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# DELAWARE CORPORATION LAW AND TRANSACTION COST ENGINEERING

Charles R.T. O'Kelley\*

For teachers of the introductory Corporations<sup>1</sup> course, two important themes are unavoidable—the dominant role of Delaware corporate law in the governance of publicly traded American corporations,<sup>2</sup> and the task of turning law students into value-adding professionals.<sup>3</sup> It is surprising, then, that the great majority of introductory Corporations courses currently offered in American law schools do not use or emphasize the Delaware Corporation

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<sup>1</sup> The first course in the business law curriculum at most American law schools is entitled Corporations, Business Associations, or Business Organizations. The exact coverage of these courses differs dramatically from school to school. Some courses focus substantial attention on unincorporated business associations, while others devote little or no attention to them. Some focus significant attention on federal securities law, while others give scant or no attention to that topic. Because a central focus of almost all of these courses is the corporation and the state statutory and judicial rules that comprise corporation law, I herein use the term "Corporations" to refer to all such introductory courses. For survey data concerning the content and structure of the introductory Corporations course, see Robert B. Thompson, *The Basic Business Associations Course: An Empirical Study of Methods and Content*, 48 J. LEGAL EDUC. 438 (1998) (explaining results of survey taken on Corporations courses).

<sup>2</sup> The importance of Delaware law to the teaching of, and scholarship about, corporate law is reflected in the predominant focus on Delaware judicial decisions and institutions that characterize many of the essays in this Symposium on Business Law Education. *E.g.*, William W. Bratton, *Delaware Law as Applied Public Choice Theory: Bill Cary and the Basic Course After Twenty-five Years*, 34 GA. L. REV. 447 (2000); Jill E. Fisch, *Teaching Corporate Governance Through Shareholder Litigation*, 34 GA. L. REV. 745 (2000); Lawrence A. Hamermesh, *Why I Do Not Teach Van Gorkom*, 34 GA. L. REV. 477 (2000); Faith Stevelman Kahn, *Transparency and Accountability: Rethinking Corporate Fiduciary Law's Relevance to Corporate Disclosure*, 34 GA. L. REV. 505 (2000); Ed Rock & Michael Wachter, *Corporate Law as a Facilitator of Self Governance*, 34 GA. L. REV. 529 (2000).

<sup>3</sup> Again, the focus on skills-building and professionalism is evident in the Conference on Teaching Corporate Law panel on that subject, and the resulting essays in this Symposium. *E.g.*, James A. Fanto, *When Those Who Do Teach: The Consequences of Law Firm Education for Business Law Education*, 34 GA. L. REV. 839 (2000); Carol R. Goforth, *Use of Simulations and Client-Based Exercises in the Basic Course*, 34 GA. L. REV. 851 (2000); Therese Maynard, *Teaching Professionalism: The Lawyer as a Professional*, 34 GA. L. REV. 895 (2000); Richard W. Painter, *Professional Responsibility Rules as Implied Contract Terms*, 34 GA. L. REV. 953 (2000).

Code,<sup>4</sup> and that only one casebook<sup>5</sup> appears to present Delaware corporation law as a coherent system, as opposed to intermingling Delaware cases and statutory references into a mosaic that presents state corporate law as simply a series of interesting, cross-jurisdictional, common-law, and statutory solutions or approaches to the central problems facing incorporated firms and their equity owners.<sup>6</sup> Likewise, it is surprising that, while the vast majority of Corporations teachers place at least some emphasis on teaching lawyering skills and relevant theories, there is no indication that such teachers self-consciously consider the teaching of Delaware corporate law as central to that effort.<sup>7</sup>

I have a passionate<sup>8</sup> belief that a very good way to teach Corporations is to structure the course around a core goal—to teach Delaware corporate law systematically—not just bits and pieces of it, but the entire system, much the way we approach the teaching of constitutional law. This Essay is an elaboration of my reasoning and strategies, organized as a presentation and discussion of the core rationales for organizing the course in this way. The first justification flows axiomatically from the following proposition: we create value for many of our students, and harm none, by giving

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<sup>4</sup> Thompson, *supra* note 1, at 444.

<sup>5</sup> CHARLES R. T. O'KELLEY & ROBERT B. THOMPSON, CORPORATIONS AND OTHER BUSINESS ASSOCIATIONS (3d ed. 1999).

<sup>6</sup> This assertion is based on a comparison of the relative focus on Delaware cases and statutes in the leading casebooks, as well as a comparison of the organizational structure and emphases. The O'Kelley and Thompson casebook appears structurally unique in three respects. First, except for a brief introduction of federal securities law concepts, it systematically surveys the nature of the corporation in relation to state corporation law before focusing in detail on issues presented by federal securities law. Second, the coverage of state corporation law is divided so that students develop a complete understanding of the statutory and judicial norms governing publicly traded firms before being exposed to the unique problem illiquidity poses for closely held firms. Third, the chapters primarily emphasizing the interface between state corporation law and the publicly traded corporation are structured to allow a detailed and coherent study not only of the general issues and rules of state corporation law, but also to promote a systematic study of Delaware corporation law. Thus, chapter subpart headings contain specific references to the Delaware corporation code section that students should read in preparation for a particular class. Additionally, each chapter focusing on the publicly traded corporation contains the seminal Delaware cases on all substantive points and is structured to present systematically the entire framework of Delaware corporation law. O'KELLEY & THOMPSON, *supra* note 5.

<sup>7</sup> Thompson, *supra* note 1, at 444-45.

<sup>8</sup> The Teaching Corporate Law Conference was organized around the "passions" in the teaching of corporate law that each participant identified.

them an opportunity to become experts in Delaware corporate law.<sup>9</sup> As discussed in Part I below, I believe there are significant “marketing” reasons—how we present our role as teacher and the role of the introductory Corporations course to students—for adopting this goal or rationale.

The second justification takes as a given that one of our goals is to give students a theoretical understanding of how corporate lawyers create value for their clients, and that a related goal is to begin to equip students with the substantive understanding and skills that good corporate lawyers must have. As discussed in Part II, I submit that training students to be experts in Delaware corporate law provides important building blocks and opportunities to teach the transaction cost engineering role of the value-adding corporate lawyer. This Essay concludes in Part III with a brief discussion of two examples of the use of Delaware corporate law in the basic course.

### I. THE “MARKETING” ROLE OF ASPIRING TO TRAIN EXPERTS IN DELAWARE CORPORATE LAW

Teachers of the introductory Corporations course must deal with three universally recognized phenomena. First, Corporations is viewed by many students as a “bar course.” Thus, while it is usually not a prerequisite for graduation, most law students feel compelled to take it. Second, Corporations is a “business” course. Many of the students who reluctantly take Corporations because they feel they must, will do so with extreme disinterest and with a certainty that they lack the background to do well in the class. Finally, almost all of the students in the class will have experienced a strange transformation sometime during or at the end of their first year of law studies that makes them uninterested in preparing for, or participating in, the bulk of their classes. Instead, they save their energy

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<sup>9</sup> In other words, I am asserting that we who teach Corporations should have a more ambitious goal than simply helping students learn the general principles of corporation law, or systematically teaching the Model Business Corporations Act (M.B.C.A.) or the law of the state in which a particular law school is located. Whatever the value of instruction in general principles, the M.B.C.A., or home-state law, systematic instruction in Delaware corporation law should be a more fundamental goal of the course.

and passion for the courses, particularly advanced courses, in the areas in which they hope to practice, and for extracurricular activities, clinics, externships, and part-time employment.

There are a number of strategies for dealing with students' fear, loathing, and disinterest in the Corporations class. I have probably tried most of them, including giving in and treating it as a bar course designed principally to convey basic understanding of common law, statutory rules, and classic issues that should be spotted by the minimally competent attorney.

My current teaching strategy, however, is to teach the basic Corporations course as an "advanced course" with the goal of motivating as many students as possible to become committed and engaged. Setting as a goal that students will leave the basic course well on their way to becoming experts in Delaware corporate law is an essential part of my strategy. From the first day of class, I tell my students that my goal is to increase the value of their human capital, and that I am going to do this, in part, by giving them a chance to become experts in, and indeed advocates for, Delaware corporation law.<sup>10</sup> I then make a series of empirical assertions that I ask students to challenge as we go through the course.

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<sup>10</sup> The need for corporate lawyers wherever situated to be experts in Delaware law is reflected in the following explanation of the extent to which Arizona lawyers should give legal opinions regarding the corporation law of other jurisdictions:

Opinions of Arizona lawyers are customarily limited to the laws of the State of Arizona, and a lawyer usually does not render an opinion about the organization, existence, and good standing of a corporation formed under the laws of a jurisdiction in which the lawyer is not licensed to practice. In most cases, that opinion is provided by local counsel in the state of incorporation. The Committee recognizes a general exception to this rule in the case of corporations formed under the laws of Delaware as a result of the common choice of Delaware as the state of incorporation. A lawyer rendering an opinion about the status of a corporation formed under the laws of another jurisdiction, including Delaware, should have sufficient knowledge of the laws of that jurisdiction and conduct the due diligence necessary to render the opinion.

State Bar of Arizona Corporate, Banking, and Business Law Section Subcommittee on Legal Opinions, *Report on Rendering Legal Opinions in Business Transactions*, 727 P.L.I.-CORP. 9, 26 (1991).

- *ASSERTION #1. Delaware is the jurisdiction most often chosen for publicly traded corporations or corporations that are likely to become publicly traded.*

Empirically, I can easily show that Delaware is the overwhelmingly preferred jurisdiction of current publicly traded firms.<sup>11</sup> But can I show that this apparent dominance represents current reality as opposed to being a reflection of a past preference that no longer exists? It could be that Delaware is the current leading state of incorporation only because until recently it was the favored state of incorporation for firms making or preparing to make the transition from closely held to publicly held status, but now is being edged out by a different state in the market for corporate charters. I assert that this is not so, but invite and encourage students to verify my assertion with practitioners in the business law departments of Atlanta's leading firms.

Many students have direct or indirect connections with these firms, and within a relatively short time reports come back to class strongly affirming my assertion. Indeed, at least one or more students will report that their firm almost never incorporates clients anywhere other than Delaware.

I now, hopefully, have most students' full attention. I have engaged the intellectual curiosity of many students who came to the class unaware of the unique importance of the little Commonwealth of Delaware. I have also engaged the interest of practical-minded students who are surprised that sophisticated attorneys are interested in the corporate law of Delaware, and, for the first time, begin to think that this course may be something more than just a bar course.

I then make the following additional, related empirical claims:

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<sup>11</sup> See, e.g., David P. Bancroft, *Some Selected Issues in Organizational Sentencing for Environmental Offenses*, 1998 SD19 A.L.I.-A.B.A. 119, 127 n.11 (noting that "60% of Fortune 500 companies are incorporated in Delaware due to lower taxes and tough anti-takeover laws, 280,000 corporations all together"); Richard H. Doppes et al., *Corporate Governance Out of Focus: The Debate Over Classified Boards*, 54 BUS. LAW. 1023, 1055 n.18 (1999) (noting that "currently, about 60% of the Fortune 500 and 50% of firms listed on the New York Stock Exchange are incorporated in Delaware"); Carol Vinzant, *Why Do Corporations Love Delaware So Much?*, FORTUNE, Feb. 1, 1999, at 32, (noting that over half of all Fortune 500 companies are incorporated in Delaware).

- ASSERTION#2-A. *When representing individuals who are forming a business association for which corporate status is appropriate, but which is unlikely to become a publicly traded firm—what I call a “permanent close corporation”<sup>12</sup>—Delaware is still, presumptively, the best jurisdiction in which to incorporate.*
- ASSERTION #2-B. *Assertion #2-A is true whether the permanent close corporation’s principal headquarters will be in California, Georgia, Oregon, Hawaii, or any other American state.*
- ASSERTION#2-C. *Assertion #2-A is true whether the attorney representing the individuals forming the permanent close corporation works in the business department of a large metropolitan law firm, for a general practice firm located in a small town, or in any other practice setting.*

This is a more controversial set of assertions. First, I have not made the empirical claim that Delaware *is*, in fact, the jurisdiction most often chosen, or currently preferred, for incorporated firms that are likely to be permanent close corporations. Instead, I have asserted either that Delaware is the jurisdiction which *should* be chosen for such firms more often than not, or that before choosing the state of incorporation for a permanent close corporation the incorporating attorney should always consider Delaware.

Not all teachers or practitioners of corporate law will agree with either version of this assertion. Indeed, a majority may disagree with both versions on the grounds that they are empirically untrue: While Delaware may offer advantages to publicly traded firms, it

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<sup>12</sup> A permanent close corporation should not be confused with a partnership corporation—a business enterprise that is rationally formed as a corporation, perhaps because of advantageous tax or limited liability rules, even though the investors would have otherwise preferred the governance rules provided by partnership form. The number of partnership corporations currently being formed should be significantly less than the number organized in prior decades because of the limited liability company and the limited liability partnership, both giving closely held firms the advantages of limited liability, partnership-like governance norms, and the unfettered choice between being taxed as a corporation or a partnership. For a discussion of the contracting problems that underlie partnership corporations, see Charles R.T. O’Kelley, Jr., *Filling Gaps in the Close Corporation Contract: A Transaction Cost Analysis*, 87 NW. U. L. REV. 216, 246-47 (1992) [hereinafter O’Kelley, *Filling Gaps*].

does not offer such advantages to most permanent close corporations. I readily acknowledge that my assertions in this regard are not universally shared, to say the least. However, I invite students to use this course as an opportunity to form their own judgments, which can best be done by becoming experts in Delaware law, as they need to be in order to represent publicly traded firms, and to also become experts in competing corporate law systems. The need for this is now apparent to them, for even if my strong assertions are true, a corollary factual maxim must also be acknowledged: Delaware law is not always the best choice for a permanent close corporation.<sup>13</sup> Thus, students must engage in the comparative study of corporate law both to know when or if Delaware law should be chosen for a permanent close corporation, and to know which state of incorporation to select in circumstances where Delaware is not the appropriate choice.<sup>14</sup>

I now raise the stakes further with the following "marketing" assertions:

- *ASSERTION#3-A. Delaware is the presumptive choice for state of incorporation for any to-be-incorporated business association, and because a significant number of lawyers do not realize this or are not experts in Delaware corporate law, students who do realize this and who are*

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<sup>13</sup> Clearly Delaware is the state of incorporation chosen by a significant number of closely held corporations. See Dennis S. Karjala, *An Analysis of Close Corporation Legislation in the United States*, 21 ARIZ. ST. L.J. 663, 671 n.30 (1989) (stating that Delaware hosts not only large public companies but also thousands of close corporations whose true "home" is elsewhere). Still, the majority of lawyers and academics probably believe that the state in which a closely held corporation maintains its principal business headquarters is, presumptively, the appropriate state of incorporation. See, e.g., WILLIAM L. CARY & MELVIN A. EISENBERG, *CORPORATIONS: CASES AND MATERIALS* 98 (6th ed. 1988) ("A corporation with only a few owners . . . will almost invariably incorporate locally, that is, where it has its principal place of business."); Cyril Moscow, *Michigan or Delaware Incorporation*, 42 WAYNE S. L. REV. 1897, 1947 (1996) (maintaining that "[f]or the largest businesses headquartered in Michigan, the overwhelming choice for state of incorporation has been Delaware. . . . For closely held Michigan businesses, it is almost always preferable to incorporate in Michigan to avoid the additional costs and litigation exposure of incorporating elsewhere"); Harry J. Haynsworth, *Special Problems of Closely Held Corporations*, 1991 C688 A.L.I.-A.B.A. 1, 55 ("Except in unusual circumstances, a corporation should be incorporated in the state where it will conduct the major portion of its business.").

<sup>14</sup> Of course, comparative study of corporate law is also necessary with respect to publicly traded firms.



*experts in Delaware corporate law will have a competitive advantage in the marketplace as they practice corporate law.*

- ASSERTION #3-B. *Incorporating in Delaware is a value-adding choice for a significant number of business associations.*

Now I have explained the ultimate reward flowing to students who become experts in Delaware law, assuming that all of my above assertions are true. I have asserted that students can increase the value of their human capital by becoming experts in Delaware law—that they will be able to compete more successfully in the market because of their expertise in Delaware corporate law.<sup>15</sup> Further, I have asserted that the reason this knowledge will create value for them is that it will create value for their clients. I have asserted that the choice of state of incorporation matters,<sup>16</sup> and more often than not the choice of Delaware will add value for the incorporated firm.<sup>17</sup>

What I have initially set out for my students are increasingly broad empirical assertions—that to be successful corporate lawyers, or at least to be more successful corporate lawyers, they must be masters of Delaware corporate law. Hopefully, I now have their attention as we move through the study of corporation law, with a

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<sup>15</sup> Again, I am making the implicit assertion that differences in the quality of attorneys' services will be discernible in the marketplace in a manner that will increase the attorney's return on her human capital. While it is possible that clients cannot directly measure or discern the differences in the quality of attorneys' work—even if such differences have effects, positive and negative, on transaction value—it may be that such differences can be measured by peers and communicated to the market via differences in professional reputation.

<sup>16</sup> I am making an implicit assertion that the state of incorporation matters—that attorneys can create value for firms they represent, at least in some cases, by selecting the optimal state of incorporation. The converse of this proposition would be that attorneys can decrease the potential value of a firm by selecting a less-than-optimal state of incorporation. I make this assertion explicitly when I talk about the role of the attorney as transaction cost engineer.

<sup>17</sup> The reasons for Delaware's dominance in corporate law are commonly described as including the "network benefits emanating from Delaware's status as the leading incorporation jurisdiction, Delaware's proficient judiciary, and Delaware's unique commitment to corporate needs." Ehud Kamar, *A Regulatory Competition Theory of Indeterminacy in Corporate Law*, 98 *COLUM. L. REV.* 1908, 1908 (1998) [hereinafter Kamar, *Regulatory Competition*]. For a handy list of citations to the literature concerning the reasons for Delaware's competitive advantage over other jurisdictions, see *id.* at 1923-28 nn.59-76.

primary emphasis on Delaware cases and the Delaware General Corporation Law. But I have also set the stage for another focus—the comparative study of business associations and the role of corporate lawyers as transaction cost engineers.

## II. THE LAWYER AS TRANSACTION COST ENGINEER

One of my central missions in the introductory Corporations class is to ensure that each student has a basic theoretical understanding of how transactional lawyers create value for their clients in organizing and advising jointly owned business associations. To accomplish this goal, I introduce the central principles developed by scholars in the field of transaction cost economics.<sup>18</sup> I, and others, have written about the application of these principles as lawyers and lawmakers carry out their respective roles in the governance of corporations and other business associations.<sup>19</sup> For the basic course,

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<sup>18</sup> The field of transaction cost economics can be described as an ongoing project dedicated to working out the insights of Ronald H. Coase, most of which are set out in his two seminal works, *The Nature of the Firm*, 4 *ECONOMICA* 386 (1937), and *The Problem of Social Cost*, 3 *J.L. & ECON.* 1 (1960). Modernly, the most influential contributors to the development of transaction cost economics have been Oliver Williamson and Armen Alchian. See OLIVER E. WILLIAMSON, *THE ECONOMIC INSTITUTIONS OF CAPITALISM: FIRMS, MARKETS, RELATIONAL CONTRACTING* (1985) (using transaction cost economics to analyze economic institutions in book dedicated to, inter alia, Ronald H. Coase); Armen A. Alchian & Harold Demsetz, *Production, Information Costs, and Economic Organization*, 62 *AM. ECON. REV.* 777 (1972) (discussing notion of corporation as originating from contractually structured team); Armen A. Alchian & Susan Woodward, *The Firm is Dead; Long Live the Firm: A Review of Oliver E. Williamson's The Economic Institutions of Capitalism*, 26 *J. ECON. LIT.* 65 (1988) (summarizing Williamson's contributions to analysis of firm and providing analytical review of transaction cost theory and its implications).

<sup>19</sup> See Margaret M. Blair & Lynn A. Stout, *A Team Production Theory of Corporate Law*, 85 *VA. L. REV.* 247 (1999) (proposing mediating hierarchy model of corporations); D. Bruce Johnson, *The Quasi-rent Structure of Corporate Enterprise: A Transaction Cost Theory*, 44 *EMORY L.J.* 1277 (1995) (discussing new valuation hypothesis within transaction cost economics); Jason Scott Johnston, *The Influence of The Nature of the Firm on the Theory of Corporate Law*, 18 *J. CORP. L.* 213 (1993) (analyzing revolution in corporate law scholarship that originated with Coase's article); Curtis J. Milhaupt, *Property Rights in Firms*, 84 *VA. L. REV.* 1145 (1998) (examining property rights theory through focus on comparison of United States, Japan, and Korea); Curtis J. Milhaupt, *A Relational Theory of Japanese Corporate Governance: Contract, Culture, and the Rule of Law*, 37 *HARV. INT'L L.J.* 3 (1996) (examining and explaining Japanese corporation through relational theory); O'Kelley, *Filling Gaps*, *supra* note 12, at 216 (discussing gap-filling role of efficiency-minded courts and why contractual gaps are explainable under transaction-cost based theory); Charles R. O'Kelley, *Opting In and Out of Fiduciary Duties in Cooperative Ventures: Refining the So-Called*

however, I do not seek to explore the current empirical and theoretical debates about transaction cost economics. Instead, I hammer home the following basic points.

First, I want to tie my focus on Delaware corporate law to a central tenet of transaction cost economics: transactional or organizational form does matter. The value of a particular business transaction or venture can be affected positively or negatively by the contractual choices made at the formation of the venture.<sup>20</sup> Second, I want my students to see that it is the role of a corporate lawyer to make these crucial organizational choices. If these decisions are to be made in a value-adding way, the corporate planner must understand the "comparative costs of planning, adapting, and monitoring task completion under alternative governance structures."<sup>21</sup> This requires a sophisticated understanding of not only substantive business association law, but also the fundamental tensions present in any business organization and the characteristics and needs of the particular client.

The insights of transaction cost economics identify the economic and behavioral factors that explain why productive activities are most efficiently organized in a particular way. There are three key concepts: bounded rationality, opportunism, and team-specific investment.

"Bounded rationality" describes the nature of investors' cognitive ability. While investors intend to act rationally, there are limits on their cognitive abilities to process accurately all available information about a potential investment decision involving transactions that will continue into the future and, often, for an indefinite period of time.<sup>22</sup> "Opportunism" is self-interest seeking coupled with guile:

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*Coasean Contract Theory*, 70 WASH. U.L.Q. 353 (1992) (taking issue with Johnston's proposed revisions to Coasean contract theory) [hereinafter O'Kelley, *Opting In*].

<sup>20</sup> "The underlying viewpoint that informs the comparative study of issues of economic organization is this: Transaction costs are economized by assigning transactions (which differ in their attributes) to governance structures (the adaptive capacities and associated costs of which differ) in a discriminating way." WILLIAMSON, *supra* note 18, at 18.

<sup>21</sup> *Id.* at 2.

<sup>22</sup> Bounded rationality is the cognitive assumption on which transaction cost economics relies. . . . Confronted with the realities of bounded rationality, the cost of planning, adapting, and monitoring transactions need expressly to be considered. Which governance structures are more efficacious for which types of transactions? *Ceteris paribus*, modes that make large

exploiting informational or positional advantages to extract an unfair share of the gains from joint or team production.<sup>23</sup> "Team-specific investment" is the value of a particular investment that is attributable to a team production activity. Put another way, it is the portion of the value of a particular team member's investment that would disappear if such team member were forced to shift her capital to its next most valuable use.<sup>24</sup>

Bounded rationality and lack of complete information about the future combine to create the central problem that faces all investors in a joint endeavor—how to preserve the ability of the investors, both individually and collectively, to adapt to changed circumstances without creating undue risk that adaptive mechanisms will be used opportunistically.<sup>25</sup> The answer for simple transactions of limited duration is to negotiate a fully contingent contract that specifies *ex ante* how the contractual relationship will respond upon the occurrence of every possible contingency.<sup>26</sup> This contractual response is not efficient for business endeavors involving significant team-specific investment in a venture of long-term duration. Bounded rationality makes it difficult or impossible to presentiate<sup>27</sup> the future to the required degree. As a result, the sum of the *ex ante*

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demands against cognitive competence are relatively disfavored.

*Id.* at 45-46.

<sup>23</sup> [G]enerally opportunism refers to the incomplete or distorted disclosure of information, especially to calculated efforts to mislead, distort, disguise, obfuscate, or otherwise confuse. It is responsible for real or contrived conditions of information asymmetry, which vastly complicate problems of economic organization.

*Id.* at 47-48.

<sup>24</sup> This insight should be credited to both Williamson and Alchian. Alchian and Woodward put it this way: "If a resource can leave a team without cost or loss of its value, Williamson would say it is independent or is not team-specific, or is 'redeployable.'" Alchian & Woodward, *supra* note 18, at 68.

<sup>25</sup> O'Kelley, *Opting In*, *supra* note 19, at 354-56.

<sup>26</sup> See Ian R. Macneil, *Contracts: Adjustment of Long-Term Economic Relations Under Classical, Neoclassical, and Relational Contract Law*, 72 NW. U. L. REV. 854, 862-64 (1978) (discussing classical contract law and discrete transactions) [hereinafter Macneil, *Contracts*]; Ian R. Macneil, *The Many Futures of Contract*, 47 S. CAL. L. REV. 691, 738 (1974) (charting extreme transaction and extreme relational poles noting that at transactional extreme "only the practically unplannable (of which there is little) [is] left unplanned").

<sup>27</sup> "Presentiation" is the essence of attempting to write a fully contingent contract—to "presentiate" is to bring the future to the present. Macneil, *Contracts*, *supra* note 26, at 863 & n.25.

transaction costs<sup>28</sup> incurred in drafting a highly particularized and individualized contract, and the *ex post* transaction costs<sup>29</sup> incurred in attempting to negotiate a satisfactory adjustment to the contract when it subsequently proves inadequate, generally will be substantially greater than the benefits from such approach. Instead, the value of a jointly owned business venture will often be increased if investors operate pursuant to a governance mechanism or structure for their joint endeavor that leaves the consequences of many contingencies unspecified. The preferred structure will provide rules and procedures that determine how both the team and team members are able to adapt to future contingencies when they arise.<sup>30</sup>

This is where the experienced corporate lawyer steps in.<sup>31</sup> As a transaction cost engineer she must create the optimal governance structure for the prospective venturers whom she represents.<sup>32</sup> In

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<sup>28</sup> *Ex ante* transaction costs are "the costs of drafting, negotiating and safeguarding an agreement." WILLIAMSON, *supra* note 18, at 20.

<sup>29</sup> *Ex post* transaction costs "include (1) the maladaptation costs incurred when transactions drift out of alignment . . . (2) the haggling costs incurred if bilateral efforts are made to correct *ex post* misalignments, (3) the setup and running costs associated with the governance structures (often not the courts) to which disputes are referred, and (4) the bonding costs of effecting secure commitments." *Id.* at 21.

<sup>30</sup> "The organizational imperative that emerges in such circumstances is this: *Organize transactions so as to economize on bounded rationality while simultaneously safeguarding them against the hazards of opportunism.*" *Id.* 32.

<sup>31</sup> For a thorough summary of the various ways in which efficient corporate lawyers create value for their entrepreneurial clients, see Ronald J. Gilson & Robert H. Mnookin, *Foreword: Business Lawyers and Value Creation for Clients*, 74 OR. L. REV. 1 (1995).

<sup>32</sup> The following excerpt from Professor Ronald Gilson's path-breaking article explains how corporate lawyers, as transaction cost engineers, create value for their clients.

I suggest that the tie between legal skills and transaction value is the business lawyer's ability to create a transactional structure which reduces transaction costs and therefore results in more accurate asset pricing. Put in terms of capital asset pricing theory, the business lawyer acts to constrain the extent to which conditions in the real world deviate from the theoretical assumptions of capital asset pricing. My hypothesis about what business lawyers really do—their potential to create value—is simply this: Lawyers function as transaction cost engineers, devising efficient mechanisms which bridge the gap between capital asset pricing theory's hypothetical world of perfect markets and the less-than-perfect reality of effecting transactions in this world. Value is created when the transactional structure designed by the business lawyer allows the parties to act, for that transaction, as if the assumptions on which capital asset pricing theory is based were accurate.

carrying out this planning role, the sophisticated corporate lawyer searches for the governance structure that best economizes on anticipated *ex ante* and *ex post* transaction costs.<sup>33</sup>

With this basic background in place, I spend much of the Corporations course elaborating on the relationship of corporation law, and particularly Delaware corporation law, to the corporate lawyer's effort to provide the optimal governance structure for each of the business associations that she represents. The following are the essential premises that I expect all of my students to understand.

PREMISE #1. The corporate lawyer as transaction cost engineer can increase the value of a prospective business association by selecting for it the optimal type of business organization: sole proprietorship, partnership, Limited Liability Company (LLC), limited partnership, or corporation.<sup>34</sup>

PREMISE #2. If corporation form is selected, the corporate lawyer as transaction cost engineer can increase the value of the prospective incorporated business by choosing the optimal standard form governance structure<sup>35</sup>—the body of legislative and

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YALE L.J. 239, 255 (1982).

<sup>33</sup> The sophisticated corporate lawyer's task involves the application of knowledge and judgment in circumstances where limits on the lawyer's rationality and knowledge are both key variables. The problem, which we seek to prepare our students to solve, is formidable. "A complicating factor in all this is that the *ex ante* and *ex post* costs of contract are interdependent. Put differently, they must be addressed simultaneously rather than sequentially. Also, costs of both types are often difficult to quantify." WILLIAMSON, *supra* note 18, at 21-22.

<sup>34</sup> See O'Kelley, *Filling Gaps*, *supra* note 12, at 216, 226-33, 239-42 (discussing features and advantages of various forms of organization).

<sup>35</sup> I use the term "standard form governance structure," rather than the more inclusive term "standard form contract," because one of the central reasons investors adopt corporate form is to avoid use of traditional contracts and resort to judicial enforcement thereof as the principal mechanism for adapting to changed circumstances as they arise. See Macneil, *Contracts*, *supra* note 26, at 885 (stating that governance needs of ongoing relations "have led to the spinoff of many subject areas from the classical, and later the neoclassical, contract law system, e.g., much of corporate law and collective bargaining").

judicial rules that will best economize on the sum of *ex ante* and *ex post* transaction costs.<sup>36</sup>

PREMISE#3. The corporate planner as transaction cost engineer can increase the value of the organization form chosen by knowing when and how to tailor the standard form governance structure chosen. As a corollary to this premise, the corporate lawyer will minimize *ex ante* transaction costs by choosing the standard form governance structure that requires the least *ex ante* tailoring.<sup>37</sup>

PREMISE#4. The corporate planner as transaction cost engineer can increase the value of the incorporated business by effectively advising the board of directors on an ongoing basis concerning directors' fiduciary obligations, and concerning the extent, nature, and limits on their discretion. As a corollary to this rule, the corporate planner can minimize *ex post* transaction costs that will be incurred as the corporation makes post-incorporation adaptive decisions by selecting the state of incorporation that makes the most credible promise to maintain efficient standard form rules. An important part of this promise is the state's assurance that it will update its legislative rules and judicial precedents in a timely and helpful fashion so as to minimize the *ex post* transaction costs

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<sup>36</sup> It is common to refer to state corporation law as providing a "standard form contract." See, e.g., Stephen M. Bainbridge, *Community and Statism: A Conservative Contractarian Critique of Progressive Corporate Law Scholarship*, 82 CORNELL L. REV. 856, 864 (1997) (stating that "corporate statutes and decisions amount to a standard-form contract voluntarily adopted—perhaps with modifications—by the corporation's various constituencies"); Lynda J. Oswald, *Shareholders v. Stakeholders: Evaluating Corporate Constituency Statutes Under the Takings Clause*, 24 J. CORP. L. 1, 15-16 (1998) (stating that "the corporation is a combination of various contractual relationships, with the state's primary role being the creation and provision of a standard form contract").

<sup>37</sup> O'KELLEY & THOMPSON, *supra* note 6, at 162. For a detailed examination of a transaction cost approach to tailoring the standard form governance structure in a closely held corporation setting, see O'Kelley, *Filling Gaps*, *supra* note 12, at 216, 242-53.

associated with ongoing governance of the incorporated firm.<sup>38</sup>

### III. TESTING THE HYPOTHESIS THAT DELAWARE CORPORATION LAW IS PRESUMPTIVELY A VALUE-ADDING CHOICE

I have now laid out the theoretical framework that explains the corporate lawyer's role as transaction cost engineer, and the relationship of that role to state corporation law. Additionally, as set out in Part I, I have asserted that Delaware is the presumptively optimal standard form governance structure. My entire Corporations course constitutes a testing of that hypothesis. We do this by working through the various substantive and procedural issues that constitute the study of corporations, and, where appropriate, by studying where and how Delaware law differs from that of other jurisdictions. And we do this by focusing on the basic governance problems that arise in a business association, first concentrating on the publicly traded firm, and then considering the markedly different considerations faced by permanent close corporations—firms that are not, and do not expect to become, publicly traded. I would need a book to explain all of the ways in which we test the hypothesis in the basic course. So in my remaining space, I will provide two illustrations of how I use Delaware corporate law in this pervasive, foundational way, each of which plays a role in telling one of the many stories that make up my class—the unique Delaware approach to the resolution of midstream power struggles between shareholders and managers.

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<sup>38</sup> See ROBERTA ROMANO, *THE GENIUS OF AMERICAN CORPORATE LAW* 32-37 (1993) (listing legal regime that reduces costs of doing business and guarantee on desirability of state's code as primary concerns of firms); Kamar, *Regulatory Competition*, *supra* note 17, at 1908, 1923-36 (discussing Delaware's competitive advantages); Edward B. Rock, *Saints and Sinners: How Does Delaware Corporate Law Work?*, 44 *UCLAL. REV.* 1009, 1009 (1997) (using case law to study corporate norms).



A. *SCHNELL V. CHRIS-CRAFT INDUSTRIES* AND THE CONFLICT BETWEEN LEGAL RIGHTS AND EQUITY

In all United States jurisdictions, the basic allocation of power and responsibility between shareholders and directors entrusts the management of the corporation's business and affairs to the directors.<sup>39</sup> The primary ownership power assigned to the shareholders is the election of the directors, normally by plurality vote at the annual meeting of shareholders.<sup>40</sup> Under normal circumstances, a corporation holds an annual meeting as scheduled by the board in the exercise of its management power, subject to any scheduling rules contained in the corporation's bylaws. So long as there is harmony between the managers and the shareholders, the annual meeting will be held at a time reasonably contemplated by the shareholders given the corporation's bylaws and past practices, and the current directors' nominees—usually themselves—will be reelected to a new one-year term.<sup>41</sup>

To introduce students to both the corporate form and the unique Delaware standard form governance structure, it is interesting early in the course to explore the relative rights and powers of managers and shareholders when there is disharmony—when a subset of the shareholders wishes to change the corporation's policies by electing a new team of directors. An excellent case to introduce this issue is *Schnell v. Chris-Craft Industries*.<sup>42</sup>

*Schnell* arose from the conflict between the directors of Chris-Craft and a dissident shareholders' group that planned to conduct a proxy contest to oust the current managers. The bylaws set the

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<sup>39</sup> See DEL. CODE ANN. tit. 8, § 141(a) (1991) (stating that "[t]he business and affairs of every corporation organized under this chapter shall be managed by or under the direction of a board of directors").

<sup>40</sup> O'KELLEY & THOMPSON, *supra* note 6, at 156-57, 174-76.

<sup>41</sup> *Id.* at 177-78.

<sup>42</sup> 285 A.2d 437 (Del. 1971). *Schnell* is still considered the seminal case regarding when equity will trump law. See, e.g., Chadwick M. Cornell, *Reits and Upreits: Pushing the Corporate Law Envelope*, 145 U. PA. L. REV. 1565, 1597-98 (1997) (discussing subsequent uses in light of *Schnell*); Dale A. Oesterle & Alan R. Palmiter, *Judicial Schizophrenia in Shareholder Voting Cases*, 79 IOWA L. REV. 485, 528-41 (1994) (showing extensive analysis and application of *Schnell* doctrine); William T. Quillen, *Constitutional Equity and the Innovative Tradition*, 56 L. & CONTEMP. PROBS. 29, 36 (1993) (discussing legal versus equitable remedies).

next annual shareholders' meeting for January 11, 1972. The directors, however, met on October 18, 1971, and amended the bylaws to advance the meeting date to December 8, 1971.

The dissident shareholders, having relied on the meeting date set in the bylaws, were not ready to commence a proxy contest on the accelerated schedule. Accordingly, they petitioned the Delaware Court of Chancery to enjoin the holding of the meeting earlier than previously set in the bylaws. Despite the defendant's assertion that they were acting for legitimate corporate purposes unrelated to the struggle for control, the Court of Chancery found that the directors changed the meeting date to frustrate the dissident shareholders' efforts to mount an effective proxy contest.<sup>43</sup> Despite this finding, the Court of Chancery refused to grant injunctive relief, reasoning that the directors had simply exercised powers granted to them both by the Delaware Corporation Code and Chris-Craft's bylaws.<sup>44</sup>

The Delaware Supreme Court reversed, using the following rationale:

[M]anagement has attempted to utilize the corporate machinery and the Delaware Law for the purpose of perpetuating itself in office; and, to that end, for the purpose of obstructing the legitimate efforts of dissident stockholders in the exercise of their rights to undertake a proxy contest against management. These are inequitable purposes, contrary to established principles of corporate democracy.<sup>45</sup>

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<sup>43</sup> "I am satisfied, however, in a situation in which present management has disingenuously resisted the production of a list of its stockholders to plaintiffs or their confederates and has otherwise turned a deaf ear to plaintiffs' demands about a change in management designed to lift defendant from its present business doldrums, management has seized on a relatively new section of the Delaware Corporation Law for the purpose of cutting down on the amount of time which would otherwise have been available to plaintiffs and others for the waging of a proxy battle."

*Schnell*, 285 A.2d at 434 (quoting Court of Chancery).

<sup>44</sup> *Id.* at 438-39.

<sup>45</sup> *Id.* at 439.

I ask students, how can the Delaware law be efficient if it allows directors to change the annual meeting date under any circumstances? Soon we are exploring the default rules of the Delaware Corporation Code. Section 211(b) provides that the annual meeting of shareholders shall be held "on a date and at a time designated by or in the manner provided in the bylaws."<sup>46</sup> Section 109(a) specifies as a default rule that the shareholders have exclusive power to amend the bylaws, but that they may give the directors concurrent power to amend the bylaws via a provision in the certificate of incorporation.<sup>47</sup>

From consideration of the relevant Delaware statutory provisions, students will correctly surmise that the Chris-Craft certificate of incorporation contained a provision granting directors the power to amend the bylaws. Further, after examining Delaware Code sections 102, 241, and 242, the students will realize that either Chris-Craft's original founders decided to so empower the directors, or the shareholders have consented to such provision via a post-incorporation amendment to the certificate of incorporation.

In the ensuing discussion, students see that the statutory scheme protects the shareholders from any possibility of directors changing the bylaws to manipulate the meeting date, unless the founders or shareholders have created this possibility by granting bylaw-amending power to the directors. Why did the Chris-Craft founders or shareholders create this power? Presumably they created it because it is more efficient to allow the directors, as part of their ordinary management of a corporation, to adapt the bylaws to changed circumstances as needed, than it is to require that the shareholders participate in approving such changes.<sup>48</sup>

Why then should a Delaware court step in and second-guess the directors' use of the very power that the shareholders have either granted or otherwise accepted? We can inject at this point some consideration of the teachings of transaction cost economics. A better drafted grant of authority to directors might have limited

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<sup>46</sup> DEL. CODE ANN. tit. 8, § 211(b) (1991).

<sup>47</sup> "The fact that such power has been so conferred upon the directors . . . shall not divest the stockholders . . . of the power, nor limit their power to adopt, amend or repeal bylaws." *Id.* § 109(a).

<sup>48</sup> See *supra* notes 25-30 and accompanying text.

their meeting-setting or bylaw-amending power to circumstances not involving elections, or to require shareholder concurrence in such circumstances, or otherwise to lessen the likelihood of the directors using their discretion to achieve selfish as opposed to corporate goals. Why were the bylaws not structured in this way? Is it possible that the bylaws are the product of bounded rationality<sup>49</sup>—the failure of the planners to adequately “presentiate”<sup>50</sup> the future? The grant of substantial discretion to Chris-Craft directors, however, was not absolute. The planners knew that if directors used their discretionary powers opportunistically,<sup>51</sup> the corporation or its shareholders might be entitled to equitable relief. In other words, the planners’ decision not to draft fully contingent provisions to eliminate possible opportunism by the directors may have been value-enhancing. The sum of increased *ex ante* drafting costs and the predicted costs of negotiating around the maladaptations likely to result from a detailed set of bylaws crafted to constrain director opportunism would exceed the predicted costs flowing from constraining directors via *ex post* judicial imposition of equitable discretion instead of via explicit contractual limitations.

Thus, our consideration of how the Court of Chancery should have decided this case, and of whether the Delaware Supreme Court is wise to reverse, focuses on the effect this case will have on future users of the corporate form in Delaware. Arguably, users of the corporate form will perceive that overall transaction costs are economized by a system in which Delaware’s Court of Chancery will occasionally engage in judicial second-guessing of directors’ clear abuse of their bylaw-amending power; assured that the Court of Chancery will protect fundamental shareholder governance rights, shareholders will continue granting directors the concurrent power to amend the corporation’s bylaws.<sup>52</sup>

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<sup>49</sup> See *supra* note 22 and accompanying text.

<sup>50</sup> See *supra* note 27 and accompanying text.

<sup>51</sup> See *supra* note 23 and accompanying text (discussing opportunism).

<sup>52</sup> I want students to see the link between judicial decisionmaking and *ex ante* planning. Can the planner expect that judges involved in future litigation between shareholders and managers will make decisions that are intended to ensure that transaction costs are economized? Will the judges involved in future litigation appreciate the incentive effects their decisions will have on future users of corporate form? One of the major advantages of Delaware as a state of incorporation is the judiciary’s keen awareness of the need to provide

In considering the fairness and efficiency of the Delaware approach, I want students to compare it with the provisions of the Model Business Corporation Act (M.B.C.A.), which give directors the power to amend the bylaws unless such power is taken away in the articles of incorporation.<sup>53</sup> This seemingly innocuous difference represents a profound philosophical difference between Delaware law and M.B.C.A.-based statutes regarding who should be presumed to have the power to change the bylaws—the shareholders who are the firm's residual claimants, or the directors?<sup>54</sup>

Students now see the first of many examples of Delaware law providing greater statutory protection for shareholders than do competing jurisdictions. But they also see the first of many examples of the value created by Delaware's constantly updated body of judicial precedents. I provide students with a brief look at subsequent Delaware cases in which shareholders have asked the Court of Chancery to grant equitable protection from directors' use of their management power.<sup>55</sup> I want students to see how useful these cases are to the corporate lawyer in his role as ongoing advisor to the corporation. They provide a rich set of stories of acceptable and unacceptable use of directors' management power.<sup>56</sup> No other jurisdiction provides a similarly comprehensive or constantly renewed and updated body of precedents.

## B. THE ROLE OF SHAREHOLDER CONSENT ACTIONS

After the lessons learned from *Schnell*, I ask students to consider how the standard form corporate governance structure should deal with the following problem. Shortly after the annual shareholders

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predictability and certainty for planners and users of corporate form.

<sup>53</sup> See MODEL BUS. CORP. ACT § 10.20 (1994) (providing for amendment by board of diversity as shareholders).

<sup>54</sup> This is a good opportunity to consider other governance rules that state legislatures could consider. For example, would it be more efficient to provide as an immutable rule that shareholders have exclusive power to amend the bylaws? Or should immutable and exclusive authority apply only to amending the bylaws with respect to the date, time, and location of the annual meeting? No statute provides such protection for shareholders.

<sup>55</sup> *Stahl v. Apple Bancorp.*, 579 A.2d 1115 (Del. Ch. 1990); *Blasius Ind. v. Atlas Corp.*, 564 A.2d 651 (Del. Ch. 1988); *Aprahamian v. HBO*, 531 A.2d 1204 (Del. Ch. 1987).

<sup>56</sup> For a rich account of Delaware's use of stories to communicate the rules of the game, see *Rock*, *supra* note 38.

meeting of Techno Corporation, the shareholders learn that Techno's chief executive officer and several board members are being investigated for possible serious violations of federal technology transfer restrictions. Suppose a majority of the shareholders would like to remove the current directors from office immediately, rather than allow them to continue in office for nearly a year. What options are available to the shareholders? To answer this simple hypothetical, students must explore the statutory provisions that govern the election and removal of directors, and the calling of annual and special meetings of the shareholders.

In Delaware, as in all United States jurisdictions, the normal or default rule provides that directors are elected at the annual meeting of shareholders for terms that run until the next annual meeting.<sup>57</sup> It is the responsibility of the corporation's managers to call the annual meeting.<sup>58</sup> If the managers fail to do so within thirty days of the scheduled date, or within thirteen months after the last held annual meeting, whichever is later, then any shareholder may petition for mandatory injunctive relief, and it can be expected that the Court of Chancery will summarily order that the meeting be held.<sup>59</sup>

As students assess the statutory rules governing annual meetings in the context of the Techno hypothetical, they realize that this mechanism will not work to the advantage of the majority shareholders. There is no likelihood that the current managers will call an annual meeting any sooner than legally required. Thus, if the shareholders' only removal option is use of the annual-meeting mechanism, then the majority shareholders will be forced to put up with the current managers for at least another year.

We then consider the possibility of earlier removal of the directors via a special shareholders' meeting. The default rule in Delaware allows removal of one or more directors, with or without cause, by simple majority vote of shareholders.<sup>60</sup> The obvious venue for a shareholder vote to remove the directors would be a specially

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<sup>57</sup> Delaware Code title 8, sections 211(b) and 141(b) combine to give us this rule.

<sup>58</sup> The power to call the annual meeting flows from Delaware Code title 8, section 141(a), and the directors' general supervisory authority. Responsibility flows from authority.

<sup>59</sup> DEL. CODE ANN. tit. 8, § 211(c) (1991).

<sup>60</sup> *Id.* § 141(k).

called meeting of the shareholders. In Delaware, a special meeting of the shareholders "may be called by the board of directors or by such person or persons as may be authorized by the certificate of incorporation or the bylaws."<sup>61</sup>

Considering this framework, we can see a shareholder, even a majority shareholder, has no statutory power to call a special meeting of shareholders. Unless Techno's certificate of incorporation or bylaws contain a provision granting such power, the majority shareholders are again without power to replace the directors before the next annual meeting.

A comparison of Delaware law and the M.B.C.A. is instructive at this point. Under the M.B.C.A. rule, the holders of at least ten percent of a corporation's voting shares are entitled to demand that a special meeting of the shareholders be held.<sup>62</sup> The M.B.C.A. rule would empower Techno's dissident shareholders to demand a special meeting for the purpose of removing and replacing the shareholders. Many students will assume that this provision is superior to Delaware's approach in that it better protects the interests of majority shareholders by enabling them to effect an immediate change in control, rather than waiting for the next annual meeting of shareholders.

I first challenge this conclusion by asking students what will happen if the directors refuse to call a special meeting demanded by the holders of at least ten percent of the corporation's shares. At this early point in the semester, students are still startled to realize that the shareholders must look to the directors to call the meeting. Shareholders simply have no management power to act even to the limited extent of calling the meeting. Therefore, if the directors refuse the shareholders' demand, the shareholders will be forced to seek mandatory injunctive relief. Under the M.B.C.A., a petition for such relief is in order if "notice of the special meeting was not given within 30 days after the date the demand was delivered to the corporation's secretary. . . ."<sup>63</sup> And, when notice of a special meeting is given, such notice must specify a time and date for the meeting

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<sup>61</sup> *Id.* § 211(d).

<sup>62</sup> MODEL BUS. CORP. ACT § 7.02(a)(2) (1994).

<sup>63</sup> *Id.* § 7.03(a)(2).

that is "no fewer than 10 nor more than 60 days before the meeting date."<sup>64</sup> So, without violating its legal obligations, the current board of directors may wait thirty days after receipt of a proper demand before giving notice of that meeting, which can be scheduled for as much as sixty days after the notice date. Thus, under the M.B.C.A. framework, the majority shareholders cannot hope to effect a replacement of the current directors via a specially called shareholders' meeting for at least ninety days.

It may still appear that the M.B.C.A. approach is at least somewhat more protective of majority shareholder rights than is the Delaware framework. I now ask students to consider the impact of Delaware Code section 228, which in pertinent part provides:

[A]ny action required . . . to be taken . . . or any action which may be taken at any annual or special meeting of . . . stockholders, may be taken without a meeting, without prior notice and without a vote, if a consent or consents in writing, setting forth the action so taken, shall be signed by the holders of outstanding stock having not less than the minimum number of votes that would be necessary to authorize or take such action at a meeting [at which all shareholders were present] shall be delivered to the corporation.<sup>65</sup>

I next ask students to rethink their initial view that the M.B.C.A. framework is more efficacious. Viewed from the perspective of disenchanted majority shareholders, Delaware Code section 228 is a far superior device for effecting a change of control than is reliance on the ability to call a special shareholders' meeting. Additionally, we can now question whether the M.B.C.A. default rule empowering holders of ten percent of the voting shares to call a special meeting is a value-adding rule as compared to the Delaware rule giving no meeting-calling rights to shareholders, but empowering a majority of shareholders to act without a meeting by written consent. It can

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<sup>64</sup> *Id.* § 7.05(a).

<sup>65</sup> DEL. CODE ANN. tit. 8, § 228(a).



be argued that the Delaware approach makes an efficient distinction between the rights that should be given to an already formed majority group of shareholders (the right to act immediately and without need for a meeting) and the rights that should be given to minority shareholders (the right to an annual opportunity to participate in a democratic dialogue with other shareholders). In contrast, the M.B.C.A. approach treats minority shareholders and coalesced majority shareholding blocks identically, allowing both types of shareholders to call a special meeting via a demand joined in by holders of ten percent of the voting power, but denying majority shareholders an effective device for causing an immediate change in the makeup of the board of directors.

#### IV. CONCLUSION

The foregoing provides a brief look at why and how I build my introductory Corporations course around Delaware corporate law. The discussion in Part III is replicated day after day as we move from a basic introduction to the statutory norms that define the relative rights and duties of shareholders and managers, to a detailed look at the role of shareholder litigation and fiduciary duty, and, finally, to a comparison of the rules governing publicly traded corporations, and the numerous alternative approaches to the problem of the non-publicly traded corporation. By the end of the course, I am able to certify that most of my students are well on the way to becoming experts in Delaware corporate law and competent transaction cost engineers. For those who wish to improve their mastery, I offer advanced courses in Mergers and Acquisitions, Corporate Governance, and Corporate Law Appellate Litigation. These courses, too, are designed to enable students to increase their appreciation of the lawyer's role as transaction cost engineer and of the value added by Delaware corporate law. At the very least, I am confident that this approach provides students with a coherent, comprehensive understanding of the basic principles of business association law. I am hopeful, however, that for many of my students, this approach will provide a significant, if only viscerally measurable, increase in the value of their human capital as prospective business planners, litigators, or entrepreneurs.