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### The Value of Document "Treasure Hunts" in Teaching Transactional Law and Skills

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# THE VALUE OF DOCUMENT “TREASURE HUNTS” IN TEACHING TRANSACTIONAL LAW AND SKILLS

Joan MacLeod Heminway\*

I am Joan Heminway. I am from The University of Tennessee, and I am really delighted to be able to talk to you today about a pretty simple teaching technique that I use—one that I think has far more power than people might give it credit for. What I want to do is, first, walk you through what the teaching technique is. Then, I am going to talk you through some law, because the exercise I am demonstrating has to do with actually applying law. This exercise is not directly used for planning and drafting, although it could be used as a precursor to planning and drafting. Rather, perhaps more importantly, from my perspective, the exercise is geared to teaching students research skills and finding documents. That's what my treasure hunt idea is all about.

I want to talk to you about this exercise because I think it can be used in a lot of different settings. I teach both from an experiential standpoint and from a doctrinal perspective. My courses are almost always a fusion of both, because I practiced for so many years before I began my law teaching career. For example, I teach Business Associations, which is primarily doctrinal, but I use this exercise in that class. On the other hand, I also teach Corporate Finance, which is primarily (the way I teach it) experiential. (There is a doctrinal component to Corporate Finance; it involves the practical application of multiple areas of substantive legal doctrine.)

You can teach using this type of exercise in a large class; you can teach using it in a small class. You can engage in the treasure hunt in class; you can do it outside the classroom. (At this juncture, I feel like I am in Alice in Wonderland or a Dr. Seuss book.<sup>1</sup>) You can do it in a basic class or in an advanced class. The key for me is the beauty of achieving a number of different potential learning objectives with one teaching tool.

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\* Rick Rose Distinguished Professor of Law, The University of Tennessee College of Law. New York University School of Law, J.D. 1985; Brown University, A.B. 1982.

<sup>1</sup> In particular, Alice's many adventures in different settings and the colloquy in *Green Eggs and Ham* come to mind . . . .

You do not have to be an expert to do this. It can be done with very simple doctrine.

What I want to do today, is take you through one of the more complex applications of this teaching tool. We're going to skip right ahead to advanced business entity law and business drafting law. I teach Corporate Finance as a planning and drafting course, and today we're going to use an example from that course. In front of you is a summary of a number of different things. One, background information about the teaching tool itself. Two, an example from a Corporate Finance assignment (a different treasure hunt than the one I'm giving you today). And three, a blog post. Some things for you to take home with you—literally, physically to take home with you, that relate to this.

Before getting into the exercise, let's first talk about the corporate finance law and teaching aspect of it. Several years ago, I presented at a session at this conference on teaching Corporate Finance as advanced contract drafting.<sup>2</sup> As I then noted the overall structure of my course is to introduce the students—who, by that time, have had a course in business associations law—to the instruments of corporate finance (stock, equity, and hybrids) and then to talk them through the basic transactions in which they're used. For me, this course relies heavily on using precedent transaction documents. The focus is on the linkage between law and drafting.

I use this device in this course for several things. First of all, I want to reinforce some things about business entity law, which they've all been exposed to already. I also need to teach them some new business law doctrine. Oftentimes, in advanced classes, the students don't yet have exposure to all the doctrine they need. They have had experience with foundational doctrine, but class meetings and exercises like the one I am demonstrating today, may need to introduce new components of the applicable doctrine.

So, for example, in business associations law, apropos of today's exercise, the students would need to know about stock and debt and, more specifically, they would need to know that corporations may issue common stock or preferred stock and should understand the basics of those instruments. But the student might not have, depending on the courses taken, have actually seen what preferred stock looks like on the page, how it's drafted and implemented, or delved into areas of state

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<sup>2</sup> See Joan MacLeod Heminway et al., *Innovative Transactional Pedagogies*, 12 TRANSACTIONS TENN. J. BUS. L. 243, 243–51 (2011) (*Corporate Finance as Advanced Contract Drafting* portion of panel).

corporate law statutes in which the law gets into some detail relating to that drafting and implementation. My Corporate Finance course can close those gaps, and the exercise we’ll be working on today is designed in part to achieve those planning and drafting goals.

I want to compel my students to look at other areas of law (contract law in particular), along with business associations law, and merge their legal analyses under those different areas of law. This exercise helps students to work toward that goal. Because Corporate Finance is a planning and drafting course, I use this as a way of facilitating the linkage of legal doctrine to skills, while at the same time reinforcing the potential impact of theory and policy. These kinds of exercises can allow an instructor to have a good conversation about doctrine, skills, theory, and policy. Also, as I earlier said, the exercise focuses primarily on research, transaction-related research skills. This is not, generally, case law research, although that is something in which legal counsel also would have to engage as part of corporate finance work.

Today we’re talking about treasure hunts.<sup>3</sup> This isn’t a perfect treasure hunt; what you will be looking for today is not truly hidden. But in other respects, the exercise I am demonstrating today may be described as a game in which each person competes to be the first in discovering something based on written instructions. Now, you do have a writing in front of you (and I normally would use one), but I will ask you to generally overlook the rule that requires written instructions today, because I primarily want you to respond to my oral instructions today.

With that thought in mind, I will first bring you up to speed on relevant legal doctrine. How many of you teach or have taught either Business Associations or Corporate Finance? Okay. About half. I know we also have some commercial law people in the room. As a general rule, faculty members teaching these kinds of business law courses are not frightened off by statutory law. Set forth below is the key statutory provision under the Delaware General Corporation Law of the State of Delaware:

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<sup>3</sup> A treasure hunt is defined as “a game in which each person or team attempts to be first in finding something that has been hidden, using written directions or clues.”

*Treasure hunt*, <http://www.dictionary.com/browse/treasure-hunt> (last visited Nov. 20, 2018).

Every corporation may issue 1 or more classes of stock or 1 or more series of stock within any class thereof, any or all of which . . . may have such voting powers, full or limited, or no voting powers, and such designations, preferences and relative, participating, optional or other special rights, and qualifications, limitations or restrictions thereof, as shall be stated and expressed in the certificate of incorporation or of any amendment thereto, or in the resolution or resolutions providing for the issue of such stock adopted by the board of directors pursuant to authority expressly vested in it by the provisions of its certificate of incorporation.<sup>4</sup>

This provision addresses the designation and establishment of preferred stock. Preferred stock, for those of you who don't teach in this area, is preferred not because people love buying it more than they love buying common stock. Rather, it is preferred because when the company is liquidated, the holders of that stock would come first in terms of getting a payout, or (depending on the definition of preferred stock you're using) if there is an intent to pay out dividends, those dividends usually would be preferred in amount or timing to any dividends on the common stock.

I should note that it's very useful in corporate finance practice for a corporation to have preferred stock around—to have a class of preferred stock authorized for issuance. What's not so useful is setting up the preferred stock terms *ab initio* in the corporation's chartering document.<sup>5</sup>

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<sup>4</sup> DEL. CODE ANN. tit. 8, § 151(a); *see also, e.g.*, TENN. CODE ANN. § 48-16-102(a) (“If the charter so provides, the board of directors may determine, in whole or part, the preferences, limitations, and relative rights (within the limits set forth in § 48-16-101) of: (1) Any class of shares before the issuance of any shares of that class; or (2) One (1) or more series within a class before the issuance of any shares of that series.”).

<sup>5</sup> A corporation’s chartering document is the document filed with the secretary of state of the jurisdiction of incorporation in order to organize the corporation. In Delaware, this document is referred to in the statutes as a certificate of incorporation. *See* DEL. CODE ANN. tit. 8, § 101(a) (“Any person, partnership, association or corporation, singly or jointly with others, and without regard to such person's or entity's residence, domicile or state of incorporation, may incorporate or organize a corporation under this chapter by filing with the Division of Corporations in the Department of State a certificate of incorporation . . . .”). In states adopting the Model Business Corporation Act, this document typically is referred to in the statutes as articles of incorporation. *See, e.g.*, MASS. GEN. LAWS ANN. ch. 156D, § 2.03(a) & (b) (“Corporate existence begins when the articles of organization become effective . . . . The filing of the articles of organization with the state secretary shall be conclusive evidence that the incorporators satisfied all conditions precedent to incorporation and that the corporation has been incorporated . . . .”). In Tennessee, this document is referred to in the statutes as a charter. *See* TENN. CODE ANN. § 48-12-103(a) & (b) (“[C]orporate existence begins when the charter is filed

If a firm’s preferred stock is established that way, the terms are fixed. How would the firm and its legal counsel know in advance what a party wants to buy? They don’t. The law (specifically, state corporate law statutes) takes this into account and effectively says, “Gee, maybe instead of the way stock is normally set up—by putting all of the terms and provisions in the corporation’s chartering document—let’s give some flexibility to the board of directors, to actually establish the terms later.” We call this statutory invention blank check preferred stock. Why? Because it gives the board a blank check on which it can write the terms of the instrument later.

Today’s exercise involves blank check preferred stock, which the above-quoted provision in the Delaware law authorizes (specifically, when it refers to stock with “such voting powers, full or limited, or no voting powers, and such designations, preferences and relative, participating, optional or other special rights, and qualifications, limitations or restrictions thereof, as shall be stated and expressed . . . in the resolution or resolutions providing for the issue of such stock adopted by the board of directors pursuant to authority expressly vested in it by the provisions of its certificate of incorporation.”<sup>6</sup> The statutory language allows the board of directors to establish many different terms and provisions. They’re characterized, listed within the provision; they include things like voting powers.

The board’s resolutions answer various questions relating to the terms and provisions of the preferred stock. Does this preferred stock have the power to vote or does it not? And if it does, on and under what terms and conditions? The terms may also include, for example, things like preferences. How much is this class or series of equity preferred over the common stock and in what areas? If you are dealing with a New York Stock Exchange company, a class of equity security is not preferred unless it’s preferred both as to liquidation and to dividends, for example.<sup>7</sup> In my Corporate Finance course, we unpack in class and talk through some of

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by the secretary of state. . . . The secretary of state’s filing of the charter is conclusive proof that the incorporators satisfied all conditions precedent to incorporation”).

<sup>6</sup> DEL. CODE ANN. tit. 8, § 151(a).

<sup>7</sup>See N.Y. Stock Exch. Listed Co. Manual § 703.05(B), <http://wallstreet.cch.com/LCMTTools/PlatformViewer.asp?selectednode=chp%5F1%5F8&xmanual=%2F1cm%2Fsections%2F1cm%2Dsections%2F> (last visited Nov. 20, 2018) (“In order to be called preference or preferred stock, the issue should be preferred as to dividends and on liquidation.”).

these terms and provisions. The statute supplies a laundry list of what can be done, if the corporation's chartering document authorizes blank check preferred stock. A corporation also can have a semi-blank check preferred stock—a class or series of preferred stock that only gives the board the power to set up certain of the things on the statutory laundry list, fixing other terms or provisions in the charter. We talk through that possibility as well in class meetings.

I mention all of this so that you have an idea of what the board can do. The establishment of terms and provisions of a class or series of stock either can be done within the charter itself, or it can be done by resolution of the corporation's board of directors "by authority expressly vested in it"<sup>8</sup> by the provisions of the charter. Again, that's what the blank check piece of the statute is. By way of contrast, the statutory language that references terms and provisions that are stated in the charter is the traditional way of setting up preferred stock right within the certificate of incorporation (charter) of the firm. But it is the blank check part of the statute that is at issue in the exercise we are doing today.

The board of directors exercises its blank check authority by adopting a resolution or resolutions providing specifically for the designation and issuance of the stock. So, if it's within the authority granted in the chartering document of the firm, the board of directors may have blank check authority to set up the terms and provisions of preferred stock later. And that is what you really want in a lot of corporate finance transactions.

Set forth below is an example of an implementation of the statutory authority under Delaware law to provide for blank check authority in a corporation's certificate of incorporation.

The shares of Preferred Stock of the Corporation may be issued from time to time in one or more classes or series thereof, the shares of each class or series thereof to have such voting powers, full or limited, or no voting powers, and such designations, preferences and relative, participating, optional or other special rights, and qualifications, limitations or restrictions thereof, as are stated and expressed herein or in the resolution or resolutions providing for the issue of such class or series, adopted by the Board of Directors as hereinafter provided.

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<sup>8</sup> DEL. CODE ANN. tit. 8, § 151(a).



Authority is hereby expressly granted to the Board of Directors of the Corporation, subject to the provisions of this Article IV and to the limitations prescribed by the Delaware General Corporation Law, to authorize the issue of one or more classes, or series thereof, of Preferred Stock and with respect to each such class or series to fix by resolution or resolutions providing for the issue of such class or series the voting powers, full or limited, if any, of the shares of such class or series and the designations, preferences and relative, participating, optional or other special rights, and qualifications, limitations or restrictions thereof.<sup>9</sup>

Notice the repetition of the statutory laundry list of terms and provisions. Notice generally how the charter provision matches the statutory provision. It therefore appears that this blank check preferred stock charter provision intends to use the full authority of the Delaware General Corporation Law to provide for blank check preferred stock.<sup>10</sup>

Note also that this charter provision is a hybrid of sorts. It allows for the creation of preferred stock both through terms and provisions included in the charter and through the board's exercise of blank check authority. In other words, the charter-based authority for the establishment of preferred stock allows for the charter to expressly set forth preferred stock terms and provisions or for the board to adopt resolutions providing for preferred stock terms and provisions.

I note that those board resolutions designating the terms and provisions of preferred stock get separately filed with the secretary of state after the board adopts them, just like the chartering document does. So they're available, along with the pre-existing charter, and are searchable when one desires or needs to look at things related to the corporation. I want to be clear that blank check authority doesn't allow the board to cheat and do things in secret, which some people might think. It actually is a very transparent process that anticipates the need for flexibility and

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<sup>9</sup> Amended and Restated Certificate of Incorporation of Eastman Chemical Company, §4.2(a), [https://www.sec.gov/Archives/edgar/data/915389/000091538912000058/exhibit3\\_01.htm](https://www.sec.gov/Archives/edgar/data/915389/000091538912000058/exhibit3_01.htm) (last visited Nov. 20, 2018).

<sup>10</sup> I note that the charter provision includes additional language that one would want to evaluate before making this claim in an unqualified manner.

timeliness in determining preferred stock terms and provisions in various contexts.

It is finally time for the exercise. Here's what I want you all to do. Some of you it looks like have computers. Probably all of you have a phone. I've done this exercise on both, so I believe that you can engage with it either way, and even if you don't remember your Lexis or Westlaw or Bloomberg password. In any case, I would like you to try to find a blank check preferred stock charter provision. This is the treasure hunt part. I'm giving you 10 minutes. It should not take you that long. . . . I want you to be prepared to tell me what you did to find that charter provision (called a certificate of incorporation in Delaware). Then, I want you to tell me, based on the brief synopsis I've given you here, how the charter provision you locate might relate to the general statutory authority for the provision under Delaware law.

So, for example, does the charter provision you have located use the full extent of the Delaware statutory authority? Does it not? Does the charter provision authorize the designation of preferred stock with voting rights? Does it not? Start to think about the individual terms and provisions that this particular firm has included in its certificate of incorporation. It might be useful for you to have my example provision in front of you, since some of you may want to do proximate word searches using, for example, a Boolean tool.

Again, take 10 minutes to locate and analyze a blank check preferred stock charter provision, I will then get back with you to find out what you've found and what you've learned. By the way, this assignment includes the ability to engage in full and open conversation. You may talk with a colleague. You may raise your hand to ask me questions. In any event, I'm going to circulate around the room and just look over your shoulder (which is what I do with the students when I offer this as an in-class assignment). Sometimes I can help them along a little bit by seeing what they have on the screen. So I'm going to wander at least around the perimeter of the room. Just raise your hand if you want to let me know anything or ask me a question.

Audience:                      It's cheating if I use the ones I have from classes, right?

J. Heminway:                Yes, I want you to do the search here, real-time, to simulate student activity. Even if you have blank check preferred stock provisions online that you use for class, please try and do the assignment independently and find your own here.

- J. Heminway: By the way, don't use as your exemplar the Eastman Chemical Company certificate of incorporation because that's the one I have excerpted for you here. It would be pretty easy with the language I gave you, for you to find that one. See if you can find another.
- J. Heminway: Did you find something?
- Audience: Yeah.
- J. Heminway: Good. Be prepared to tell me how you found it and summarize any interesting observations you might have.
- Man: Everything I keep coming up to requires a password or subscription.
- J. Heminway: What searches might you do to get around that? Sometimes using the word “free” works.
- J. Heminway: Did you find anything?
- Audience: Yeah, just a Google search. I don't know the company.
- J. Heminway: That happens sometimes. I have another interesting example of that.
- J. Heminway: Is there anybody who hasn't found an example yet?
- Man: Yeah. Don't worry about me.
- J. Heminway: Keep going, folks. You can share your frustration as well.
- [Broken dialog between participants and J. Heminway about the difficulties encountered while searching.]
- J. Heminway: Doing okay?
- Audience: Mm-hmm (affirmative). I've got one.
- J. Heminway: Do you have things to say about it?
- Audience: It's incredibly long.

J. Heminway: A lot of them are long. I gave you a short one. You can talk about that—how yours is different.

For the last two minutes, since most of you have found relevant provisions, I'm going to display the legal provision—the Delaware statutory authority for blank check preferred stock, on the screen. You may want to use it to see if there's anything interesting for you to talk about with respect to relationship of your provision to the statutory authority. Having the text in front of you might help.

Audience: I've only got about 15 minutes of charge on my phone so I'm conserving it.

J. Heminway: No worries. I'm sure you can contribute anyway.

[J. Heminway gives a notice to wrap up searching.]

J. Heminway: Okay. I hate to break up a good conversation, but you two are the only folks that I saw actually talking about your searches and results. What did you talk about? Did you talk about the assignment?

Audience: We have a nondisclosure agreement.

Audience: We did talk about the assignment, and then we were talking about something else.

J. Heminway: That's fine. I only ask because I do really encourage students to talk, even in connection with their written assignments, because I believe that two people in discussions with each other can do better than one. Most times three can do better even than two, sometimes four, depending on the type of assignment. I wouldn't go beyond five for most group assignments like this. But you could assign this in a larger class, for example, to a pair or to a threesome. And just have them grab people within their classroom “neighborhood” to engage in the assignment. Then you can typically give the students less time because usually they can find things a lot faster.

I know most of you found this within a few minutes—within five minutes from what I could see, going around the classroom. Who's willing to share their search strategy with me? What did you search? Where did you search? Go ahead.

Audience: SEC EDGAR.

- J. Heminway: Okay, SEC EDGAR, which is not a person, right?
- Audience: No, EDGAR is a database for SEC filings because I'm pretty sure that you don't find private stuff easily. And then I picked classes of stock issued and directors, and that was my search.
- J. Heminway: And you searched this on the SEC's website?
- Audience: No, I just typed "SEC EDGAR" and classes of stock issued by board of directors.
- J. Heminway: Within a search engine? Google?
- Audience: Just in whatever browser came up on this phone that I borrowed.
- J. Heminway: Okay. Good, okay.
- Audience: It generated a long list, and then I found the first . . . and Delaware was in my search. ACS Corporation has a provision: "Preferred stock may be issued in one or more series. The board of directors is hereby authorized to issue the shares in such series." And this goes on for multiple screens as to the extent of the authority . . . .
- J. Heminway: So what is . . . the difference? This provision that I showed you has a very general statement of authority, but we know that there is additional language that followed. Is your example a blank check preferred stock provision that gives the board the authority, but also gives the directors instructions?
- Audience: No, it gives them authority to create multiple classes, and they can do different things in different classes, the same things in different classes, different rights in different classes, different rights to subscribe to different classes. They have all these lists of things that directors could do. It's almost like warning the shareholders that the directors can do anything with these blank check shares.

- J. Heminway:            So do you have a thought as to whether that type of drafting (with the very specific provision saying, "In this class we can do this, or in this series we can do that") is better or worse qualitatively than the kind of drafting you see in a more general provision? Or why you might pick one drafting method over the other if—
- Audience:                If I wanted my shareholders not to read it, I would draft it like this.
- J. Heminway:            More detail, harder to read. Okay. Harder to parse, maybe.
- Audience:                I do like the specific proviso that, rather than just saying the board can designate preferred stock, the board can designate some of the shares in a series. So, the directors can have the power to designate the shares in a particular series and ensure that the total number of shares issued isn't more than whatever number of shares of preferred stock the charter authorizes.
- J. Heminway:            Which is what we call the authorized capital. Authorized preferred capital is the maximum amount of preferred stock the corporation can issue.
- Audience:                The maximum number, but that number of shares doesn't have to all be issued at one time, which is not expressly stated there. I like that addition if I'm representing the board and giving them maximum flexibility.
- J. Heminway:            Right, so you might see, for example, language in the charter that provides for designation at one time or at multiple times (e.g., from time to time)—language like that.
- Audience:                Yeah, each such series, whenever the shares might be issued. . . .
- J. Heminway:            Whenever they might be issued.
- Audience:                The language includes a reference to "the foregoing" . . . .

- J. Heminway: I don't like the "foregoing" part. I might strike that. I'm not big on those kinds of ambiguous reference words, but—
- Audience: That's the language that they've got.
- J. Heminway: Okay. Very nonspecific, in my view.  
Other searches and other observations? Yes.
- Audience: So I just Googled directly. I just Googled—
- J. Heminway: And what did you Google?
- Audience: I Googled sample blank check preferred stock provision in a certificate of incorporation.
- J. Heminway: Okay, and what did you find?
- Audience: SEC.gov. And so there were a bunch of SEC.gov—
- J. Heminway: So it didn't send you . . . . Someone else, I can't remember who it was I was talking to, was originally getting webpages that just talked about preferred stock—
- Audience: So I got Ruth's Chris Steak House [Ruth's Hospitality Group].
- J. Heminway: That was one of the top ones in your search.
- Audience: Did you get that one?
- Audience: Yeah.
- J. Heminway: Okay, he's got that, too. So there are . . . the three, four . . . four people with Ruth's Chris. Five. Okay.
- Audience: That's interesting—
- Audience: That firm may have paid more money to advertise on Google.
- J. Heminway: Quite possibly, for their name to come up first.
- Audience: It's an SEC filing.
- J. Heminway: So how is the Ruth's Chris provision drafted? Either as a comparison/contrast with the exemplar I showed you or what you're hearing

- about from your audience peers—e.g., the one that we just talked about?
- Audience:            Well, in the Ruth's Chris provision, there are no words . . . . There's no specific delineation of the voting powers at all. It just talks about powers, preferences, rights, qualifications, limitations, and restrictions.
- J. Heminway:        So think about that. In the context of what I told you about the doctrine, do you have a thought about the utility or lack thereof . . . qualitatively good, bad, et cetera . . . in the language used in the provision that you found, vis-à-vis the language in the one I provided?
- Audience:            I don't. I would love to hear what somebody thinks.
- J. Heminway:        Yes.
- Audience:            So I found one that was actually a Colorado firm: GeoBio Energy.
- J. Heminway:        GeoBio Energy, okay.
- Audience:            And one of the things I liked about it: it actually labeled the text as a blank check preferred stock provision, in the charter.
- J. Heminway:        That's pretty rare to actually find the charter language labeled with the nomenclature that we use to describe it. Descriptive nomenclature. Okay. Mm-hmm. . . .
- Audience:            So it had a provision on issuance that had some general language, but what I liked about it is then it had seven or eight, I guess nine, subsections, and each one dealt with a different type of term or provision.
- J. Heminway:        One on voting, one on—
- Audience:            Yes, voting rights, rights in liquidation, rights for dividends. So from a contract drafting perspective, I like the way it was organized.
- J. Heminway:        You liked it. So what's the danger, though, of expressly laying out things individually, from a contract drafting perspective?



- Audience: It didn't lay out the actual provision. It just laid it out as something the board can address.
- J. Heminway: Okay. What's the danger, and what's the beauty, of articulating these kinds of specifics in a provision like this?
- Audience: It makes it much easier to read but it may be limiting—
- J. Heminway: Okay. Yeah. So this is the conversation you want to have with the students in class. You could just write instead, for example,, "To the fullest extent permitted by Delaware law." Did anybody find an example that does that? No? Okay. Perhaps there's a norm against doing that. You want to use this as an occasion to talk about drafting norms, and how they can be determined by non-experts . . . . If we did a sampling of the search results of an entire class of my Business Associations students (72) or Corporate Finance students (20) and found a bunch of different examples (none of which take that approach), it tells us that there's a norm. There may be some case law underlying that observation that we want to explore.

You also have to deal with, though, the problem that when you list, if you forget something . . . you have a problem. Because the corporation's board then cannot actually designate preferred stock with that particular provision. Why? Because the authority comes from the statute through the charter. If you haven't given the board the authority to create preferred atock with that kind of provision. Voting may often be left off the list of items the board can provide for.

- Audience: Voting is often left off that list because we don't want the board to be able to issue voting preferred stock to Warren Buffett just because he's the only guy with cash and the economy's in the dumps. So we've now constrained the board's power, and when Warren comes knocking, he says, "I want voting control," and they say, "Well we're not authorized to do that. We'd have to go back and change the charter, and that's just . . . well . . . we'd

rather go to some other source of capital to deal with that financing need" . . . . But we constrain the actions of the board when we desire to self-limit our bargaining authority in the same way that an athletic director at a college could say, "I just have to pass on the word that came from the board of trustees and through the president: the football coach is fired. It's not my decision. I just have to announce it." In the same kind of way, we're setting up the directors to be able to say, "No, we're not going to go that route, because we would have to amend the corporation's charter, and that requires a stockholder vote." And from the common shareholder's perspective that's great because they don't want supermajority votes given out to dilute their governance power just because the firm is in trouble financially].

J. Heminway:      You raise a great point, which is that limitations like this can be very purposeful, and a drafter of a certificate of incorporation can put them in extremely consciously with something like that in mind. Limitations can be included in the charter *ab initio* when you actually file to form a corporation. Charters can also be amended, so you can add or to limit blank check preferred in a subsequent amendment of your charter, but those changes require shareholder approval.

Audience:      I'm curious of whether you think this particular limitation is deliberate or inadvertent. The example I found was from a venture capital association and this is their model provision and so forth and so on.

J. Heminway:      The NVCA? Is that . . . did you go to the NVCA website?

Audience:      Yes.

J. Heminway:      How did you find that? What was your search?

Audience:      Through Rutgers University.

J. Heminway:      Okay. So you did a little backdoor.

- Audience: Yeah, but here's the key. Much of the wording is comparable. There are tweaks that are a little bit different, but they are not meaningful. But here's the important distinction. It says that you can issue preferred with rights, powers, and preferences and add qualifications *with respect thereto, as stated or expressed herein, and in the resolution, or resolutions, provided by the series by the board*. So instead of that word *or*, it's *and*, which of course is conjunctive. So have they really-
- J. Heminway: That's beautiful.
- Audience: -hemmed themselves in, that it's the lowest common denominator between. . . .
- Audience: It has to be in both.
- Audience: It has to be in both.
- J. Heminway: It has to be in both.
- Audience: If it's not in one, it's not permitted.
- Audience: It's not valid.
- Audience: That's right.
- Audience: It typically wouldn't be in the charter . . . . They've constrained themselves (the directors), and they're particularly worried about, because they're looking in terms of down round financing, in the venture capital world, the dilution effect and loss of power and loss of control that could happen. So the drafters of the charter want to very carefully delineate the powers, so subsequent rounds can be granted, as it affects them. And they also probably have step-up rates, to be able to fund that down round, and maintain their priority and-
- J. Heminway: So, what if-
- Audience: The NVCA exemplars are a great set of documents, by the way.

J. Heminway:            If you do venture capital work with your students, it's a great website. But *apropos* of this conversation that the two of you are having, we have to be aware that those forms are geared to very specific issues and a very specific type of financing. I don't usually have students who can have the kind of conversation you two just had on your own, in class. It's nice to have an enlightened audience for today, but I talk about those limitations with the students.

Did you have something to add?

Audience:            Well I was just going to say that to make it real, you could use the clip from 'The Social Network, where Zuckerberg's co-founder finds out he just got diluted.

J. Heminway:            I've used that. I've used that. It's very powerful, it's very short. It's the scene where the computer gets slammed down on a desk. It's available free, on YouTube, as a slice of the movie. Thank you for mentioning that. Good suggestion.

Audience:            So my question is, what is your pedagogical goal in doing this? It seems to me that if you're trying to teach corporate law, that this could be very useful. I could see doing this in secured transactions. Go get some security agreement, and let's compare the language. Why would you want it this way? Why would you want it that way? Or are you trying to teach some drafting here? Because if that's the case, then my concern is (and I hate the phrase best practices because I think best practices is just common) that the language the student may find is not necessarily the best—going through the exercise. The way we're engaging the exercise today is as a pre-drafting exercise. You could then layer on top of this a drafting exercise in a particular context that reflects on a conversation that you've had in class about the particular circumstances in which different drafting techniques might be valuable. And that leads me to another point. We've been talking about *conscious* limitations. I can tell you that there are many

*unconscious* limitations. Drafters leaving voting off the list of items that the drafters actually want the board to have when it exercises its authority to issue preferred stock.

J. Heminway: There's a great case on this point in Delaware, for example, if you teach in this area.<sup>11</sup> Among many other things—many other teaching objectives of the case—the opinion notes that the board did not have authority to issue stock with voting rights because there was no provision allowing for voting stock to be issued in that particular company's certificate of incorporation.

Also, as a result of some research I did on the financial crisis, I teach one session near the end of my Corporate Finance course on the use of preferred stock in the financial crisis, as a regulatory tool to help get the United States out of the financial crisis. And I found in one of the charters for one of those companies that the corporation did not have clear authority for the board to designate preferred stock with voting rights. And guess what? It issued preferred stock with voting rights to the federal government. Now, the federal government is probably going to overlook that; the other shareholders are going to overlook that. There's going to be no lawsuit. But that's not a context that we see happen a lot. And so I actually, in a law review article,<sup>12</sup> cite back to that preferred stock issuance, pointing out the provision in the company's chartering document and showing that it's very much like the other case (although not quite as beautiful as an example) . . . .

In this connection, we talk about conscious drafting. We note that, if you pull the exact language out of the Delaware General Corporation Law, at least at the moment that provision is drafted, and use it properly, the blank check charter provision then conveys the full statutory authority. But the use of *and/or* (as earlier discussed) is another interesting aspect of drafting in this area, and I do cover that in my Corporate Finance course

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<sup>11</sup> The referenced case is *Waggoner v. Laster*, 581 A.2d 1127 (Del. 1990).

<sup>12</sup> See Joan MacLeod Heminway, *Federal Interventions in Private Enterprise in the United States: Their Genesis in and Effects on Corporate Finance Instruments and Transactions*, 40 SETON HALL L. REV. 1487, 1492–93 (2010).

also, in connection with drafting convertible debt.<sup>13</sup> But if the and/or distinction came up in this exercise in class, we would also talk about it here, and what *and* versus *or* means in the specific drafting context. *Or* of course, can be inclusive or exclusive, but it gets us back to a contract drafting question, regardless, as to what the language means in context. Just like the matter of listing elements of a board's blank check authority to designate preferred stock, versus taking a more general approach to providing for that authority. (And if we choose to include a list, what's in the list? What characterizes the voting rights if they are in the list? Etc.)

What we come to (in terms of take-aways) at the end of the preferred stock unit in Corporate Finance is that preferred stock is a very flexible tool. This class involves the students picking up a substantial drafting project on their own as the course proceeds, so we do little pre-drafting projects like this along the way. Through the substantial drafting project, they have to produce written provisions that address legal questions (usually I ask them to do three) for the end of the semester. They pick their own projects, whether they involve debt, preferred stock, common stock—their own versions of things that we've covered over the course of the semester or something completely new—and they each have to write a structured memorandum to me that explains why they drafted the provision the way they did, to address the legal questions that arose as they considered how to draft what the client needed. My *Transactions* article on the teaching of this course as a whole covers that assignment, if you're interested in it.<sup>14</sup>

In any event, the treasure hunt exercise we did today would be a precursor to drafting the way I've introduced it today. Finding precedent transaction documents—a number of them—is a great way to start identifying drafting issues and norms. We could weave this exercise into a drafting assignment later in the course. And if you have a 75-minute (or longer) class period, you might be able to do a little bit of drafting on an

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<sup>13</sup> See *Broad v. Rockwell Int'l Corp.*, 642 F.2d 929, 950 (5th Cir. 1981). The *Broad* court writes as follows:

Broad suggests that the use of the conjunctive “and” in Section 4.11 (“shares of stock and other securities and property”) means that in every instance of a merger, the holders of the Debentures would be entitled to receive all three types of property specified above. This might be a plausible construction, but for the fact that it would make meaningless the qualification to that phrase that follows immediately thereafter . . . .

*Id.*

<sup>14</sup> See Heminway, *supra* note 2, at 249–51.

individual provision like this, if (after identifying and discussing multiple precedent documents) you gave the students a subsequent problem, involving real players and a real legal situation that you wanted them to deal with. The class then could compare and contrast the student work product (perhaps in a subsequent class meeting).

Sometimes I will assign an exercise like a treasure hunt to students when I can't be in class. I'll assign one of these and (for a smaller class) ask them to post what they find on TWEN (The West Education Network) or whatever course management website I'm using. We then unpack the results in a subsequent class session. In that session, I'll ask the students the same kinds of questions that I asked you here today, about how they found what they found (how they proceeded with their search).

Speaking of that, did none of you use a database for the treasure hunt? Did any of you use Bloomberg, for example? I thought I heard somebody talking about Bloomberg or—

Audience: I was trying to. I couldn't log in.

J. Heminway: You couldn't log in? Okay.

Audience: But now I've logged in.

J. Heminway: One of the things that I do for my students both in Corporate Finance and in my Advanced Business Associations course is I invite a representative of each of the main law research vendors—one person from Lexis, one person from Westlaw, one person from Bloomberg—to come in and use different transactional tools for doing document treasure hunts. And we do various different things like give them prompts—give the vendors' prompts—to come into class and show the students how to find documents and guidance using their respective products. Different types of preferred stock provisions, different types of debt instruments or provisions within them. . . . Students get that teaching real time.

I used to do electronic (Lexis, Westlaw, and Bloomberg) database training on my own with my students in those courses. It took a lot of time, and I wasn't as expert as some of the vendor representatives are on certain things (including updates to their products). I have now worked

out training sessions led by the vendor representatives during which I can interrupt them at any time and add my own hypotheticals or thoughts to the examples and recommended processes they are teaching. So it has become a collaborative teaching environment, which I find is really useful for the students.

Audience:                      Do you bring them all in at once?

J. Heminway:                 I bring them in on different days. They each get their own individual day. They each get 75 minutes to teach and to interact with the students.

Audience:                      Just an idle thought. I'm wondering if there'd be any value to doing the treasure hunt almost in reverse. Give the students the samples, and then ask them, "What is wrong? What's missing?" before they get exposure to the underlying law.

J. Heminway:                 You clearly can do that, too. In a typical; practice situation, they have to find the precedent document. So, they must have some basis for searching. Although I've sometimes just given the students instructions, for example, to find a blank check stock provision. Just like that, without offering any significant explanation. And sometimes the students will be able to find it, like those of you in this session did. Thanks for playing along with me today. I appreciate your participation, wisdom, and feedback.