952 (1955); see Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505 (1965); Bayne, *A Philosophy of Corporate Control*, 112 U. PA. L. REV. 22 (1963); Berle, *The Price of Power: Sale of Corporate Control*, 50 CORNELL L.Q. 628 (1965).

5. BERLE & MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932).

6. Between 1940 and 1966, investment company total assets increased from \$2.1 billion to \$47.3 billion. Stockholdings accounted for most of this increase: from \$1.8 billion to \$41.1 billion. During the same period, noninsured private pension funds increased their shareholdings from \$.1 billion to \$39.7 billion. SEC, *Report on the Public Policy Implications of Investment Company Growth*, H.R. REP. No. 2337, 89th Cong., 2d Sess. 276-78 (1966). In 1940, there were some 300,000 mutual fund accounts; this number had grown to 6.7 million by 1965, owned by some 3.5 million investors. *Id.* at 2.

7. A recent example of such fund power is the MGM proxy contest, involving among others, six funds holding 940,000 shares. The Puritan Fund of Boston, which held the balance of power with 404,000 shares, cast its votes in favor of the incumbents and assured their victory. *Wall Street Journal*, Mar. 9, 1967, p. 2, col. 2. The role of institutional investors in corporate control is increasingly being scrutinized. See BAUM

an unusually large number of state corporation statutes have been modified or rewritten. To be sure, much of the change has been incremental, such as adoption by many states of the Model Business Corporation Act. Yet a few of these statutory changes can fairly be classified as revolutionary.⁸

These developments necessarily affect the contents of the corporations course: the focus of the course will perforce shift from the key Delaware and New York cases to the new statutes, particularly in the discussion of close corporations, control devices, and incorporation formalities. Changes in the classroom approach to the course, however, may prove even more important than the substantive changes. The effort of *Baker & Cary* to expand the student's exposure to financial materials, market information and business trends has continued. Moreover, the growing need to integrate the study of corporations with the related studies of taxation, commercial law, and antitrust law has made problem-oriented teaching especially attractive. The desire by some teachers to present legal issues in a context akin to what the lawyer encounters in practice has accentuated this movement.

II

The organization of *Frey, Morris & Choper* [hereinafter referred to as *F, M & C*] is based on the life cycle of a corporation. It moves from the launching of the enterprise and the issuance of securities, through the study of control, management, and asset distributions, to the problems of dissolution, reorganization, and insolvency. Strangely, no other corporations casebook—at least in recent years—has adopted this altogether logical and workable organization. The first eighteen pages discuss the attributes of various types of business organizations; there is no detailed coverage of partnership and agency, general jurisdictional problems, and related matters. Such restraint is laudable, since corporations casebooks and courses are already overburdened with materials. Since the book is devoted entirely to corporations, and weighs in at some 1400 pages, it might be expected to be thorough, and it is. Moreover, it takes account of recent developments in both litigation and scholarship.

Following the introductory materials, the book deals with the problems of defective incorporation and piercing the corporate veil in the same section. The materials on defective incorporation are

& STILES, *THE SILENT PARTNERS: INSTITUTIONAL INVESTORS AND CORPORATE CONTROL* (1965). An index of the extent of institutional power is total ownership of shares: pension funds and investment companies together held approximately 12% of the total stock outstanding in the United States in 1966. SEC, *op. cit. supra* note 6, at 276.

8. E.g., the Florida Close Corporation Law, FLA. STAT. ANN. §§ 608.0100-.0107 (Supp. 1966); the Ohio "de facto merger" provision, OHIO REV. CODE ANN. § 1701.84 (Supp. 1966).

short and to the point; particularly interesting is a table from an article by Professor Frey which analyzes the defects and the liabilities imposed in some 200 irregular incorporation cases (p. 46). However, I find the section on disregarding the corporate entity somewhat lengthy; a few of the taxicab liability decisions as illustrative cases⁹ together with a note on the subject might have been preferable.

My only serious disagreement with the coverage of *F, M & C* concerns the materials on organization and financing. It would be useful in the corporations course to detail the procedures for organizing and financing a corporation and to establish the importance of advance planning. An eight-page note toward the beginning of the book discusses the formation of a corporation; a two-page note in the second chapter deals with the various forms of corporate securities. The note on formation includes the entire corporate charter of General Electric (a short two and one-half page document) and thus establishes the point that articles of incorporation need not be massive; however, the book does not deal with the more complex articles and by-laws of the usual business corporation, the inclusion of which—together with a provocative problem or two—would have been helpful to the student. Similarly, the inclusion of a problem or an illustration which points out the provisions of various corporate securities and their importance would have been helpful to the student in building a framework for the analysis of control, management, and corporate distributions. *Stevens & Henn* attempted this, quite unsuccessfully in my view, by reproducing *in extenso* the provisions of securities issued by the Consolidated Edison Company of New York. *F, M & C* includes only a short note and a citation of Dewing's classic book on corporation finance.¹⁰ Both of these case-books might have done well to excerpt or summarize the cited pages of that text.¹¹

There is little to criticize in the remaining sections of the book. The issue of securities regulation is introduced early—and desirably so—with what is probably the best casebook treatment of the 1933 Act to date. The cases are well selected, and the organization follows that of Professor Loss,¹² from whose book excerpts are drawn. This coverage contrasts with the comprehensive, but necessarily

9. Two decisions in New York, one unfortunately too late for inclusion in *F, M & C*, summarize the subject well. *Mull v. Colt Co.*, 31 F.R.D. 154 (S.D.N.Y. 1962); *Walkovszky v. Carlton*, 18 N.Y.2d 414, 276 N.Y.S.2d 585 (1966). Moreover, if this subject is to be discussed, it might be well to refer to the broader social implications of limited liability. See, e.g., Sax & Hiestand, *Slumlordism as a Tort*, 65 MICH. L. REV. 869, 913 (1967).

10. DEWING, *FINANCIAL POLICY OF CORPORATIONS* (5th ed. 1953).

11. Perhaps some would object that senior securities are of declining importance as a source of corporate funds. However, they remain of great importance in the organization of close corporations. See generally, Herwitz, *Allocation of Stock Between Services and Capital in the Organization of a Close Corporation*, 75 HARV. L. REV. 1098 (1962).

12. LOSS, *SECURITIES REGULATION* (2d ed. 1961).

dated, treatment of this subject in *Baker & Cary* and with the unusually confusing presentation in *Stevens & Henn*. The section on control devices, which is equally well organized and comprehensive, is introduced by an excellent note that raises some of the current questions about the viability of the corporate democracy model. There is a smooth transition from control devices to section 14 of the 1934 Securities Exchange Act and the proxy rules. The materials on executive compensation are quite contemporary; particularly pleasing is the inclusion of the Koppers "phantom stock plan" decision.¹³ A very complete chapter on corporate distributions to shareholders is introduced by a note that clearly explains the nature of "surplus" and its relation to the payment of dividends (p. 799). The inclusion of this note at the beginning of the chapter should do much to eliminate what has often been regarded as inevitable student confusion on this point. The book concludes with chapters on solvent dissolution and solvent reorganization, and a chapter, not usually found in corporations materials, on bondholders' rights and insolvency.

III

Every casebook author must at some point decide whether he is writing exclusively for students, or for the practicing lawyer as well. These objectives are by no means mutually exclusive; however, excessive focusing on the detailed and complex problems faced by the corporate bar inevitably diminishes the usefulness of the book to students. Less exhaustive notes, primarily keyed to comprehension rather than comprehensiveness, better serve the teacher's needs. *F, M & C* chooses the student oriented approach (Preface, p. vii), and I suspect that the lack of encyclopedic coverage will be disturbing to few teachers and fewer students. Indeed, many—and I include myself in this group—will find *F, M & C* the most teachable of the available corporations books.

A disturbing fact remains, though: corporations casebooks exhibit a remarkable sameness. Despite important differences in currency and organization of materials, the casebooks all deal with the subject as an integrated body of legal doctrine, which is largely independent of the particular problems that regularly arise within that body of law. The corporations course may thus tend to be a rather dull procession of general principles punctuated by an occasional interesting litigation history. Particularly in the second year of law school, only the most highly motivated student is likely to be intrigued by this approach. Moreover, this is not how the corporate lawyer sees his subject. An example from *F, M & C* may illustrate this point: al-

13. *Lieberman v. Koppers Co.*, 38 Del. Ch. 239, 149 A.2d 756 (Ch.), *aff'd*, 38 Del. Ch. 540, 155 A.2d 596 (Sup. Ct. 1959). See Note, *Phantom Stock Plans*, 76 HARV. L. REV. 619 (1963).

though the section on control devices is well edited, the student may not come away with any notion of the relative *uses* and *functions* of voting trusts, agreements, cumulative voting, and share-transfer restrictions. Does he know when, or why, to use one and not the other—the advantages of each? I think, without overstating its virtues, that the problem approach would serve well in this context. For example, in Professor Herwitz's materials on *Business Planning*,¹⁴ the first of six problems addresses, in a highly successful manner, the uses of various control devices. This approach arouses intense student interest; the student is forced to choose among alternatives, to integrate cases and statutes, and to resolve ambiguities in each. Class discussion moves rapidly to a consideration of the various situations which call for the use of each device. There is no reason to limit such a desirable pedagogic technique to third-year courses.

Integration of problems into the teaching materials, unfortunately, is often not so simple a matter as handing out a question to be discussed in connection with the assigned cases. The materials require rearrangement, and considerably more text may be required. Moreover, the use of problems may suggest textual materials not otherwise included. So, for example, a problem on the capital structure of corporations would demand materials more extensive than those presently included in *F, M & C*. In this sense, the problems mold the course; that is as it should be, since the problems are reflective of the lawyer's work and the scholar's research. Of course, unless such problems are carefully delimited, they will raise issues extending beyond the usual boundaries of the course. A problem on dividend payments and corporate distributions would inevitably raise numerous tax questions. Should they be cut off? Is it fair to assume that the student will later learn the answers to these questions in an elective corporate taxation course; and will that course integrate the corporate and tax aspects of dividend policy, or must the student elect yet another course in business planning?

Most corporations casebooks are already too massive to be covered in the allotted class time. If problems and the related additional materials are added, the burden may become impossible. Still, it is fair to ask whether adding these materials, at least in some measure, and eliminating detailed coverage of such subjects as *ultra vires*, watered stock, and defective incorporation might not be an advantageous trade.

I have pursued this line of thought because what is really needed is a new corporations casebook with an inventive and original approach. Of the books now available, however, I consider *F, M & C*—though traditional in approach—to be the best organized, most current, and most easily understood. While wholesale rethinking and

14. HERWITZ, BUSINESS PLANNING (1966).

revision may be necessary to develop materials of the type I envision, *F, M & C*, with some additions, will do at least the next best job of satisfying these objectives.

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