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Book Reviews: Cases and Materials on Corporate Finance

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BOOK REVIEWS

CASES AND MATERIALS ON CORPORATE FINANCE. By Victor Brudney† and Marvin A. Chirelstein.†† Mineola, New York: The Foundation Press, Inc. 1972 (Supp. 1973). Pp. xxxix, 1196. \$17.50. Reviewed by John J. Woloszyn.†††

As a law student, paging through a law school catalog always reminded me of browsing in an old fashioned bakery; both exercises require a great deal of discipline. Appetite sharpened by curiosity, I would find myself possessed with an overwhelming desire to sample almost every course offered. But one's brief tenure as a law student, like one's waistline, imposes its own discipline. I would ultimately resign myself to the fact that not everything I saw could be included in my educational diet.

If the reader will indulge me a moment longer in my gastronomic metaphor, the first question that came to mind while reviewing Brudney and Chirelstein's *Cases and Materials on Corporate Finance* was how will the contemporary law school catalog-browser look upon a course on corporate finance. I suspect that a significant number of law students, when faced with a choice including such glamorous entrees as constitutional and criminal law, will simply pass over something sounding as indigestible as corporate finance. This is unfortunate; perhaps, like many things which demand a subtle palate, the taste must be "acquired."

I am concerned, however, over the possibility that students who find a course on corporate finance appealing will nevertheless not take the course because of the competition of other courses in the corporate area. A good portion of any law student's time will be consumed by digesting the staples of a well-balanced law school curriculum: contracts, torts, property, etc. To the extent that students desire to delve beyond their basic courses in corporate, agency and partnership law, there is fierce competition for their attention. The assortment of courses generally offered in the corporate/business area, including corporate tax, securities regulation, antitrust, legal accounting and business planning, all vie for the limited space left on the market list of law students. Students may decide that a course on corporate finance is too limited in its focus on corporate problems when compared to these other contenders. Such a view would be selling a course on corporate finance short if the course adopted the approach taken by Professor Victor Brudney and Professor Marvin A. Chirelstein in their casebook.

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Brudney and Chirelstein's *Corporate Finance* is a formidable compilation of both legal material and related readings on financial and management theory. A substantial part of the text is devoted to articles on economic theory written by economists, business writers and legal scholars active in business affairs. The ratio of this non-legal material to the legal material is far higher than is normally found in the average casebook. In part this situation can be explained because the subject matter is not easily amenable to a strict casebook approach. But the weight placed upon the non-legal material is in large measure attributable to the authors' recognition of the fact that students will have difficulty understanding the policy and probable effects of legal constraints in the corporate finance area without a thorough understanding of the financial and managerial theories which motivate the decisions of corporations and investors. Moreover, the authors appreciate the necessity for future corporate or investor counsel to be able to understand and effectively communicate with their clients. To this extent, the non-legal material assists law students in understanding the concepts and decisional rules of financial theory, which guide or purport to guide, management and investors. The material also familiarizes law students with the language in which these concepts and rules are usually expressed.

In fact, at the outset of compiling the text, the authors hoped that they could "integrate" the economic and legal material in the specific sense that the solutions to legal problems could be drawn from economic theory.¹ Unfortunately, they found that legal and economic principles were not fully congruous. While financial theory is helpful in understanding the body of law that has developed in this area, it does not serve as the law's exclusive foundation. The authors opine that this situation stems from an essential difference in the objectives of the law and of financial theory. They note that the conventional goal of management is to maximize the wealth of the corporation's investors by maximizing the value of the corporation and its securities. In contrast, the legal constraints that have developed in the field of corporate finance have primarily focused on fairly dividing the value of the corporation among various interested parties who assert competing claims. Accordingly, financial theory's primary concern is in developing an overall "maximizing strategy," for management and investors, "making the pie as large as possible; the other [law] worries about how to split it up."² The economic and legal materials throughout the text echo this theme, emphasizing the divergent interests of law and financial theory in maximizing and dividing the pie.

The text has been divided into five parts by the authors who attempted to assemble the material in a thematic scheme which has a beginning (Part I), a middle (Parts II, III, and IV), and end (Part V).

1. V. Brudney & M. Chirelstein, *CASES AND MATERIALS ON CORPORATE FINANCE* xv (1972).

2. *Id.* at xvi.

Part I ("Enterprise and Securities Valuation") begins the thematic scheme by posing the threshold question of how should a corporation and its securities be valued. The materials begin with an Advisory Report filed by the SEC and an opinion by a federal district court in an insolvency reorganization. These are followed by a series of generally excellent articles dealing with the general topic of enterprise valuation. Among the problems considered by these articles are the discounting of future returns, the meaning of "returns," the inadequacy of traditional accounting statements in evaluating returns and the concept of risk taking.

With the foundation laid, the authors enter the middle realm where, for the next three parts, the themes will be variations on the principle theme of maximizing the value of the enterprise. Part II ("Capital Structure and Senior Securities") begins the middle part by examining the problem of whether changes in the composition of the capital structure by varying the mix of outstanding securities can increase the value of the corporation. The use of bonds, preferred stock, convertible securities and warrants are treated in adequate fashion. Some attention is also focused on the hobgoblins of stated capital and dividend regulation. The second half of Part II examines the legal relationship between senior and junior security holders. Materials included here focus on the resulting cost of capital as determined by the choice between debt and equity, as well as the effect of tax policy on that choice.

Part III ("Dividends and Dividend Policy") examines maximizing strategy with regard to dividend policy. The principle question presented in Part III is whether a corporation's dividend policy will have an impact on the value of the enterprise. The authors also examine the effect of taxes on dividend policy and the functions that may be performed by the repurchase of outstanding stock.

Part IV ("Mergers and Acquisitions") explores the function of mergers and acquisitions in increasing the value of the enterprise. Materials on the accounting aspects of a merger are included, as well as the corporate law and tax aspects. Attention is also given to the problem of how the enhanced value resulting from merger should be divided among participating security holders and how it should be divided between them and management.

Finally, the ending of the thematic scheme, in Part V ("Information and Disclosure") finishes the book with a study of the relationship between corporation and investor and the effect of the federal securities laws on that relationship. In the first half of Part V, the question of how corporate-level decisions affect the goals and actions of individual investors is explored. In the second half of Part V, the type of information needed by investors and investment advisors is analyzed, and attention is directed to the adequacy of the federal securities laws as a vehicle for prompting sufficient flow of that information between corporations and the investing community.

In view of all of the book's strengths it is only fair to raise three

points with regard to what I consider minor weaknesses. First, between Part V and the treatment of federal securities law in other parts, the text presents an extremely comprehensive study of federal securities regulation. So thorough is this treatment that *Corporate Finance* could almost serve as a text for a course on federal securities regulation. Undoubtedly, any analysis of corporate finance is going to necessitate a detailed study of the securities laws, particularly given the objectives of the authors in Part V. However, it seems that at least some of this material could be deleted from Part V without causing any substantive harm to the text.

Second, it is unfortunate that the authors chose to limit the focus of their book to the problems of public corporations and their investors to the exclusion of closely held corporations. Admittedly, public corporations dominate the economic life of our nation, but the average law student is more likely to eventually encounter his corporate problems on the closely held scale. Moreover, corporations themselves do not neatly divide into these two categories.

Third, it is also unfortunate that the authors chose to limit the scope of their book to problems primarily indigenous to senior and junior securities to the exclusion of problems created by other methods of financing. Short term loans, leasing and receivables and inventory financing fall equally within the category of corporate finance. Often selecting from alternative types of financing, the most appropriate type for a particular corporation at its particular stage of development is one of the most perplexing problems corporate counsel faces.

In summary, although one could have added a few pinches here, and perhaps subtracted a pinch there, the basic recipe is a sound one. Brudney and Chirelstein have adopted an approach which guides a law student to delve into the subject matter to a greater depth than many other courses offered in the corporate area. The book allows the law student to come away with a better understanding of the inter-action between the law and the business community. To my law student catalog browser I can only recommend that *Corporate Finance* will be enjoyable and rewarding to those who stop to sample.

DISORDER IN THE COURT, Report of the Association of the Bar of the City of New York, Special Committee on Courtroom Conduct. By Norman Dorsen, Executive Director and Leon Friedman, Associate Director,† New York: Pantheon. 1973. Pp. 432. \$15.00. Reviewed by Eugene J. Davidson.††

† Mr. Dorsen is a professor of Law at New York University, a former law clerk to Supreme Court Justice John M. Harlan, and General Counsel of the American Civil Liberties Union. Mr. Friedman is Executive Director of the Committee for Public Justice.

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