

THE SYSTEMS APPROACH TO TEACHING BUSINESS ASSOCIATIONS

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INTRODUCTION

The systems approach applies the methods of systems analysis to law. The principal method is to describe the system, situate a problem within the system, and take system mechanics into account in solving it.

The system might be the “legal system”—essentially litigation. But more often, it is a “law-related system”—one not composed of law, but one in which law plays a role. That system might be crime, the Internet, the corporation, or any other activity substantially affected by law. The analyst situates the application of law in the context of the physical system as it actually operates. In business associations, that context may be law offices, boardrooms, the daily interactions of business co-owners, as well as courtrooms and settlement discussions. One situates the application of law in the context of the physical system by describing the system with emphasis on the causal connections through which it operates.

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In 1995, Lynn M. LoPucki and Elizabeth Warren published *Secured Credit: A Systems Approach*, a casebook for teaching secured transactions.¹ That book demonstrated not only the practicality, but also the popularity of this real-world approach. The book has been adopted at more than one hundred law schools and is now in its ninth edition.² In the introduction to the Teacher's Manual for the first edition, they wrote:

The application of systems analysis to law is in its infancy. The reason we chose it as the principal heuristic device for this book is that, like Moliere's character in "Le Bourgeois Gentilhomme" who realized with proud amazement that he had been speaking prose all along, we realized that we, and many other legal academicians with a realist bent, have been doing systems analysis all along.³

Within a few years, three companion texts expressly based on the systems approach were published.⁴ All have been successful.

Two years after the publication of *Secured Credit: A Systems Approach*, LoPucki explained the systems approach to legal

1. LYNN M. LOPUCKI & ELIZABETH WARREN, *SECURED CREDIT: A SYSTEMS APPROACH* (1995).

2. LYNN M. LOPUCKI ET AL., *SECURED TRANSACTIONS: A SYSTEMS APPROACH* (9th ed. 2020).

3. LYNN M. LOPUCKI & ELIZABETH WARREN, *SECURED CREDIT: A SYSTEMS APPROACH TEACHER'S MANUAL* 3-4 (1995).

4. DANIEL KEATING, *SALES: A SYSTEMS APPROACH* (7th ed. 2020); LYNN M. LOPUCKI ET AL., *COMMERCIAL TRANSACTIONS: A SYSTEMS APPROACH* (7th ed. 2020); RONALD MANN, *PAYMENT SYSTEMS AND OTHER FINANCIAL TRANSACTIONS: CASES, MATERIALS, AND PROBLEMS* (7th ed. 2020).

scholarship.⁵ Since then, legal scholars have applied the approach as he described it in numerous areas of law,⁶ including corporate law.⁷

This Article addresses the use of system analysis in teaching. We wrote it to coincide with the publication of our casebook, *Business Associations: A Systems Approach*, for the basic law school course in business associations.⁸ The purpose of this Article is to clarify the systems approach as we have applied it, make the approach more accessible, and, ultimately, to redirect both legal scholarship and teaching to the context of legal practice.

As applied to teaching law, the systems approach (1) explains the law in the context of the physical—as opposed to conceptual—systems in which it is applied; (2) organizes the law for study by grouping rules and concepts according to the functions they perform in those systems; and (3) enables students to apply the material provided to solve problems that require knowledge of how the system

5. See Lynn M. LoPucki, *The Systems Approach to Law*, 82 CORNELL L. REV. 479, 480 (1997).

6. See, e.g., Iman Anabtawi & Steven L. Schwarcz, *Regulating Ex Post: How Law Can Address the Inevitability of Financial Failure*, 92 TEX. L. REV. 75, 80 (2013) (applying the systems approach to law-related financial systems); James A. Henderson, Jr. & Jeffrey J. Rachlinski, *Product-Related Risk and Cognitive Biases: The Shortcomings of Enterprise Liability*, 6 ROGER WILLIAMS U.L. REV. 213, 258 (2000) (applying the systems approach to products liability law); Timothy F. Malloy & Peter Sinsheimer, *Innovation, Regulation and the Selection Environment*, 57 RUTGERS L. REV. 183, 233 (2004) (applying the systems approach to environmental law); Tomar Pierson-Brown, *(Systems) Thinking like a Lawyer*, 26 CLINICAL L. REV. 515, 515 (2020) (applying the systems approach to advocacy); Paul M. Schwartz, *Voting Technology and Democracy*, 77 N.Y.U. L. REV. 625, 630 (2002) (applying the systems approach to election law); Alison McMorrán Sulentic, *Can Systems Analysis Help Us to Understand C.O.B.R.A.?: A Challenge to Employment-Based Health Insurance*, 39 J. MARSHALL L. REV. 753, 753 (2006) (applying the systems approach in health care law).

7. See, e.g., Tamara Belinfanti & Lynn Stout, *Contested Visions: The Value of Systems Theory for Corporate Law*, 166 U. PA. L. REV. 579, 579 (2018) (arguing that systems analysis can resolve central debates about the nature of the corporation); David Orozco, *A Systems Theory of Compliance Law*, 22 U. PA. J. BUS. L. 244, 244 (2020) (applying the systems approach to corporate compliance law); Troy A. Paredes, *A Systems Approach to Corporate Governance Reform: Why Importing U.S. Corporate Law Isn't the Answer*, 45 WM. & MARY L. REV. 1055, 1060 (2004) (applying the systems approach to corporate and securities law).

8. LYNN M. LOPUCKI & ANDREW VERSTEIN, *BUSINESS ASSOCIATIONS: A SYSTEMS APPROACH* (2020).

works.⁹ Each of these features is the subject of a separate Part of this Article.

Although casebook authors must incorporate all three features aggressively to make the systems approach effective, neither the students nor teachers using it need to understand the approach or even be aware that they are its beneficiaries. LoPucki and Warren did not explain the systems approach in *Secured Credit: A Systems Approach*, and we do not explain the systems approach in *Business Associations: A Systems Approach*.

The three features of the systems approach described here are not unique to it. Casebooks that take other approaches may describe the physical systems involved, discuss the role of laws in the functioning of the systems, and posit problems that simulate legal practice. But without aggressively doing all three, casebooks will not be able to provide students with enough information to solve realistic legal strategy problems. Learning to solve such problems is, for students, an attractive feature of the systems approach.

I. LAW IN THE CONTEXT OF PHYSICAL SYSTEMS

A system is a regularly interacting set of elements that work together to achieve a goal or goals.¹⁰ Systems commonly consist of subsystems, each of which performs some function necessary for the entire system to work. For example, the engine is a subsystem of a gasoline-powered automobile. The engine performs the function of converting gasoline to mechanical force. The radiator is a subsystem of the engine. Its function is to cool the engine while it operates.

9. Writers unfamiliar with the systems approach sometimes refer to the physical system as “architecture.” Sjøfjell and Taylor say of Lawrence Lessig’s use of “architecture,”

Lessig is referring to the obvious — and yet widely overlooked — constraints imposed by the physical world. This is a mode of regulation that has to do with materiality, not in the legal sense of having a material (e.g. financial) consequence, but in the sense of emanating from physical matter, such as naturally occurring phenomena, for example the location of natural resources, or human-built physical constraints, including communications technology inventions which allows for the movement of capital across borders, shares to be traded in micro-seconds or which transform labour contracts.

Beate Sjøfjell & Mark B. Taylor, *Clash of Norms: Shareholder Primacy vs. Sustainable Corporate Purpose*, 13 INT’L & COMPAR. CORP. L.J. 40, 43–44 (2019).

10. See, e.g., DONELLA H. MEADOWS, THINKING IN SYSTEMS: A PRIMER 11 (Diana Wright ed., 2008) (“A system is an interconnected set of elements that is coherently organized in a way that achieves something.”).

A system is “physical” or “concrete” to the extent that it “exists in . . . space-time and is composed of real people and/or other physical objects.”¹¹ Examples of systems range from the purely physical—machines or living organisms—to the entirely conceptual—such as mathematics, the grammatical structure of language, or the common law.¹² In an entirely conceptual system, the objects are merely imagined or represented. The systems approach teaches law in the context of the physical systems—law offices, courtrooms, and legal documents—rather than as merely abstract rules.

A physical system is “law-related” if the application of law contributes to the system’s function.¹³ Because law is always applied by people—lawyers, judges, and others—people are part of every law-related system. Thus, law-related systems are always social systems that exist in the physical world. They are not entirely mechanical like the engine of an automobile. But they are analogous in that they too consist of subsystems that perform identifiable functions for the system as a whole. For example, a court system consists of at least two clearly distinguishable subsystems: (1) a clerk’s office that receives, retains, and disseminates documents and (2) judges who read and hear arguments and render decisions.

The combination of a business and an entity (business–entity) is the main physical system within the scope of the business association course.¹⁴ Other physical systems within the scope of the course are the states’ systems for forming, documenting, and disclosing information about business entities, the state and federal court systems in which entity law matters are litigated, the Security and Exchange Commission’s (SEC) information reporting and disclosure system (EDGAR), the SEC’s enforcement system, and, tangentially, three liability enforcement systems—foreclosure, execution, and bankruptcy.¹⁵

11. LoPucki, *supra* note 5, at 488 (internal quotation marks omitted).

12. “Law,” as used here, has no physical existence. In a different sense of the word “law,” statutes and cases contained in books may be considered “law.” But if all such books and other physical manifestations of law were destroyed, “law,” as used here, would still exist.

13. See LoPucki, *supra* note 5, at 488.

14. Although a single business can employ several entities, and a single entity can own several businesses, the practice generally followed in teaching business associations is to implicitly assume a single entity owning a single business and consider other possibilities infrequently.

15. See LOPUCKI & VERSTEIN, *supra* note 8, at 142.

The systems approach describes legal phenomena in the context of the physical systems in which they occur.¹⁶ The descriptions are concrete, not merely conceptual.¹⁷ For example, the statement that “the corporation reincorporated from California to New York by statutory conversion in accord with its plan of conversion” is a conceptual description, not a physical one. The corporation, the reincorporation, and the plan may exist physically, but the description does not indicate whether they do or not. A physical description would describe what people did to constitute the statutory conversion, the places where they did it, and the physical documents they created in doing it. Such a description might include the drafting of a document by an attorney (the plan of conversion), the adoption of the plan by the corporation’s board of directors at a board meeting, the approval of the plan by the corporation’s shareholders by completing “voting instruction forms” online that are tallied in connection with a shareholders’ meeting that takes place in a hotel, the drafting of another document (the articles of conversion) by the attorney, the execution of that document by an officer, the filing of the articles of conversion by the attorney with the corporations divisions of the secretary of state’s offices in both states, and the acceptance of the two filings by the states’ employees.¹⁸ A physical description would certainly mention that the corporation’s offices, factories, and stores all remained exactly where they had been before the “move.”

Corporate law’s prohibition on the issuance of watered stock provides a second example. Described conceptually, the prohibition is against issuing stock with an aggregate par value in excess of the value of the consideration received by the corporation in return.¹⁹ That description makes the prohibition seem to be a protection for the corporation and its pre-existing shareholders against dilution of the value of their shares.²⁰ But a physical description would reveal that the board of directors, not a court, determines the value of the consideration, and that “[i]n the absence of actual fraud” the board’s

16. See LoPucki, *supra* note 5, at 488.

17. See *id.* (discussing how a system is conceptual if it exists in thought or as an idea but does not have a physical or concrete existence).

18. See, e.g., MODEL BUS. CORP. ACT §§ 9.31–9.33 (AM. BAR ASS’N 2016).

19. See LOPUCKI & VERSTEIN, *supra* note 8, at 203–04.

20. For example, assume that the original investors in Corporation pay \$100,000 for 100 shares each with a par value of \$1,000. If new investors pay \$50,000 for 100 identical shares, all shares would be worth \$667 per share. The original investors shares would be “diluted.”

value is conclusive.²¹ Thus, par value is not a protection against even intentional dilution, unless dilution is part of a scheme to actually defraud someone. A physical description might also add that “par value” with respect to shares is any amount described using those words in the corporation’s certificate of incorporation—thus tying the abstract concept of par value to a physical document.²²

The board of directors is a subsystem of the business–entity system, in that the board performs or delegates most of the business–entity’s decision-making function.²³ In accord with the systems approach, we describe the board of a large public company as a physical system.²⁴ Included in the description are such matters as the numbers of directors (five to eighteen members with an average of 10.8), who chooses them and how (a startlingly biased election procedure), the basic demographics and backgrounds of board members, the frequency with which boards meet (four to eight times a year), the unique function of board committees as decision makers rather than recommenders, the nature of board membership (a part-time job consisting mainly of preparing for and attending meetings), and board members’ pay (on average, just short of \$300,000 a year).²⁵ Within the board as a system are subsystems for calling, noticing, and conducting a board meeting—each with its own governing law.²⁶ For example, the system for calling a meeting might consist of the documents conferring authority to do so on some person, the person, and another document that would constitute the “call.”²⁷

The primary function of a business–entity system is to make profits by selling goods or services.²⁸ We largely ignore that and other business functions because they are not sufficiently related to entity law.²⁹ We confine our consideration to the entity-law-related functions

21. See DEL. CODE ANN. tit. 8, § 152 (2020) (“In the absence of actual fraud in the transaction, the judgment of the directors as to the value of such consideration shall be conclusive.”).

22. See *id.* § 151 (“Every corporation may issue . . . stock . . . with par value . . . as shall be stated and expressed in the certificate of incorporation . . .”).

23. See LOPUCKI & VERSTEIN, *supra* note 8, at 313.

24. See *id.* at 314 (describing the function of a corporate board of directors).

25. See *id.*

26. See *id.* at 317–18.

27. See *id.* at 317–18, 324.

28. See *id.* at 1 (“A *business* is an organization that sells goods or services in an effort to make profits.”).

29. See generally *id.* Some aspects of those business functions are governed by nonentity law, such as antitrust, trademark, employment discrimination, and workers’ compensation, making them law-related. We exclude them from our book

of the business–entity. But in explaining the board’s decision-making function, for example, we present the governing law in the context of the board’s physical operation.³⁰ Students need this knowledge of the physical system to ground themselves in what might otherwise seem a swarm of abstract legal concepts. Grounding students’ knowledge in the physical systems makes it easier for students to relate that knowledge to the problems they must solve, both in the business associations course and later in practice.

Studying the law-related systems is preferable to merely studying the law because “human beings understand the world by constructing working models of it in their minds.”³¹ Many of the students who take the business associations course have no experience with either business or its governing legal regime. The physical systems we describe as part of the systems approach are easier for them to understand and incorporate into their models than are conceptual descriptions.³² For example, a largely conceptual description might be that a corporation is formed by “filing articles of incorporation and the necessary fees with the filing office.” A more physical description might instead be that a corporation is formed by “mailing articles of incorporation with a check for the amount of the necessary fees to the Office of the Secretary of State.” The latter is easier for students to understand because it is in physical terms that students already understand: mail, check, and an office they could Google for an address.

In short, physical systems are easier to visualize than purely conceptual systems. Because the physical view we present is the view students will have when they practice, our view better prepares students for practice.

II. ORGANIZATION OF LAW BY FUNCTION

Ours is the first business associations book to be ordered by function. The competing business associations casebooks are ordered

and this paper because they are not related to the law that is the subject of the business associations course.

30. See *id.* at 319–22 (presenting the case *In re Walt Disney Co. Derivative Litigation*, 906 A.2d 27 (Del. 2006)).

31. PHILLIP N. JOHNSON-LAIRD, *MENTAL MODELS* 10 (1983); see also Lynn M. LoPucki, *Legal Culture, Legal Strategy, and the Law in Lawyers’ Heads*, 90 NW. L. REV. 1498, 1509 (1996) (elaborating on these models).

32. See generally LOPUCKI & VERSTEIN, *supra* note 8 (describing the physical systems of business associations).

by entity type.³³ That is, each contains a section on partnerships,³⁴ a section on corporations,³⁵ and usually a section on LLCs.³⁶ Within each of those sections, the materials discuss, to greater or lesser degrees, some number of the eight functions that we have identified as having to be carried out in every business entity: (1) decision-making; (2) limiting liability; (3) financing the business; (4) merging and dividing; (5) suing managers; (6) investment transfer; (7) investment withdrawal; and (8) participation in society. If every function were discussed in the section on each entity type, the result would be twenty-four subsections and mind-numbing repetition. Instead, most competing books discuss all the functions covered with respect to corporations, repeat only a few with respect to partnerships and LLCs, and do not provide significant coverage of limited partnerships.

A. The Decision to Group by Function

Each chapter in our book describes how a function is performed.³⁷ Because the functions are performed in essentially the same way in all four entity types, the governing law is the same or similar. With respect to the eight functions, the rules for the four entity types collapsed into manageable numbers of categories. That occurred because the rules and practices with respect to the four entity types have been converging for several decades. The types no longer differ much from one another.

Part of the reason for the convergence is that the ideology of private ordering dominates the field. All five of the entity laws we cover are enabling statutes consisting mainly of default rules.³⁸

33. See, e.g., WILLIAM K. SJOSTROM, *BUSINESS ORGANIZATIONS: A TRANSACTIONAL APPROACH* (3d ed. 2020) (providing sections on partnerships, corporations, LLCs, limited partnerships, and limited liability partnerships).

34. See, e.g., *id.* at 145–82 (explaining partnerships); *id.* 185–209 (explaining limited partnerships).

35. See, e.g., *id.* at 277–766.

36. See, e.g., *id.* at 211–75.

37. See e.g., LOPUCKI & VERSTEIN, *supra* note 8, at 161–211 (describing entity finance).

38. See *Jones Apparel Grp., Inc. v. Maxwell Shoe Co., Inc.*, 883 A.2d 837, 843–43 (Del. Ch. 2004) (holding that provisions of certificates of incorporation can displace all Delaware General Corporation Law provisions unless displacement would violate public policy). See also MODEL BUS. CORP. ACT § 7.32 (AM. BAR ASS'N 2016) (allowing provisions of shareholder agreements to displace all MBCA provisions unless displacement would violate public policy); REV. UNIF. P'SHIP ACT § 105 (UNIF. L. COMM'N 2013) (allowing partnership agreements to displace all statutory provisions except those specifically excepted); UNIF. LTD. P'SHIP ACT § 105

Managers and their advisers decide, by provisions in the fundamental documents, how the eight functions are performed in a particular business–entity. In doing so, they are rarely limited by mandatory rules of law.

The managers and advisers develop methods and practices that assist business–entity participants in achieving their goals. Examples related to decision-making include voting trusts, vote pooling agreements, irrevocable proxies, cumulative voting, majority voting, and consents. These devices are associated most closely with corporations. But all can be used in any of the four entity types. Using the systems approach, they need only be covered once.

The main differences remaining among entity types are the default rules and the words signaling entity type. Competition among the drafters of entity laws to increase the numbers of entities formed under their laws is eroding the differences among default rules.³⁹ All drafters tend to adopt whichever default rules are the most popular. The differences in words signaling entity type are also eroding. That is occurring in part because partnerships, LLCs, and limited partnerships substitute the more familiar language of corporations for the sometimes-awkward language used in the other laws. LLCs adopt “boards of directors,” partnerships have “executive committees,” and all three of those entity types issue “shares” rather than the “interests” suggested by the default rules.⁴⁰

The grouping of rules and practices by function instead of entity type is the most striking difference between *Business Associations: A Systems Approach* and competing casebooks.⁴¹ By grouping rules and practices governing the same function, the systems approach saves

(UNIF. L. COMM’N 2013) (allowing partnership agreements to displace all statutory provisions except those specifically excepted); UNIF. LTD. LIAB. CO. ACT §105 (UNIF. L. COMM’N 2013) (authorizing membership agreement to override statutory defaults); UNIF. LTD. P’SHP ACT §105 (UNIF. L. COMM’N 2013) (allowing LLC operating agreements to displace all statutory provisions except those specifically excepted).

39. See generally DEL. CODE ANN. tit. 8 (2020) (noting that the drafters are the Delaware Council of the Corporate Law Section of the Delaware State Bar Association); MODEL BUS. CORP. ACT (AM. BAR ASS’N 2016) (noting that the drafters are the Corporate Laws Committee of the American Bar Association); REV. UNIF. P’SHP ACT (UNIF. L. COMM’N 2013); UNIF. LTD. LIAB. CO. ACT (UNIF. L. COMM’N 2013); UNIF. LTD. P’SHP ACT (UNIF. L. COMM’N 2013) (referring to the Uniform Laws Commission’s respective drafting committees for the RUPA, the ULLCA, and the ULPA).

40. LOPUCKI & VERSTEIN, *supra* note 8, at 249 (providing the example of LLCs with boards of directors issuing shares).

41. Compare LOPUCKI & VERSTEIN, *supra* note 8, at ix-x, with SJOSTRUM, *supra* note 33, at ix-x.

teachers and students time, avoids the necessity for boring repetition, and facilitates comparison across entity types.

Application of the systems approach to other areas of law may yield similar efficiencies in presentation. Prior to the publication of *Secured Credit: A Systems Approach*, secured transactions casebooks covered only a single type of lien: the Article 9 security interest.⁴² But literally thousands of other types of liens, each with their own authorizing law, performed substantially the same function. They included real estate mortgages, non-Article 9 security interests, and a variety of statutory, common law, and judicial liens. LoPucki and Warren covered all of them in the same number of pages as books that covered only Article 9 security interests.⁴³

B. The Language of Grouping by Function

The words “system” and “function” are already part of students’ vocabularies in the senses in which we use them. We do not use other systems terminology—such as “physical system” or “law-related system”—in the book.⁴⁴ As a result, the systems approach requires no special vocabulary.

Entity statutes use different words to refer to the same concepts. For example, an equity investor is called a “shareholder” or “stockholder” in a corporation, a “member” in an LLC, a “partner” in a partnership, and a “general partner” or “limited partner” in a limited partnership.⁴⁵ Because the four kinds of investors are functionally the same, it is helpful to have a single, “entity-neutral” word that can be used to refer to all four kinds of investors when the point being made is the same as to all four of them.

The entity-neutral terms we use for four concepts appear in italics in Figure 1. The entity-specific terms corresponding to each of

42. See, e.g., STEVEN L. HARRIS & CHARLES W. MOONEY, JR., *SECURITY INTERESTS IN PERSONAL PROPERTY: CASES, PROBLEMS, AND MATERIALS* xii-xix (6th ed. 2016) (providing the table of contents containing only Article 9 security interest materials).

43. Compare LOPUCKI & WARREN, *supra* note 1 (containing 764 pages), with HARRIS & MOONEY, *supra* note 42 (containing 749 pages).

44. See generally LOPUCKI & VERSTEIN, *supra* note 8 (refraining from the use of physical system or law-related system).

45. See generally MODEL BUS. CORP. ACT (AM. BAR ASS’N 2016) (referring to investors as shareholders); REV. UNIF. P’SHIP ACT (UNIF. L. COMM’N 2013) (referring to equity owners as either general partner or partner); UNIF. LTD. LIAB. CO. ACT (UNIF. L. COMM’N 2013) (referring to equity owners as members).

the four entity-neutral terms are shown below the entity-neutral terms on the Table.

Figure 1: Entity-Neutral Terminology⁴⁶

The entity-specific term for the entity-neutral concept in the column heading is shown below the heading for each of the entity types in the left column.

(1) Entity type	(2) <i>Shares</i>	(3) <i>Investors</i>	(4) <i>Managers</i>	(5) <i>Fundamental documents</i>
Corporation	Shares (MBCA) Stock (DGCL)	Shareholders or stockholders	Directors	Articles of incorporation, bylaws
Limited Liability Company (LLC)	Interests	Members	Managers	Certificate of organization, operating agreement
Partnership (LLP)	Interests	Partners	Managing partners	Partnership agreement
Limited partnership (LP)	Interests or units	General partners Limited partners	General partners	Certificate of limited partnership, partnership agreement

Entity-neutral discussion also requires the terms “one-tier” and “two-tier” with respect to decision-making structures. Decision-making structures are one-tier when the investors themselves make the decisions (*e.g.*, partners voting) and two-tier when they divide decision-making between themselves and managers (*e.g.*, shareholders voting on some matters and directors voting on others).

We did not invent any of the eight terms we use to facilitate entity-type-neutral discussion.⁴⁷ The eight terms exist because the numbers of entity types are proliferating even while the existing types are becoming more like one another. Courts and commentators have increasingly found it necessary to generalize across entity types, and they have invented language in which to do so.⁴⁸ We merely sought out the most common usages in court opinions and journal articles.

46. LOPUCKI & VERSTEIN, *supra* note 8, at 3.

47. The terms are shares, investors, managers, fundamental documents, one-tier, two-tier, entity-neutral, and entity-specific.

48. See, *e.g.*, *Acacia Invs., B.S.C.(C) v. W. End Equity I, Ltd.*, 121 N.Y.S.3d 848 (N.Y. Sup. Ct. 2020) (referring to two LLCs and a corporation as the “AION Entities”).

C. The Effect of Grouping by Function

If the rules and practices regarding each function differed significantly by entity type, organizing those rules and practices by function would generate no efficiencies. The number of sections would still be the number of entity types multiplied by the number of functions. Two characteristics of the rules and practice made grouping by function effective. First, the rules and practices with respect to a function were usually the same for two or three entity types, if not for all four. The uniform laws governing partnerships, LLCs, and limited partnerships recently underwent a “harmonization” process that eliminated differences in language that were not intended to produce differences in outcomes.⁴⁹ The remaining language is frequently identical except for the words—such as “partner,” “member,” or “limited partner”—that signal entity type.⁵⁰ Second, when the rules differed, the differences were often in language but not substance. Describing that difference usually required only a single sentence. As a result, the systems approach generated substantially fewer categories that required discussion of differences than did the traditional approach.

Because the systems approach juxtaposes rules regulating the same function, rules are easily compared. Such comparisons have the pedagogical advantage of calling students’ attention to rule features. The comparisons raise two questions. Does some difference between the entity types justify a difference in the rules? If not, which rule is better? The existence of two rules, both adopted, facilitates discussion by pushing students off the facile position that whatever rule has been adopted is best.

Corporate law is more extensive and better developed than partnership, LLC, or limited partnership law. By prodding the reader to look for the partnership, LLC, or limited partnership rules that address a given function, the systems approach often prompts them to realize that no such rules exist. That does not mean the function is not performed—or even that law does not govern the function.

What the lack of any rule for an entity type does mean is that courts will infer a rule from the legislators’ silence. The lack of rules

49. Harry J. Haynsworth, *Our Mini-Theme: The Uniform Business Organizations Code and Its Constituent Acts*, BUS. L. TODAY, Apr. 2015, at 1 (describing the harmonization project).

50. Compare REV. UNIF. P’SHIP ACT § 409(b) (UNIF. L. COMM’N 2013), with UNIF. LTD. P’SHIP ACT § 409(b) (UNIF. L. COMM’N 2013), and UNIF. LTD. LIAB. CO. ACT § 409(b) (UNIF. L. COMM’N 2013).

regulating meetings is an example. In the absence of such rules, courts may draw any of three conflicting inferences. The first is that no requirements exist, and the parties are free to do whatever they wish. For example, in the absence of rules requiring meetings in LLCs, courts may conclude that a majority of the members or managers can make decisions without consulting or even notifying the others.⁵¹ The second possible inference is that the court should imply rules regulating meetings from the actions of the members or managers.⁵² If the members held one meeting and did not explicitly decide *not* to hold another, they impliedly agreed to hold meetings, and so must continue to hold meetings. A third possible inference is that the law for that entity type is incomplete, making it necessary to borrow rules from other entity types by analogy. For example, courts resolved the uncertainty over whether LLC veils could be pierced by concluding that LLCs were governed by the same veil piercing rules as corporations.⁵³ Despite a shortage of legislative guidance,⁵⁴ the courts are uniformly concluding that the business judgment rule applies in favor of the managers of LLCs.⁵⁵

51. See LOPUCKI & VERSTEIN, *supra* note 8, at 324.

52. The uniform laws governing partnerships, LLCs, and limited partnerships invite this inference by defining the fundamental document to include oral and implied agreements. See UNIF. LTD. LIAB. CO. ACT § 102(13) cmt. (NAT'L CONF. COMM'RS ON UNIF. ST. L. 2013) (noting that “the definition [of operating agreement] puts no limits on the form of the operating agreement. To the contrary, the definition contains the phrase ‘whether oral, implied, in a record, or in any combination thereof.’”).

53. *Pro Tanks Leasing v. Midwest Propane & Refined Fuels, LLC*, 988 F. Supp. 2d 772, 788 (W.D. Ky. 2013) (stating that “[c]ourts treat limited liability companies the same as corporations for purposes of liability analysis” and citing cases).

54. *But see* UNIF. LTD. LIAB. CO. ACT prefatory note to 2011 and 2013 amendments (NAT'L CONF. COMM'RS ON UNIF. ST. L. 2013) (describing “replacing the ‘ordinary care/business judgment rule’ standard with the duty to ‘refrain from engaging in grossly negligent or reckless conduct, willful or intentional misconduct, or knowing violation of law,’” as one of the “three most significant substantive changes” to the ULLCA).

55. *E.g., In re Med. Mgmt. Grp., LLC*, 534 B.R. 646, 654 (Bankr. D.S.C. 2015) (“The parties also agree that members and managers of LLCs are subject to the business judgment rule . . .”); *Bakerman v. Sidney Frank Importing Co.*, No. Civ. A. 1844-N, 2006 WL 3927242, at *9 (Del. Ch. Oct. 16, 2006) (“Absent particularized allegations to the contrary, the managers of an LLC are presumed to have acted on an informed basis and in the honest belief that the decisions were in furtherance of the best interests of the LLC and its members.”); *HLHZ Invs., LLC v. Plaid Pantries, Inc.*, No. 06-797-KI, 2007 WL 3129985, at *17 (D. Or. Oct. 23, 2007), *on reconsideration*, 2007 WL 4180659 (D. Or. Nov. 21, 2007) (“I do not see anything in the statutes, however, to persuade me that the business judgment rule would not apply to managers of Oregon LLCs.”).

Grouping by function applies to contracts and practices in addition to legal rules. *Business Associations: A Systems Approach* considers the most common provisions of LLC operating agreements, articles of incorporation, bylaws, resolutions, and partnership agreements along with the associated legal rules. For example, our text shows students a public company's waiver of a corporate opportunity,⁵⁶ and our problems ask students to consider opportunity waivers drawn from LLCs and limited partnerships.⁵⁷

D. The Treatment of Public Companies

A "public company" is a company whose shares are traded on a stock exchange or over the counter. To distinguish public from nonpublic companies, we consider any company required to file annual reports with the SEC to be public, and all others to be nonpublic. Nonpublic companies are sometimes referred to as "private companies" or "closely held companies," but both those terms are potentially confusing.⁵⁸

Entity laws rarely make any distinction between public and nonpublic companies.⁵⁹ The same rules apply to both. But the contexts in which the rules are applied differ sharply with the number of investors. For example, contractual restrictions on the trading of investments in public companies typically apply only to small groups of insiders for short periods of time, while contractual restrictions on the trading of investments in nonpublic companies typically exist for an entirely different purpose, apply to all investors, and are intended to be permanent. Another example is that meetings of investors in publicly held companies present logistical problems that are almost entirely absent from meetings of investors in nonpublic companies.

56. See LOPUCKI & VERSTEIN, *supra* note 8, at 383.

57. *Id.* at 389–90.

58. "Private company" typically means a company that is not a public company. But "private company" is not widely used and sometimes means a company that is not government owned. "Closely held" has two meanings: (1) a company with relatively few investors, or (2) a corporation that has qualified as a closely held company under that law of its state of incorporation. Because the second definition is not used in the Model Business Corporation Act (MBCA) and is not of practical importance under the Delaware General Corporation Laws (DGCL), we chose to use the first definition in *Business Associations: A Systems Approach*. See MODEL BUS. CORP. ACT (AM. BAR ASS'N 2016); DEL. CODE ANN. tit. 8, § 342 (2020).

59. *But see* MODEL BUS. CORP. ACT § 14.30(b) (AM. BAR ASS'N 2016) (defining a sort of public company and MBCA § 14.30(a)(2) applying a separate dissolution rule to such companies).

The differences between the public and nonpublic contexts often require separate treatment with respect to a particular function. When necessary, we accomplish this with separate sections regarding public and nonpublic companies within an assignment.⁶⁰ For example, the discussions in the last three of the five sections of Assignment 14, *The Scope of Investor Decision Making*, are of only the public company context.⁶¹

In theory, the categories of public and nonpublic could interact with the four categories of entities to generate the need for eight discussions of the same topic.⁶² But in actuality, we found that did not happen. Despite language in federal statutes and regulations that suggests their application only to public *corporations*, federal securities laws are being applied to public companies without regard to entity type.⁶³ That is, public LLCs and limited partnerships are treated as if they were corporations. In addition, entities increasingly employ their freedom under state entity law to adopt rules, practices, and language from other entity types. For example, public LLCs often have “boards of directors” and issue “shares” to their investors. Public LLCs and limited partnerships seem to recognize their obligation to include “shareholder proposals” in their proxy statements, even if they have members or partners, not shareholders. As a result, distinguishing the public context rarely adds more than a single category—public companies.

Some casebooks address the need to distinguish the public and nonpublic contexts by dividing their coverage of corporations into publicly and closely held corporations—a further balkanization of the subject.⁶⁴ Under such an approach, rules regarding the same function in different contexts—such as shareholder voting in public and closely held corporations—are separated from each other and often must be

60. See, e.g., LOPUCKI & VERSTEIN, *supra* note 8, at 258–66 (providing separate explanations of investor voting procedures in public and private entities).

61. See *id.* at 236–50.

62. We are unaware of any publicly held partnerships, but aside from that, all four entity types are employed in both the public and private contexts.

63. For example, Securities and Exchange Act Rule 14a-8, 17 C.F.R. § 240.14a-8 (2011) addresses “shareholder proposals.” The rules do not define “shareholder,” and the system is routinely processing proposals by LLC members and limited partners as if they were corporate shareholders. See, e.g., Constellation Energy Partners LLC, SEC No-Action Letter, 2011 WL 2906770, at *1 (July 18, 2011).

64. See, e.g., ALAN R. PALMITER & FRANK PARTNOY, *CORPORATIONS: A CONTEMPORARY APPROACH* 350–53, 928–35 (2d ed. 2014) (discussing the basics of shareholder voting and later the basics of shareholder voting in the close corporation context).

repeated.⁶⁵ The systems approach includes all the investor voting rules in the same assignment and separately discusses the public context only to the extent necessary.

III. PROBLEMS IN THE CONTEXT OF LEGAL PRACTICE

The third element of the systems approach is that students apply the material in the readings to solve problems of the kind they will later encounter in practice. The first subsection below explains how our problems differ from those that commonly appear in business associations casebooks and how we intend that students and teachers use them. The second subsection explains the link between understanding law in terms of systems and the ability to advise clients.

A. The Problems as Pedagogy

From the student's perspective, learning through the systems approach consists of three steps. First, the students read about how a relevant portion of the legal system functions. Second, before class the students—working alone or together—assume the roles of lawyers to solve the problems of hypothetical clients by deciding what to do in each case. The students' actions range from advising clients based on the students' reading of statutory or contractual provisions to formulating legal strategies that require students not only to hypothesize taking actions on behalf of their clients, but also to hypothesize the responses of others and imagine the paths forward that would enable the client to achieve its objectives. Third, the students participate in discussions of some of the problems in class.

Classes can be in the traditional format, in which the teacher lectures for part of the time and directs discussions of the problems or other materials for the remainder. In the Teachers' Manual, we furnish additional material about the cases, the law, and the problems that teachers can, but need not, provide to the students. The text and statutes cited in the problems supply all of the information students need to master the subject and solve the problems.

We prefer simulation to discussion as the means of addressing the more complex problems. The simulations we conduct are an integral part of the class, with the teacher playing the role of the client and the students playing the role of the client's attorney. The student-attorney presents his or her solution to the client, who reacts as a

65. *Id.*

sophisticated client might. If the particular student–attorney cannot answer a question, the teacher–client can—as in the real world—add to the legal team or substitute another student–attorney in his or her place.

The problems are constructed so that in-class simulation can provide students with nearly all the options they would have in practice for solving the client’s problem, including gathering additional facts through interviews (we play the interviewees), consulting with another attorney (another student in the class), negotiating with an opponent (we play the opponent, start by offering absolutely nothing, and then invite the student–attorneys to tell us why we need to give them anything more).

Because it requires both knowledge and creativity, the problem-solving process gives students a sense of accomplishment. It also directly prepares them for the work they will be doing in practice.

We have divided the book into assignments.⁶⁶ Each is about eighteen pages of text and cases followed by two to three pages of problems. Each is intended for a seventy-five-minute class. The problems range from easy at the beginning—to build confidence—to complex and challenging at the end—to support interesting discussions. In the easiest problems, clients pose questions that students can answer from statutes or document provisions. The problems direct the students to the specific provisions.

In keeping with our focus on the physical system, each problem is set in a particular time and place. The time is usually the first meeting between lawyer and client with respect to the particular matter and the place is usually the lawyer’s office. The clients have first and last names and the settings are as fact-rich as space permits. They include only the information that would typically be available at that time and place. The purpose is both to engage the student in the clients’ stories and to limit the tools available for solving the problem to those that would be available to attorneys with real clients.

Each of the problems asks how the student would respond to the client’s inquiry. Students who have been trained only to apply law to facts to discover issues must learn to take additional steps: resolving the doctrinal issues, drawing conclusions (even if they are merely that the law is uncertain), and then *recommending what the client should do*. The correct advice may be to do nothing, to file a lawsuit, to seek further information, to include a particular provision in a contract, to

66. See LOPUCKI & VERSTEIN, *supra* note 8, at ix–xxv (displaying a division into several assignments within the table of contents).

create a particular entity structure, or to engage in a multistep transaction.

We favor problems that have single best solutions, because students are encouraged by the answer snapping into place once they achieve the intended insight. The purpose of a strategy is often to overcome doctrinal uncertainty, so it may be an unwelcome irony when the choice among strategies is itself uncertain. That said, complex problems are by their nature often amenable to multiple strategies or solutions.

Students learn by doing. Here, the “doing” is the using of the materials to solve the problems. That requires students to reread portions of the text and think about them in the context of the problems instead of the contexts of our presentations. In doing so, the students make new connections within the materials and ultimately absorb the materials into their mental models of the world.

The systems approach to law is closely linked to legal strategy. Legal strategy is a plan for getting a client from the situation the client is now in (the problem) to the situation the client wants to be in (the goal), within constraints of time and money.⁶⁷ To formulate legal strategy, students need a lot of information about how the legal system functions—including information about what things cost and how long they take. The systems approach explains the physical, law-related systems as simply and directly as possible, because that is the only way to provide students with sufficient information to solve complex problems.

Reading cases is alone inadequate as a means of acquiring that information. First, judges—particularly Delaware judges—are verbose, yielding low ratios of usable information acquired to pages read. Second, cases typically deal with multiple issues, some of which are not relevant to the matter at hand. Third, in writing opinions, judges are explaining events—their decisions in the cases before them—rather than delivering information about system function. Fourth, cases are idiosyncratic—at best, they present the law of a particular jurisdiction at a particular time. Problem-solving requires current information regarding the relevant jurisdiction.

The systems approach uses aggressively edited cases to convey information regarding system function and achieve verisimilitude. A portion of a case may be included because it contributes a particularly clear or authoritative statement of legal doctrine, the description of a

67. See DEANNE C. SIEMER, FRANK D. ROTHSCHILD & PAUL J. ZWIER, *TEACHING LEGAL STRATEGY* 4–7 (2006) (stating and explaining this definition).

business practice, the description of a common and memorable legal predicament, an authoritative statement of the rationale for a particular rule, or a description of an exotic legal environment. The cases we use are rarely longer than four pages or older than ten years.

Instead of lengthy cases, we use text, tables, graphics, and aggressively edited cases to deliver the needed information as efficiently as possible. Text can present current law and signal the scope of its applicability across jurisdictions and entity types.

B. The Link Among Problems, Systems, and Strategies

The principal function of most law-related systems is to process situations into outcomes. To learn how a system functions is to learn which situations lead to which outcomes. For example, the defective notice of a directors' meeting leads to invalidity of the actions taken at the meeting.⁶⁸ The systems approach is to identify those situations and their consequences as clearly and directly as possible.

Legal strategies are plans for moving clients from their situations to the outcomes they seek. In most instances, the lawyer uses the system's functioning to create that movement. Lawyers shape their clients' facts to be those for which the system provides the desired outcome. Metaphorically, one can think of the systems as tracks and the strategies as the trains that run on them. Knowing which situations lead to which outcomes is a necessary prerequisite to formulating legal strategy. But the student also needs to know how to formulate a strategy. The systems approach seeks to meet both needs.

Actions are the building blocks of strategies. Legal strategists advise clients, communicate with officials on their behalf, negotiate with third parties, design transactions, and draft documents. They document events, bring and defend litigation, make requests, and give instructions. To determine what to do in a particular situation, the strategist must determine the client's goal(s) and formulate a plan for reaching them. To do that, strategists must imagine what the client might do, the responses of others, and the client's countermoves. Once the strategist has chosen what they think to be the best plan for reaching the client's goal and the client has authorized it, the strategist must implement the first step, assess the response, revise the plan, and

68. See LOPUCKI & VERSTEIN, *supra* note 8, at 317 ("Action taken at a meeting without notice to all directors is invalid. *E.g.*, Dolan v. Airpark, Inc., 513 N.E.2d 213, 215 (1987).").

repeat. Structurally, the process is analogous to what accomplished chess players do.

The problems provide students with multiple occasions to use the information provided in the text, and thereby reinforce their learning of it. The strategy problems also provide the basis for teaching the process of strategy formulation.

The problems indirectly provide the basis for normative discussions of entity law and system function. That is, by reading the text, solving the problems, and discussing their solutions, students learn how the system functions and rehearse their future role in it. They imagine people in a variety of situations and observe and participate in simulations of the process that determines those people's outcomes. They can see who law helps, who it hurts, the situations in which it works well, and the situations in which it works poorly. Because they are seeing these things in an academic environment, students have the opportunity to reflect on them. Thus, the systems approach frames and facilitates normative discussions.

CONCLUSION

The systems approach is a method for teaching law in a casebook-classroom setting. The text evokes, and students imagine, the physical systems in which law is practiced. As is reflected in commonly used phrases such as the "legal system," the "court system," and the "criminal justice system," the language of systems is the customary way to describe these environments. The environments are functioning systems that process problems into solutions. The systems approach describes and models the systems' functioning, explains how the systems process particular kinds of problems, and ultimately enables students to learn what to do to achieve particular results on behalf of their hypothetical clients.

The systems approach views law as instructions for the operation of law-related systems. The instructions directly tell courts how to process cases, and indirectly provide lawyers with the information they need for strategy and planning. The law-related systems include portions of the business–entity, but also include the state systems for chartering and tracking entities, the federal systems for securities law disclosure and enforcement, portions of the court systems, and others. Students can no more understand entity law without knowledge of the law-related systems than they can understand the instructions for operating a machine without knowledge of the machine itself. The

systems approach presents law in the context of the systems law governs.

An obsolete paradigm has long hobbled the teaching of business associations. That paradigm regards each entity type as fundamentally unique, and so as a separate object of study. The systems approach recognizes that the four main entity types—corporations, partnerships, LLCs, and limited partnerships—are highly similar variants of an archetype—entity. The same functions must be performed in all of them—and are usually performed in substantially the same ways. That recognition dramatically reduces the amount of material students must learn to understand all four types.

When used in teaching, the systems approach's objective is for students learn to solve clients' problems. To achieve that, *Business Associations: A Systems Approach* provides students with hundreds of specific problems, explains the law-related systems and the governing law as simply and directly as possible, and gives students the opportunity to solve the problems on their own. Teachers follow up by simulating in class the interactions of the hypothetical lawyers with their hypothetical clients, and then explaining how the teachers would have solved the problems. On the basis of well-documented experience in using the systems approach to teach secured transactions, we think the systems approach is a better way to teach business associations.⁶⁹

69. The following are reviews of *LoPucki & Warren, Secured Credit: A Systems Approach*: Kathryn Heidt, *Taking a New Look at Secured Transactions: Secured Credit: A Systems Approach*, 96 COLUM. L. REV. 759 (1996) (book review); William J. Woodward, Jr., *Empiricists and the Collapse of the Theory-Practice Dichotomy in the Large Classroom: A Review of LoPucki and Warren's Secured Credit: A Systems Approach*, 74 WASH. U. L.Q. 419 (1996); Nathalie Martin, *Explorations in the Classroom: A Book Review of Secured Credit: A Systems Approach*, 26 SEATTLE UNIV. L. REV. 13 (2002).