Student Exam Number ______

George Mason University School of Law
Examination Cover Sheet

Business Associations (Law 172-002)
Professor Aviram
Fall Semester 2003
Number of Pages: 4 (including this page)
Number of Questions in Exam: 3
Time Allotted: 3 hours

Exam Instructions

1. **Permissible material**: This is an open book exam. You may use any material you want that is on paper. You may not use material that is in electronic format (though you may use a print-out of that material), nor may you communicate with anyone about the exam until it is over.
2. **Length limit**:
   a. If you type the exam on a computer, it should not exceed 2,000 words. If you handwrite your exam, it should not exceed 200 lines.
   b. For every 50 words (typed exams) / 5 lines (handwritten exams) in excess of the length limit, two points will be taken off the exam's raw score.
   c. If you type your exam, please write at the end of it the word count (e.g., "Word Count: 1,489 words"). If you handwrite your exam, please do a similar line count. The words/line used in reporting the word/line count are not calculated in the word/line count itself.
3. **Legibility**: If you handwrite your exam, please write legibly. I will do my best to read your handwriting, but will have to disregard writing that is too small to read or otherwise illegible.
4. **Writing the exam**:
   a. You should give appropriate case and statutory authority for your answers, stating how each cited case/statutory provision relates to your answer.
   b. Length limit permitting, answer all issues that arise from the fact pattern, even if your conclusion on one of the issues is dispositive to other issues.
   c. If you think a question is unclear or cannot be decided without additional facts, state clearly what facts you believe to be necessary to answer the question. Length limit permitting, try to discuss the applicable rule and result for the various possible fact patterns.
   d. If the fact pattern states specifically what laws apply, analyze according to those laws. Otherwise, analyze the issue under the law or laws we addressed in the course. If we discussed how an issue is addressed differently under different laws (e.g., RUPA vs. UPA; MBCA vs. DGCL vs. NY BCL), state the rule, application and result under each legal system. Discuss choice of law only if it is necessary and the general rule (of applying the law of the state of incorporation) does not apply.

Good Luck!

The Exam Fact Pattern

This fact pattern is loosely based on the novel "A Journey to the End of the Millennium", by A.B. Yehoshua, though there are many deviations from the book's plot. The story takes place in North Africa and Western Europe around the year 1000 A.D. Assume, however, that the relevant legal system is similar to ours today, and the relevant jurisdictions apply U.S. law.

The Cast:

- **Alan –** Wealthy merchant, living in Tangier (in today's Morocco).
- **Bill –** Adventurer and skilled survivalist. Wanders North Africa from the Atlantic Ocean to the Red Sea.
- **Chris –** Alan's nephew. Raised in Tangier but migrated to Paris. Married Daphne.
- **Daphne –** Chris' wife, raised & educated in Worms (in today's Germany), and later migrated to Paris. Daphne is a famous etiquette consultant, who provides her consulting services through Daphne's Etiquette Consulting, Ltd. (DEC), a public corporation which shares are traded on the Paris Stock Exchange. Chris and Daphne are DEC's directors, and Daphne is the CEO and controlling shareholder.
- **Edward –** Daphne's brother. A merchant buying goods in Paris and selling them in Worms. Edward runs his business through Edward's Trading Company, Inc. (ETC), a corporation wholly-owned by Edward.
- **Frieda –** A minority shareholder in DEC.

The Story:

For years countless, Alan and Bill were partners in a merchant enterprise. Bill would roam the small villages of North Africa, buying goods from the locals with money supplied by the wealthy Alan, and bringing them to Tangier. Alan would then lease a ship, load all the goods and sail with Bill to Barcelona, selling the goods at a decent profit.

In the year 992, Alan met his nephew, Chris, while in Barcelona. Chris, who had immigrated to Paris, has been making a living by traveling to Barcelona, buying wares there, and selling them to customers along the route to Paris. Alan immediately identified the business opportunity: Not only did Chris speak the language of those Europeans, but he was also familiar with them and could gauge the kind of merchandise they would want to buy. After consulting with Bill, they dissolved their old partnership and established a new, three-way partnership.

No written agreement was made, though they agreed orally on the following: Alan will contribute all the capital needed by the partnership. Every year in the fall, he will give money to Bill, and Bill will travel across North Africa, purchasing (on behalf of the partnership and with the money given to him by Alan) whatever goods he finds from a list Chris prepared. These goods will be stored at Alan's warehouse in Tangier. In the spring, Alan and Bill will load the goods on a ship that Alan will lease, and travel to Barcelona. They will meet Chris in Barcelona, and deliver the goods to him. Chris will give Alan all of the proceeds received for selling the previous year's goods. Alan will then divide the proceeds between the three partners as he sees just, taking into account the contributions, efforts and needs of each partner. After dividing the proceeds, Bill and Alan will return to Tangier, while Chris will take the goods and begin his journey to Paris, selling the goods on the way.

The partners also agreed that the signature of each of the three can bind the partnership if the partner expressly states next to the signature that it is made on behalf of the partnership. This allowed Bill to sign contracts to buy goods on behalf of the partnership, and allowed Chris to sign contracts to sell goods on behalf of the partnership. Both did so many times in the following years.

The partnership was a huge success until 997. In that year, Chris married Daphne. Daphne was shocked to discover that Alan was married to two wives (bigamy was legal and socially accepted in Tangier; it was not in Paris). She demanded that Chris disassociate himself from his reprehensible uncle.

Chris relented, but needed to deliver last year's proceeds to his partners. He decided to keep one third of the proceeds (his average share in past years had been 25%, though it fluctuated and in some years his share had been as high as 40%), and sent the rest of the proceeds by courier to Barcelona, with a note explaining the reason for his abandonment of the partnership and stating that the money delivered is their share of last year's proceeds, after he has taken a one third share.

Alan and Bill, on behalf of the partnership, sued Chris to recover a portion of last year's proceeds that Chris withheld. Alan announced that in his judgment, Chris' share of last year's profits should be 20% (given the lower than expected proceeds, which Alan took as an indicator that Chris was not putting sufficient effort).

I. Analyze this lawsuit.

<u>The Saga continues</u>: Alan, Bill and Chris settled the lawsuit in an agreement in which they combined the former partnership's business with the business of ETC (for exam purposes, disregard any issues involving the merger of the businesses). The combined business would have Bill acquire goods in North Africa and bring them to Tangier, Alan would ship them from Tangier to Barcelona, Chris would transfer them from Barcelona to Paris and Edward would transfer them from Paris to their final destination: Worms.

After ETC sold some of its shares to the public and began trading on the Paris Stock Exchange, its shares were owned as follows: Alan, Bill, Chris and Daphne each owned a 15% interest; Edward owned 25%, and about 3,000 shareholders from the public owned the remaining 15%. Alan, Chris and Edward were elected as ETC's directors, and Edward was appointed CEO.

One day, during a social event at the palace of the Governor of Tangier, the Governor told Alan that he was contemplating a new tax on all goods exported from Tangier (but he had not made these plans public yet). Alan realized that if such a tax was imposed, ETC's business would be crippled (because the goods purchased by Bill and shipped to Barcelona by Alan would be heavily taxed). Alan told Edward about this conversation, adding that he was not sure if the Governor actually planned to impose the tax, or merely raised the threat it in order to have Alan and other merchants endorse the Governor's other policies (in return for not imposing the tax).

Edward told all of this to Daphne. The next day, Daphne sold a third of her shares (5% of the ETC shares) on the Paris Stock Exchange. The Parisian authorities discovered this and began an investigation of Daphne on charges of insider trading.

When news of the insider trading investigation was made public Daphne's consulting business was put at risk, since no one wants to hire an etiquette consultant who is perceived to be a criminal. As part of a PR campaign to fight the insider trading allegations, a DEC spokeswoman announced that Daphne did not commit unlawful insider trading. DEC's shares, which sold at $34 before the investigation was announced, and at $15 the day before the spokeswoman's statement, dropped to $13 the day after the statement.

Following the investigation, the Parisian authorities charged Daphne with violations of Section 10(b) of the Exchange Act and of Rule 10b-5. Separately, Frieda sued Chris personally for breaching his fiduciary duties as a director of DEC by failing to implement mechanisms to monitor and prevent Daphne (who's reputation is crucial to DEC's success) from engaging in criminal behavior that might tarnish her reputation, such as insider trading.

II. Analyze the 10b-5 charges against Daphne.

III. Analyze Frieda's suit against Chris. For exam purposes, disregard the issue of whether Frieda's suit should be direct or derivative.

Business Associations (172-002)
Memo on the Final Exam

Grades:

Raw scores were calculated out of a total of 100 points – 30 for part I, 40 for part II, and 30 for part III. Below are the average, median, lowest and highest grades for the exam and for each question separately:

	Average	Median	Lowest	Highest
Entire Exam	40.49	39	16	75
Part I	13.15	13	4	26
Part II	15.69	14	4	33
Part III	11.74	11	3	25

Letter grades were given based on the percentile ranking of the exam's total raw score, as explained in the exam preparation class (i.e., the letter grade depended not on the absolute raw score of an exam, but on the relative ranking of a given exam's raw score compared to all other exams' raw scores).

Below is an outline of what would constitute an excellent exam. This is only an example, not the example; i.e., some students received credit for very different, but well explained and correct responses. Also, the memo is not written exactly as an exam should be – It is longer that an exam should be, because I chose to emphasize in this memo some aspects that seemed worth clarifying (while addressing only briefly other aspects that seemed to be clear).

I. **The Alan-Bill-Chris Partnership**

The mainstream answer did not focus on partnership dissolution, but on the validity of Alan's division of the profits. If the term allowing Alan to do so is binding and Alan's determination (which is adverse to Chris) did not violate fiduciary duties, then the same distribution applies to the division of the partnership's assets after dissolution (overriding the default equal division rule). And since all profits were distributed each year, there weren't other assets to distribute. Certainly a wrongful dissolution may require Chris to pay damages to Alan and Bill, but the two did not sue for that. Dissolution did have some relevance (and received some points) since one may view the suit as either a suit to enforce a term of a partnership agreement (the term allowing Alan to determine profit division) or as a settlement of a partnership dissolution. However, dissolution was not the core issue in this question.

1. Did Alan, Bill and Chris form a partnership?

a. Definition of a partnership

(i) UPA §6(1), RUPA §§101(6), 202(a) – an association of two or more persons to carry on as co-owners a business for profit. 'Carrying on as co-owners' – joint profits and joint control.
(ii) Joint profits:
UPA §7(3), RUPA §202(c)(2): Sharing of gross profits does not in itself establish a partnership.
UPA §7(4)(b), (d), RUPA §202(d)(ii), (v): Receipt of a share of the profits by a person is prima facie evidence that that person is a partner, unless profits were received in payment of wages or interest on a loan.
Factual issues: Was Alan's share of the profits a payment of interest? Were Bill's & Chris' shares a payment of wages?
(iii) Joint control:
Fenwick: 8 criteria for partnership. Most relevant: Right to share profits; ownership and control of business (each partner has his "domain" in the partnership's business); community of power in administration; conduct of the parties towards third parties (each partner has signature rights that can bind the partnership).

b. Effect of lack of written agreement
(i) Formation of a partnership does not depend on partners' intention to form a partnership [RUPA §202(a)].
(ii) Partnership agreement may be oral [RUPA §101(7); *Martin v. Peyton*].

c. If ABC is not a partnership, B and C are agents of A under agency law (three-prong test). Under agency rules, C must return to A all money received in connection with his agency (*Reading v. Regem*).

2. How are the partnership's profits divided?

a. Default rule: equal share [UPA §18(a), RUPA §401(b)].

b. Did parties stray from the default? Seems clear that they did: they opted to allow Alan decide, each year, their fair shares. This may be unwise, but the court may enforce it because it is what the parties bargained for (supporting cases: *Bane, Lawlis, Day, Collins, Prentiss*).

c. Until distributed, partnership profits belong to the partnership (*Putnam*). Chris is not entitled to remuneration for his services except as set in the partnership agreement (UPA 18(f)§ ; RUPA § 401(h)). One might interpret the partnership agreement to overrule the default and consider the value of each partner's services to the partnership; however, assessing the value of the services seems to be left to Alan's discretion under the partnership agreement.

d. Chris' possession of the partnership profits does not grant him any rights to possess the partnership property (including the partnership's money) for a purpose other than a partnership purpose (which in this case is delivering it to Alan for distribution) (UPA

§25(2)(a) ; RUPA §401(g)). As an agent of the partnership (UPA §9(1), RUPA §301(1)), he is accountable to the principal (the partnership) for money he received in all matters connected with the agency (i.e., the partnership's business) – *Reading v. Regem*.

3. Was Alan's decision to give Chris only 20% of the proceeds a violation of fiduciary duties owed to Chris?

[One may also ask whether Chris' decision to withhold one-third of the proceeds a violation of fiduciary duties to Alan and Bill, but this question may be moot since withholding the money seems to violate specific terms of the partnership agreement. Nonetheless, in *GA v. Singer*, an agency law case, the court resorted to fiduciary duty analysis where an analysis of contract terms would have sufficed.]

a. The legal standard:

(i) *Meinhard*: The "selfless" standard.
(ii) *Meehan*: The "fair fight" (or fairness) standard.
(iii) *Bane, Lawlis, Day, Collins, Prentiss*: The "you make your bed, now you lie in it" standard.

b. Chris' actions violate his fiduciary duty under any standard, but policy may dictate contractual analysis rather than fiduciary duty analysis where the contract expressly addresses the issue (*General Automotive v. Singer* to the contrary).

c. Under *Meinhard*, Alan's decision is probably a violation. Under *Meehan*, whether it is a violation depends on the fairness of Alan's assessment that Chris is entitled to 20%. Under Bane et al., any decision by Alan is acceptable. Chris could have insisted on limitations on Alan's discretion. This approach is more likely to be adopted if the parties can contract to avoid this problem (which in this case they could – they could specifically allot shares, subject to modifications or bonuses if desired).

4. What was the effect of Chris' abandonment of the partnership on Alan & Bill's suit? Partners always have the power (distinguished from the right) to dissolve/disassociate. Disassociation is wrongful if in violation of a fiduciary duty (*Page v. Page*) or if the partnership was for a term, including an implied term (*Collins*). The contemplated partnership seems to be an endless chain – profits are distributed after new wares have already been purchased and shipped to Barcelona. Thus, either it is of indefinite term, and thus terminable at will, or is a permanent partnership (which is unlikely, though the *Pav-Saver* court did view the partnership in that case as of permanent, rather than indefinite duration). Wrongful dissolution allows continuation of the partnership without the dissolver, and entitles the dissolver the fair value of her interest in the partnership, minus damages incurred. Chris' interest, however, is likely to be the share determined by Alan under the oral partnership agreement, unless that term is not valid or the 20% determination is in violation of fiduciary duties (see above).

II. **<u>Rule 10b-5</u>**

1. The insider trading charge

a. Generally: Section 10(b) of the Exchange Act prohibits manipulative or deceptive devices or contrivances. Rule 10b-5 fills the prohibition with content by declaring as unlawful the making of an untrue material statement or a misleading omission of a material fact in connection with the purchase or sale of securities. Since the Parisian authorities sued under 10b-5, neither 14e-3 nor wire fraud statutes were relevant to this question.

b. An insider trading charge alleges a misleading omission of a material fact. For an omission to be actionable, there must be a duty to disclose. The duty to disclose may stem from a fiduciary duty to the issuer's shareholders (the "traditional" theory), or from a duty to the supplier of the private information (the "misappropriation" theory).

> (i) Daphne is a statutory insider, since she owns over 10% of ETC's shares. Thus, trading in ETC shares while in possession of nonpublic material information may violate Rule 10b-5 directly.
>
> (ii) Also, Daphne was "tipped" by Edward, so she would have derivative liability if: (1) Edward breached his duty of loyalty by disclosing the content of Alan's conversation with the Governor or Tangier to Daphne; and (2) Daphne knows or has reason to know of that breach. For a breach of duty of loyalty, Edward must gain some personal benefit from the tip (*Switzer*). Likely, helping his sister avoid losing money may be a sufficient personal benefit. It Daphne is a statutory insider, Edward would probably not breach a fiduciary duty by telling her the information (but then she would be liable as a statutory insider). If Daphne is not an insider, it seems that Edward's tip would be a breach of fiduciary duty to which Daphne is aware, and thus she would have derivative liability.
>
> (iii) Daphne is probably not a 'temporary insider' – this category is used for people who receive the inside information as part of providing a service to the corporation (e.g., outside lawyers, accountants, etc.). Daphne's SH status is likely not of the kind contemplated for this status. More likely, information she receives as a shareholder or family member will be analyzed under derivative liability as a 'tipee'.
>
> (iv) Misappropriation theory: The key question is whether Daphne owed a duty to Edward not to trade on the information. Not under *Chestman*, but she probably does owe such a duty under Rule 10b5-2(b)(3), since Daphne and Edward are siblings. Daphne may try to rebut the presumption of duty by establishing that she did not know nor would reasonably know that Edward expected her to keep the information confidential.

c. The elements of a 10b-5 violation

> (i) Jurisdictional nexus – assumed in the instructions to the exam ("Assume, however, that the relevant legal system is similar to ours today, and the relevant jurisdictions apply U.S. law.")

(ii) Transactional nexus – the insider trading charge relates to Daphne's sale of ETC shares. ETC shares are securities because they are "stock" (Securities Act §2(a)(1)).
(iii) Materiality –

(a) General Standard: *TSC Industries* – "...whether there is a substantial likelihood that a reasonable shareholder would consider the fact important."

(b) Balance between probability and magnitude (*Basic v. Levinson*). In this case magnitude is great ("Alan realized that if such a tax was imposed, ETC's business would be crippled…"), but the probability is not 100% ("[Alan] was not sure if the Governor actually planned to impose the tax, or merely raised the threat it in order to have Alan and other merchants endorse the Governor's other policies…").

(c) In insider trading cases, the fact that the insider traded while in possession of the private information creates a rebutable presumption that the information was material (*TGS* and Rule 10b5-1(b) vs. *Adler* and *Smith*). One way of rebutting this is showing that Daphne had planned the sale of securities in advance, for some purpose (e.g., needed cash immediately to cover medical expenses). Rule 10b5-1(c) presents affirmative defenses to the presumption.

(iv) Reliance – Reliance is presumed in omission cases [*Affiliated Ute*]. Insider trading cases are omission cases.
(v) Causation – Transaction causation is assumed in omission cases [*Litton*].
(vi) Scienter – Intent to deceive, manipulate or defraud [*Ernst & Ernst*]; under lower courts' case law, recklessness suffices [more nuanced discussion earned extra points]. Daphne intended to defraud (sell shares to people who did not know of the material information).

2. The misrepresentation charge

a. This charge, distinct from the insider trading charge, alleges that Daphne made DEC falsely deny her innocence in the insider trading charges, in order to keep DEC share prices artificially higher than they should be if the public believed the charges against Daphne.

b. Should DEC's spokeswoman's statement be attributed to Daphne? DEC's spokeswoman is DEC's agent and her actions in the scope of the agency are attributable to DEC. Given Daphne's control of DEC and her interest in making this statement, it is possible that the spokeswoman is directly Daphne's agent (apply the three-prong test), making the spokeswoman's behavior attributable to Daphne.

b. Elements of the 10b-5 violation: Same as II(2)(b) above, except for the following differences:

(iii) Materiality: In order to prove materiality, one must demonstrate that without the denial of insider trading allegations, the harm to Daphne's reputation would lower DEC's price. Such an allegation was made in *U.S. v. Martha Stuart*.
(iv) Reliance: In this case we have an affirmative statement, not an omission. We can still presume reliance under the Fraud on the Market theory (i.e., the statement kept DEC share prices artificially high, harming investors who relied on the 'integrity of the market price'). The fact that the price kept dropping after the statement makes it difficult to establish FotM.
(v) Causation: If the FotM presumption is established, transaction causation is assumed.
(vi) Scienter: It seems clear that Daphne's goal was to 'defraud' in the sense of denying the insider trading charges in order to prevent DEC share prices from falling. Perhaps she can claim that her real goal was not to affect share prices, but to persuade the authorities to drop the insider trading charge.

III. **<u>Frieda's suit against Chris for failing to police Daphne's compliance</u>**

1. Generally

a. The court usually applies the Business Judgment Rule to decisions of the Board of Directors, and defers to the board's judgment. If the BJR applies, the court will not second guess DEC's board's decision not to implement a compliance program to prevent Daphne from committing insider trading violations (rationale for the BJR: facilitating centralized management). The BJR is rebutted in two situations: (a) Directors did not conduct sufficient investigation or deliberation to make a business judgment; (b) Directors' decision is tainted with fraud, illegality or conflict of interest.

b. Note that PCV is not relevant here – PCV is relevant when suing a shareholder as a shareholder. Here, Chris is sued as a director, and it's not even clear if he holds any shares in DEC.

c. Since Daphne was the controlling SH and a one of two directors in DEC, one may argue that Chris could not have made the corporation take any actions against Daphne. *Francis*, however, makes clear that inability of a director to make the company remedy the situation does not absolve the director from has the duty to protest and hinder acts harmful to the corporation. If nothing else is possible, the director should resign.

2. Duty of loyalty

a. To the extent that DEC's board can be seen as having made a decision not to monitor compliance with insider trading rules, the board's behavior was not illegal – it didn't endorse or even permit a violation; it merely didn't actively seek to detect illegal behavior. If the decision endorsed by Frieda singles out Daphne (because of her reputation's importance to DEC's business), Chris is likely to have a conflict of interest because he is married to Daphne (*Bayer v. Beran*). Thus, BJR will not apply even if DEC's board did reach a decision not to institute a compliance program.

b. When a breach of duty of loyalty is alleged and BJR does not apply, the court will examine the challenged action's (or inaction's) fairness. If Frieda's claim is that DEC should have a policy specifically preventing Daphne from breaking any laws, the cost of such monitoring is significant (both because it would deter Daphne from working for DEC, and because it is hard to monitor every possible action Daphne does that may violate any law). Thus, even if the BJR is rebutted due to the conflict of interest, the decision not to tailor a compliance program specific to Daphne may be seen as reasonable and fair, and therefore as not violating Chris' duty of loyalty.

c. If, on the other hand, Frieda's claim is that DEC should have had a general policy preventing DEC employees from insider trading, Chris' may not be in a conflict of interest sufficient to rebut BJR because the decision equally affects all employees, not only to Chris and Daphne.

3. Duty of care

More likely, however, a court would conclude that DEC's board did not reach a business decision at all. Thus, BJR does not apply and failure to monitor insider trading violations may be a breach of the directors' duty of care. However, inapplicability of the BJR is not in itself a breach of the duty of care.

a. *Francis v. United Jersey Bank* found a violation of the DoC when a director took no action in the face of other insiders' violation of laws. But Chris did not abdicate his duties completely; he merely did not implement a compliance program (also, the court in *Francis* may have implemented a heightened level of responsibility because the corporation involved had been a financial institution; DEC is not). Even if the board's decision was a poor one, unwise decisions are not in themselves violations of the duty of care (*Kamin v. AmEx*).

b. If Chris reached an informed decision not to implement a compliance program after considering the costs and benefits, it seems the decision would be easy to defend.

c. But if Chris never considered the possibility, it may amount to a breach of the duty of care if he had notice of Daphne's misbehavior (*Francis*), had notice of a potential conflict of interest of another insider (*Van Gorkom*), or if the issue he failed to monitor regarded an important aspect of the firm's activity (*Caremark*). The reason for this (following the rationale of *Dodge v. FMC*) is that the board can decide how to monitor important aspects of the company's operation, but it cannot decide not to monitor them at all.

d. If Chris was also informed by Daphne or Edward of Alan's information, the *Van Gorkom* rationale (or even the *Francis* rationale) may apply. The *Van Gorkom* rationale may also apply automatically because the decision to risk tarnishing her reputation may be an endgame decision for Daphne – if her reputation is lost, her involvement in the etiquette consulting business (and thus in DEC) will end, so she may not consider DEC's best interest in such cases (on the other hand, since her actions will first and foremost affect her future in the etiquette business, perhaps DEC can count on Daphne to protect her reputation from harm).

e. If *Van Gorkom* does not apply, the question is whether the Daphne's possible violation of insider trading laws is an important aspect of the firm's activity given the likelihood of this to happen, and the harm to the company if it did happen. Arguably, the latter is very great, potentially mandating (under the *Caremark* rationale) that Chris, as director of DEC, address it and inform himself whether a compliance program is cost-effective. Failing to do so may be a violation of the Chris' duty of care to DEC and its shareholders (including Frieda). But *Caremark* may be distinguished from this case in two ways: (1) Unlike the directors in *Caremark*, Chris had no knowledge of past violations; (2) Unlike in *Caremark*, the board is sued for not monitoring actions that do not relate to DEC's transactions. While Daphne's private trading in other companies' stock may affect DEC indirectly by tarnishing Daphne's reputation on which DEC relies for business, such transactions are further from the core of the company's operations than illegal transactions between Caremark employees and doctors with which the company worked.

[Points were also given for explaining methods the board could use to protect DEC in case Daphne tarnishes her reputation – clauses in Daphne's employment agreement, purchasing insurance, etc.]