

UNIVERSITY OF PENNSYLVANIA

Deals:

The Economic Structure of Transactions and Contracts

LAW 720/MGMT 717

Spring 2015

Mondays and Wednesdays 3:00 to 4:20 PM

Law School room TBD

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This course will focus on the creation of value through transaction and contract design. The goals of the course are to explain how private parties structure and negotiate their commercial interactions, to discuss theories of how they ought to do so, and to give students a thorough understanding of the deal-making process.

The first two months will be devoted to discussion of barriers to transacting -- including information problems and strategic behavior -- and a range of techniques to respond to them as well to other practical aspects of the deal process. In this first part, student teams will also be assigned to follow a one of a group of currently pending transactions. In the final six weeks of the course, (different) student teams will apply the tools developed in Part I to a series of recent and particularly interesting completed transactions. This syllabus covers the first of these two parts in detail. The second part will be described once the semester is underway.

Required reading: James C. Freund, *Anatomy of a Merger: Strategies and Techniques for Negotiating Corporate Acquisitions*, course materials on Canvas and in the syllabus and handouts.

Grading bases: Class participation (50%--25% Part I, 25% Part II), assigned problems (10%), two short papers or one longer one (20%), and two group presentations (10% each).

REGULAR ATTENDANCE IS EXPECTED

YOU MAY WORK ALONE OR IN PAIRS ON ALL HOMEWORK PROBLEMS.

HOWEVER, THE INDIVIDUAL PAPERS MUST BE INDIVIDUALLY WRITTEN.

NB: THIS IS A DRAFT SYLLABUS WITH A NOVEMBER DATE. IT REPRESENTS A PLAN BUT NOT A PROMISE

Class 0 (January 11)
LAW STUDENTS ONLY—WHARTON TERM NOT YET COMMENCED
Some Economics Background

Schools Brief - Unlocking Corporate Finance, *The Economist* 81-82 (December 8, 1990).
Stephen Ross, Randolph Westerfield & Jeffrey Jaffe, *Corporate Finance* 417 (7th ed. 2005).

The readings below for Class 0 are strictly optional, but deeply thought provoking:

Ronald H. Coase, *The Nature of the Firm*, 4 *Economica* 386 (1937).

Ronald H. Coase, *The Problem of Social Cost*, 3 *Journal of Law and Economics* 1 (1960).

Franco Modigliani and Merton H. Miller, *The Cost of Capital, Corporation Finance and the Theory of Investment*, 48 *American Economic Review* 261 (1958).

Class 1 (January 13)
Introduction

Josh Levin, *Bullpen Market*, (A minor-league pitcher named Randy Newsom is selling shares of his future earnings. Should I invest?)

A Note on Implied Warranties

Potato Chip Supply Agreement (How might you modify this agreement if you represented a major national snack food company and wanted supplier to be a major supplier to you of potato chips?)

Class 2 (January 20)

The Reverse Modigliani-Miller Theorem, Part I teams setup, and an introduction to mergers and acquisitions

Pfizer-Wyeth Merger Agreement, January 25, 2009 [any would do, this one is the handiwork of Casey Cogut, L '73] (skim Article I)

Peter Huang and Michael Knoll, *Corporate Finance, Corporate Law, and Finance Theory*, 74 *Southern California Law Review* 175 (2000), pages 177-80.

Robert Bruner, *Applied Mergers and Acquisitions*, pages 531-38.

William J. Carney, *Essentials of Mergers and Acquisitions*, pages 13-25

Class 3 (January 25)
Informational Asymmetry: Adverse Selection I

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

CLASS WILL NOT MEET ON JANUARY 21 DUE TO MARTIN LUTHER KING DAY

Class 4 (January 27)
Informational Asymmetry: Adverse Selection II

Pfizer-Wyeth Merger Agreement, Sections, Article III.
Ronald Gilson, Value Creation by Business Lawyers: Legal Skills and Asset Pricing, 94 Yale Law Journal 239, pages 269 – 280 (1984) (Value Creation).
James Freund, Anatomy of a Merger, pages 242-248 (1975).

Class 5 (February 1)
Agency Costs: Moral Hazard I

Pfizer-Wyeth Merger, Articles V, VII, and VIII (sections on covenants, closing conditions, termination).
Illinois Lottery Sale

Class 6 (February 3)
Agency Costs: Moral Hazard II

Ronald Gilson, Value Creation, pages 280 - 293.
Ronald Gilson and Reiner Kraakman, Mechanisms of Market Efficiency, 70 Virginia Law Review 549, pages 613 – 621 (1984).
A note on Hotel Management and Ownership.
Problem to be handed in before class: San Francisco Luxury Hotel Development.

Class 7 (February 8)
Asset Specificity I

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

Class 8 (February 10)
Asset Specificity II

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

Class 9 (February 15)
Taxation: Basic Principles

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 10 (February 17)
Taxation: Mergers and Acquisitions

Problems to be discussed in class (need not be handed in): Pinnacle's acquisition of Tangent.

Class 11 (February 22)
Taxation: Other Regulations

John Carryou and Maurice Tamman, A Device to Kill Cancer, Lift Revenue, Wall Street Journal, December 10, 2010.
42 U.S.C. § 1320 – 7b(b).
42 U.S.C. § 1395nn (excerpts)

Class 12 (February 24)
Exogenous Risk

Materials to be distributed

Class 13 (February 29)
Putting It All Together: Contingent Contracts

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 before class: Sale of a Regional Brewer.

Class 14 (March 2)

Putting It All Together: Capital Structure

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 before class: Goodyear Tire & Rubber.

CLASS WILL NOT MEET ON MARCH 7 OR MARCH 9 DUE TO SPRING VACATION

Classes 16 and 17 (March 14 and 16)

Materials to be distributed

Classes 17-26 (March 18 through April 19)

The Deals

Materials to be distributed

See overleaf for information about Part I and Part II deals.

Notes on the deals:

It may be helpful to have some sense of what sort of deals Part I and Part II deal teams will work on. Currently pending transactions (and categories/issues) which would be good candidates for Part I deals were the course to start on November 23rd, 2015 would certainly include the following.

<http://www.nytimes.com/2015/11/17/business/marriott-to-buy-starwood-hotels.html> (merger for strategic considerations)

<http://www.nytimes.com/2015/11/17/business/dealbook/liberty-global-to-buy-cable-wireless-for-5-5-billion.html> (merger with some consideration in tracking stock)

http://www.nytimes.com/2015/10/21/business/dealbook/jpmorgan-is-said-to-be-near-deal-to-spin-off-private-equity-unit.html?_r=0 or

<http://www.nytimes.com/2015/09/09/business/dealbook/failure-of-yahoos-alibaba-spinoff-would-have-messy-consequences.html> (spinoffs)

<http://www.nytimes.com/2015/09/29/business/dealbook/alcoa-to-split-into-2-separate-companies.html> (splitup)

<http://www.nytimes.com/2015/11/19/business/dealbook/pfizer-allergan-deal-for-up-to-150-billion-is-said-to-be-close-to-complete.html?ref=topics> (tax inversion)

There are usually major limitations on what third parties can learn about the plumbing of currently pending deals. For the Part II deals, teams will have access to the documents actually implementing the deals in question. Last spring we did a smaller than usual number of deals in Part II and approached them in a somewhat different fashion. This year we will go back to the traditional format and five deals. But you may be curious what last year's deals were. They were:

The merger between TASC and Engility

(<http://investors.engilitycorp.com/phoenix.zhtml?c=251345&p=irol-newsArticle&ID=2020694>)

General Electric's spinoff of Synchrony Financial

(<http://finance.yahoo.com/news/ge-opens-share-exchange-program-190508228.html>)

The Dell going-private transaction

(<http://www.forbes.com/sites/connieguglielmo/2013/10/30/you-wont-have-michael-dell-to-kick-around-anymore/>)