

## **BUSINESS ASSOCIATIONS**

**THREE HOURS.**

**THIS IS A CLOSED-BOOK EXAM.**

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

DO read the question 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 legibly and clearly.

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

Arcadia and Urbania are states in the US.

In 1995, Andrea, Bill and Carey, who originally met when they were JD students at the University of Miami, bought a large plot of land in Arcadia with the intention of building a vacation home there. Arcadia is beautiful, but land was relatively inexpensive there at the time. After buying the land, the three friends hired a local contractor, Della, to build a simple cabin in one corner of the lot, and the cabin was completed by the end of 1996. After the cabin was completed, Andrea, Bill, and Carey stayed there on a number of occasions, sometimes together, and sometimes separately.

Andrea is a partner in a law firm, Lawpartners LLP, which is a limited liability partnership registered in Urbania. Bill is Chief Financial Officer (CFO) and a director of Exsignia, Inc., which is incorporated in Urbania, and which is in the business of organising the provision of health care services. Exsignia's shares are traded on the Urbanian Stock Exchange (USE). Carey is a columnist who writes for the Arcadian Examiner.

Exsignia has been in the habit of using the law firm of Wheel & Deal as outside counsel, but Bill is unhappy with some of Wheel & Deal's recent work. He decides that he would like to have Lawpartners LLP act as Exsignia's attorneys for a planned take-over of Drugco Inc, a drug company incorporated in Urbania and listed on the USE. The proposed take-over is an aspect of Exsignia's current expansion plans. Bill discusses his idea with Andrea, and Andrea recommends that her partner, Fred, who is developing his corporate law practice and wants to move into larger transactions, should act for Exsignia in the proposed merger. Andrea promises that she will keep an eye on Fred. Fred and Andrea issue an engagement letter to Bill without discussing the proposed representation with their partners. Bill signs the letter on behalf of Exsignia without discussing it with anyone else at Exsignia. Unknown to Andrea, and to the other partners in Lawpartners LLP, Fred is in the process of negotiating with Wheel & Deal to become a partner there, and, a few weeks after Bill signs the engagement letter, Fred moves to Wheel & Deal taking a number of associates and two other partners with him. Before he leaves Lawpartners LLP, Fred invests in shares in Drugco. After he joins Wheel and Deal, Fred tells Georgia, one of his new partners, about the proposed acquisition of Drugco, and Georgia invests in shares in

Exsignia. As a result of Fred's move, Lawpartners LLP has very little expertise in the corporate law area.

On one of their trips to the cabin in Arcadia, Bill and Andrea discuss Exsignia's proposed takeover of Drugco. Bill says that he has approached Drugco's management to see if it would be possible for Exsignia and Drugco to agree on merger terms, and he is hopeful that this may be possible because one of his old school friends, Harold, is the CFO and a director of Drugco and has a lot of influence with the Board. Bill also says that his colleagues at Exsignia are unhappy about Fred's departure from Lawpartners. Carey overhears this conversation, and decides to write a column for his paper about mergers in the health care industry as he has been short of interesting topics recently. While the three friends are staying at the cabin, they meet Della, who tells them that she is acting as agent for the owner of a beautiful stretch of land near to the cabin which would make an ideal location for a hotel. The friends visit the property, and later discuss whether they should buy the land together and build a hotel. Bill decides that the land would make an ideal location for a health spa, and as soon as he arrives home he contacts Della to make an offer for the property. At about the same time, and before his column is published, Carey buys some shares in Drugco. On Andrea's return, her partners in Lawpartners LLP tell her that they think she should have been able to prevent Fred's departure and they want her to leave the partnership.

The Board of Directors of Drugco considers Exsignia's approach at a Board meeting. Harold argues that if Drugco refuses to merge with Exsignia and a take-over attempt succeeds, they may all lose their jobs, and the Board very quickly decides to negotiate with Exsignia. The Board decides that it is too early to announce publicly that Drugco is negotiating with Exsignia. The Board delegates the authority to negotiate a merger agreement to Harold, and at a subsequent meeting it quickly approves the draft agreement Harold has negotiated. The merger agreement provides that Harold will be the CFO of the merged firm, with a significantly increased remuneration package, because Bill has decided to leave Exsignia to build and run his health spa with Andrea. Andrea and Bill decide to leave Carey out of the health spa deal as they think he would not be very useful in the business.

The staff at the USE notice some inexplicable price movements in the shares of Exsignia and Drugco, and ask if there is any reason for these movements. When the Boards of the two corporations reveal that they have agreed to merge, shareholders who sold their shares before the announcement are unhappy. The USE initiates an investigation into trading in the two corporations' shares in the period before the revelation of the merger. When the merger terms are announced, a number of Exsignia shareholders are unhappy because they think that the firm is overpaying for Drugco. The Exsignia Board meets and Bill tells the Board not to worry, because there is no risk that any of the directors and officers of Exsignia will be found to be liable for their actions over the merger.

Urbania's corporation statute is based on the Delaware General Corporation Law, and its partnership statute is based on RUPA (1997 version, including provision for LLPs) and contains the following provision:

(a) Subject to subsection (b) of this section, a partner in a registered limited liability partnership is not liable either directly or indirectly by way of indemnification, contribution, or otherwise, for any debt, obligation or other liability of or chargeable to the partnership or another partner or partners, whether arising in contract, tort, or otherwise, while the partnership is a registered limited liability partnership;

(b) Subsection (a) of this section shall not affect the liability of a partner in a registered limited liability partnership for his own negligence, wrongful acts or misconduct or that of any person under his direct supervision and control, or in any circumstances where the partner has notice or knowledge of any negligence, wrongful acts or misconduct and fails to take reasonable steps to prevent or cure the negligence, wrongful acts or misconduct.

Discuss the legal issues raised by these facts.

