

UNIVERSITY OF PENNSYLVANIA

Deals:

The Economic Structure of Transactions and Contracting

LAW 720/MGMT 717

Spring 2010

Provisional Syllabus

Mondays and Wednesdays 3:00 to 4:20 PM
Law School classroom S-245A

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This course will focus on the creation of value through transaction and contract design. The goal of the course is to explain both how private parties actually order their commercial interactions and to develop a systematic theory of how they ought to do so.

The first fifteen or so classes will be devoted to barriers to transacting-including information problems and strategic behavior-and a range of responses. In the final ten classes, student teams will apply the tools developed in the first part of the course to a series of real transactions. This syllabus covers the first of these parts in detail. The second part will be described in a separate memorandum.

Required reading: Course packet and handouts

Grading bases: Class participation, assigned problems, a group presentation, group paper

You may work alone or in pairs on all homework problems.

REGULAR ATTENDANCE IS EXPECTED

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Class 1 (January 13)
Introduction

No Reading

CLASS WILL NOT MEET ON JANUARY 18 DUE TO MARTIN LUTHER KING DAY

Class 2 (January 20)
Value Creation Through Transactional Structuring and Contracting

The Merger of Hewlett-Packard and Compaq (A): Strategy and Valuation.
HP - Compaq Summary Term Sheet
HP - Compaq Merger Agreement, Article I.

Class 3 (January 25)
Negotiation: Creating Gains versus Dividing Them Up

Robert Mnookin, Scott Peppet, and Andrew Tulumello, *The Lawyer as Negotiator* Chapter 1.

Negotiation Case to be handed out in Class

Class 4 (January 27)
The Modigliani-Miller Theorem

"Schools Brief - Unlocking Corporate Finance", *The Economist* 81-82 (December 8, 1990).
Stephen Ross, Randolph Westerfield & Jeffrey Jaffe, *Corporate Finance* 417 (7th ed. 2005).
Peter Huang and Michael Knoll, "Corporate Finance, Corporate Law, and Finance Theory", 74 *S. Cal. L. Rev.* 175 (2000), pages 177-80.
Robert Bruner, *Applied Mergers and Acquisitions*, pages 531-38.
Josh Levin, "Bullpen Market" (A minor-league pitcher named Randy Newsom is selling shares of his future earnings. Should I invest?)

OPTIONAL

Ross, Westerfield, and Jaffe, *Corporate Finance*, "Capital Structure", pages 402-09

Class 5 (February 1)
Informational Asymmetry: Adverse Selection I

HP - Compaq Merger Agreement, Articles II and III.

Paul Milgrom & John Roberts, *Economics, Organizations and Management*, pages 149-151.

Recommended: George Akerlof, "The Market for Lemons: Quality, Uncertainty and the Market Mechanism," 84 *Quarterly Journal of Economics* 488 (1970).

Problem to be handed in: Real Estate Deal with Free Look Clause

Class 6 (February 3)
Informational Asymmetry: Adverse Selection II

Ronald Gilson, "Value Creation by Business Lawyers: Legal Skills and Asset Pricing", 94 *Yale L.J.* 239, pages 269-280 (1984) ("Value Creation").

James Freund, *Anatomy of a Merger*, pages 242-248 (1975).

Grumman v. Rohr, 748 F.2d 729 (2d Cir. 1984).

Class 7 (February 8)
Agency Costs: Moral Hazard I

Paul Milgrom & John Roberts, *Economics, Organizations and Management*, pages 166-75, 179, 183-84, 185-88.

HP - Compaq Merger Agreement, Articles IV, VI, VII and VIII.

Illinois Lottery Sale

Class 8 (February 10)
Agency Costs: Moral Hazard II

Ronald Gilson, "Value Creation", pages 280-293.

Ronald Gilson and Reiner Kraakman, "Mechanisms of Market Efficiency", 70 *Va. L. Rev.* 549, pages 613-621 (1984).

Paul Milgrom & John Roberts, *Economics, Organization, and Management*, pages 259-269.
Hotel Management and Ownership.

Problem to be handed in: *San Francisco Luxury Hotel Development.*

Class 9 (February 15)
Asset Specificity I

A Quick Introduction to Transaction Costs and Asset Specificity.
Paul Milgrom & John Roberts, *Economics, Organization, and Management*, pages 133-40.
Levi's-Designs Joint Venture Part I.

Problem to be handed in: Pay or Play, Take or Pay.

Class 10 (February 17)
Asset Specificity II

Levi's-Designs Joint Venture Part II: Rights of First Refusal (Be prepared to answer questions at end of the case-do not hand in).

Problem to be handed in: Miami Dolphins Case Study: Right of First Refusal (Again, you may work alone or in pairs).

Class 11 (February 22)
Taxation

Myron Scholes et al., *Taxes and Business Strategy*, pages 1-8, 118-27, 130-32.
Guy Baehr, "NJ Transit Getting Foreign Firms to Pay the Fare: Overseas lease-back tax shelters proving profitable for agency", *The Newark Star Ledger*, July 25, 1995.
Andrew McIntosh, "Governor in the Jet-Lease Business", *Sacramento Bee*, January 3, 2006.
Bob Turner et al., "Transfer Pricing Gets More Scrutiny", *Financial Executive*, May 1, 2004.
"Explanation of Calculations in PAI Leasing Example."

Class 12 (February 24)
Inefficient Markets: Accounting

Richard Brealey, Stewart Myers and Franklin Allen, *Principles of Corporate Finance* (chapter 13) (skim).

R.B. Matthews, "The Case Against Stock Options", *Toronto Star*, September 14, 1998.

Burton Malkiel & William Baumol, "Stock Options Keep the Economy Afloat", *Wall Street Journal*, April 4, 2002.

Ruth Simon, "With Options on the Outs, Alternatives Get a Look - Companies Begin to Test Other Compensation Plans As Expensing Gains Traction", *Wall Street Journal*, April 28, 2004.

Rick Munarriz, "Intro to 'Accretive to Earnings'", The MotleyFool, October 10, 2000, available at <http://www.fool.com/research/2000/foolsden001010.htm>.

Brett Nelson, "Trick or Track?", Forbes.com, December 13, 1999, available at <http://www.spinoffadvisors.com/articles/forbes121399.htm>.

Class 13 (March 1)
Contingent Contracts

Paul Milgrom & John Roberts, *Economics, Organization, and Management*, pages. 240-241.

Robert Bruner, *Applied Mergers and Acquisitions*, pages 609-22.

Problem: Contingent Compensation Problem: Sports Apparel Licensing (Be prepared to answer the questions in class).

Problem to be handed in: Sale of a Regional Brewer.

Class 14 (March 3)
Capital Structure

Paul Milgrom & John Roberts, *Economics, Organization, and Management*, pages 505-507.

Bengt Holmstrom and Jean Tirole, "The Theory of the Firm III. Capital Structure," in Richard Schmalansee and Robert Willig, eds., *Handbook of Industrial Organization I*, pages 79-86.

Marriott Spinoff (A) (For this case, please be prepared to answer the following questions in class: (a) If you were on the board of Marriott would you have approved this transaction? (b) why or why not?).

Problem to be handed in: Goodyear Tire & Rubber.

**CLASS WILL NOT MEET ON MARCH 8 OR MARCH 10 DUE TO SPRING
VACATION**

Classes 15-26 (March 15 through April 21)
The Deals