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UPPER-LEVEL COURSES: THREE EXEMPLARS

MARK FAGAN¹ **SECURITIZATION AND ASSET-BACKED SECURITIES**
& TAMAR FRANKEL²

ERIC J. GOUVIN³ **USING TRANSACTIONS TO TEACH SECURED**
TRANSACTIONS

KATHY Z. HELLER⁴ **TEACHING DEALS THROUGH A FOCUS ON THE**
ENTERTAINMENT INDUSTRY

MARK FAGAN & TAMAR FRANKEL

SECURITIZATION AND ASSET-BACKED SECURITIES

MARK FAGAN

Introduction

I'm Mark Fagan, and I co-teach a course on securitization with Tamar Frankel at Boston University School of Law. We have come together to teach several interdisciplinary courses that combine law, business and public policy. Our course on securitization is a wonderful exemplar because it touches so many aspects of law as well as business and public policy.

We spent quite a bit of time wrestling with how to teach it. Do you teach it in a process fashion? Do you teach it by legal topic? Do you take examples and examine them? After much debate and discussion, we actually went with the linear, process path. We begin with the borrower and show the students how the originator of the loan fits in, how they take and create a Special Purpose Vehicle ("SPV"), and the SPV in turn takes the assets and turns them into securities. We walk through this process and explain how the assets can move in one direction, and the cash in the other, and then the repayment.

On the surface, this seems quite straightforward. Basically, we're taking the illiquid assets and turning them into tradable securities. But, when you unbundle it, you find a level of complexity, because in addition to our primarily players, many of whom they've already

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had some exposure to, we get our additional players: the rating agencies, the appraisers, the security brokers, and the servicers, which layer on a very interesting dynamic into this process, because they're actually not part of the core process yet have a significant impact on the outcome of the securitization process.

Course Method

To get the students excited about the class, we highlight the types of law the class will be dealing with from Contract to Property, to Securities Regulation to Tax, to Banking and Bankruptcy. Complementing the law is the business transaction which is enabled by public policy decisions.

I represent the business transaction; Tamar Frankel represents the law. For example, when we talk about a true sale, my job is to have the students understand risk. Why does this transaction represent risk? What's the investor's perspective as they look at this deal? Why would they be willing to buy one of these securities? A mortgage-backed security is an example. What would be their limitations? What would be their hesitations? Tamar Frankel explains the bankruptcy law aspect, as to how you mitigate that risk through true sale.

Because securitization is at its essence a business transaction we provide the students with contextual information. They are typically business-style case studies, as well as some role-plays, that allow the students to understand why an investor would have an interest in these securities. Or, why the banking industry had an incentive to want to securitize loans. Then Tamar Frankel will come in and actually give the law as well. Thus we conduct the course as an integrated presentation of business and law.

Case Example

What I thought would be interesting to do is to take you through one of the cases. It's towards the end of the course, and it starts to deal with the financial crisis. We happen to be in a very interesting time because post-the financial crisis, securitization is widely known, which it was not five years ago, and it is generally viewed in a negative context, certainly from the general media that the students are exposed to. What we try and do is get them to think a little bit about, "Well, how does securitization actually play?" We have talked throughout the course about the role securitization has played in mortgage-backed securities, how violations of both ethics and law by appraisers, rating agencies, etc. have contributed to the financial crisis, but at the end we come back and say, "Well, what role does securitization have as we move forward out of the crisis? Does it play a role there?"

The example we focus on is the Term Asset Loan Facility. This is a program initiated by the Federal Reserve in New York as a way to try to use securitization to enhance credit availability. To understand the context for it, in the packet you'll have about three to four pages of description associated with it and then some discussion questions, which is typically how we explore issues in the class.⁵ But, in this particular case, this happens to be just asset-backed securities, and you can see the rapid growth and then the plummet in 2007, 2008. If I showed you 2009, it would be equally troubling, but I stop in 2008 because here is where the Federal Reserve is nervous about the lack of a robust securitization market. Why would they be nervous?

⁵ See Mark Fagan, *Securitization and Asset-backed Securities* (Conference Handouts), http://www.law.emory.edu/fileadmin/Translaw/ConferenceMaterials/2010_Conference_Speaker_Materials/Fagan/Fagan_Conference_Handouts.doc.

ERIC J. GOUVIN

Well people tend to throw the baby out with the bathwater. Securitization was a great tool for asset liability management on balance sheets of banks. So if they're not using this technique, how are they addressing the mismatch in maturity on the balance sheet?

MARK FAGAN

Great example. What else?

SPEAKER

What's selling?

MARK FAGAN

What's selling? And the way in which you can see both of the points that you just raised is if you look at the Libor spread. It starts in September 2006 and goes up to March 2008, and certainly during the crisis, those spreads are astronomical in the context of finance. So the Fed is looking at this and saying, "Liquidity. How are we going to get people to buy cars if they cannot get loans? How are we going to get them to buy houses if they cannot get loans?" This much concern about liquidity in the marketplace, limits consumer willingness to spend, a key to jump starting the economic recovery. The Fed had a solution: reestablish a strong securitization market—after all, it was a powerful tool for increasing the velocity of credit for 20 plus years.

Thus, the Term Asset Loan Facility. The Federal Reserve will step in and provide funds to investors, not to borrowers, but to investors, to invest in asset-backed securities. Let that sink in for a minute. Your tax dollars are enabling an investor to go to the New York Federal Reserve and take out a fairly sizeable amount of money, the increments were a minimum of \$10,000,000 and go up from there (they actually had a bit more than several billion dollars in facility) and pay only slightly above Libor for the funds. It is almost free money to you, and the only downside is that you take a modest haircut to assure the creditworthiness. It's essentially creating a pool, so that if any defaults take place, the government isn't left holding the bag. The idea was, again, if we can get investors comfortable in this market and get securitization moving again, then all of a sudden the economy will rebound. They put it in place with an 18 month time horizon, and at the end of the 18 months, it did actually end. It was viewed as being a modest success. You can read that as being not terribly successful, and the issues around it involve the fact that the economy started to improve.

What we found interesting about this though, was that it was really a demonstration to the students, who are now somewhat skeptical about securitization, that the process is now an important vehicle for generating liquidity in the financial system.

This example also illustrates our focus on public policy issues. Where did the Fed get the authority to be able to do this?" This is about public policy. What is the role of the government in trying to stimulate private investors in the securitization process? Those issues help us make sure when a student walks out of the class, they understand the business context for why these transactions are taking place, and they understand the public policy rationale for securitization. We also want to make sure that they've learned enough law, as Tamar says: "To make sure: a) you know the right questions to ask, and b) you know which experts to seek out in some of these very special areas."

So that's how we've gone about trying to teach this basic transaction: make it interdisciplinary, use case studies and simulations wherever possible, and recognize that there are many aspects of the law that combine to make securitization a reality.

TAMAR FRANKEL

When you look at securitization, you'll find that it includes almost the entire curriculum of the law school. It starts with contract. In contract, the parties have a right to agree on anything that is legal, and it's nobody's business. They can do it in any way they want, so long as they more or less understand what they are doing and do it more or less in the same balance, that's the end of the story. Then you move to the product, and the product is property. That's a different story. In property, you must understand authorization and, therefore, only 12 to 13 forms of property are permissible; otherwise, it's against public policy. Remember correctly the first year and without information, you are naked. You must tell the people what this is all about. You have a transformation of the public policy, which underlies contract and that which underlies property that wants to create a market. You know that to create a market, you need an entirely different rule.

Now, in the middle, you have another funny creature, which is an investment company or a bank, if you will, because the SPV buys loans and issues securities. That is similar to a mutual fund with one exception, that if the Investment Company Act would apply, it wouldn't work. So, the SEC has given a very extensive, but conditional, exemption to the SPVs. Going back to teaching, students have to know something about the Investment Company Act and something about the rule that exempts. Once you do that, you find that and here I must say *mea culpa*. I was at the SEC; I was on loan for a year and a half when this exemption was given, and there was a thought about everything. I thought because the main thing was to make a very good distinction between these SPVs and investment companies, so that the managers of investment companies would not use the SPV to get rid of the regulation. What was exempt, however, was a section, which only a group of people know, 12(b)(1), which prohibits a fund, of fund, of fund, of fund. In the 1940s, that is what was done by Goldman Sachs. Yes. So they had it done and they shaved off 1, 2, 3, and 4. That was prohibited with very little permission by that section, but it was not covered, and the exemption covered SPVs.

What happened next? You had an SPV of an SPV of an SPV of an SPV. At the end, you didn't know what you had, and as a matter of fact, you had nothing, because what was taken into these SPVs was not merely an entire value of the portfolio, but the most risky part of the portfolio. So you have that and you have to explain it. Then you have also Article 9 in order to explain that the transfer is binding between the bank, or whoever produced these mortgages, and the SPV. However, the problem is that in reality, this transfer is not complete, because the transferor permits, sometimes gets assurances, and does all sorts of things so that the umbilical cord is not completely eliminated, and you have a problem there, too. Finally, you have also a little bit of bankruptcy and securities regulation.

So, how does one teach this? What the students will have to understand is the classifications. Whether they take it now or don't take it now, UCC Article 9 or Bankruptcy, they will know to whom to go, and they will know more or less what questions to ask. At the outset, that's what I tell them, "Don't think for a moment you're experts in this; you're not." Nonetheless, I think after students work at it, it is a catching subject, because you see so much and because there's so much now at stake.

Last year, we ended by asking them, “Would you invest in these things?” We thought we told them how good it is, how good it can be, and 99.9 percent of them still said, “No way am I doing this!” This year was a little better, and I think they came around. One last thing and then I’ll stop: everybody focuses on these mortgages. But the truth is that you have a lot of use for other financial assets to be securitized for the better. Mark, give us two examples.

MARK FAGAN

To give you a flavor for how it’s being used elsewhere, I will give a few examples. Next week, I’m off to Spain and doing some teaching, and there’s a person over there who is working on securitizing transportation infrastructure, and it is now being viewed as a key tool to fund and finance infrastructure in Europe. The second example is in China, where initially it was done for non-performing loans because the Chinese banks, when world trade came in, had to eliminate the non-performing loans. They are now looking at it, just as we have, as a way to improve liquidity.

So it’s become global. It introduces a whole new set of legal issues as it becomes cross-border, and that’s an exciting area. Hopefully we have given you a flavor for why this is an upper-level course. It’s a transaction, and it deals with everything you want in law. And with that, we will hand it over to our colleagues to keep it going.

ERIC J. GOUVIN

USING TRANSACTIONS TO TEACH SECURED TRANSACTIONS

I’m Eric Gouvin, and I’m also here on this coveted last spot on Saturday afternoon. When I submitted my proposal for this presentation today, I said, “I just want to share what I’m doing in my Secured Transactions class.” I proposed calling the session: “Using Transactions to Teach Secured Transactions.” So I’m contributing to Mark and Tamar’s course by providing those little secured loans in the first place that get bundled together. This is such a bread and butter topic, I believe it is really essential that someone take it seriously in law school.

Challenges in Teaching Secured Transactions

My first point about teaching Secured Transactions is that it’s hard to do because it suffers from the Rodney Dangerfield Syndrome: “it don’t get no respect.” It don’t get no respect from faculty colleagues, who think that only when you’re considering metaphysical concepts in Con Law are you really doing law professor work. It don’t get no respect from students, who think, “Oh here’s the big statute book. All the answers must be in there. There are forms involved. How hard can this be?” The lack of stature for this course in the curriculum is at odds with its importance in practice. For business lawyers, Secured Transactions is one of the places where the rubber meets the road. You have to be extremely competent in drafting and documenting the transaction, working with a complicated statute, and understanding not only just the law, but the business side as well. I think this is a really great course, and I love teaching it. But I know there are some challenges involved in it.

The second thing about teaching Secured Transactions is knowing your audience. This is a topic that's on the bar in a lot of places, so if you have a classroom full of students who are taking the course for that reason, you have to have a different set of tricks up your sleeve than if you have a true, upper-level elective class. Now over the last few years, I've got to admit, I've been stacking the deck. In the first couple of classes I spend time telling the students what a hard class this is going to be and how this is not for people who just want it for the bar. I try to get my enrollment down to about 20 students or below so we can really delve into the material I'm going to show you. If you have too big a class and you try to go to the level of depth and expertise that I want to hit, you're not going to get good evaluations. On the other hand, if you're a long tenured professor that might not matter that much.

We obviously have different levels of sophistication, interest, appreciation, and apprehension among the students. One of the things that creates apprehension is that the students are going into this subject pretty much blind. When they come to law school, what do they know about anything that lawyers, and especially commercial lawyers, do? They might have a gut-level sense about tort law because they've watched midday television, and they know that you can get rich quick by that. But with secured transactions, do they have any context? That is what my approach to teaching tries to accomplish. I try to create an environment in my classroom where the students can feel like they're gaining expertise by participating in a transaction, not quite a simulation, but a richly textured set of teaching materials to bring them along, and to help make the Code make sense.

Tips for Teaching an In-Depth Secured Transactions Course

Here are some thoughts about teaching this course that you ought to consider. First, be realistic. Be realistic about what you can really do in the class and what will be worthwhile for your students. Can I bring in super high-level securitization issues and the UCC issues that go along with that? No, I cannot -- for two reasons. First, I don't know that much about those matters. Tamar and Mark can pull it off, but I can't. Second, my students at Western New England College School of Law at Springfield, Massachusetts are not likely to do those transactions in practice. Almost all of my students in practice will help small business clients close a regular old commercial loan at the retail level. I'm going to focus on that, because that's what they're actually going to do. Very few of them will lie awake at night worrying about how to perfect a security interest in intellectual property in Malaysia. I'm not going to spend time on that either. But I am going to help make sure they know the issues that come up all the time, like the difference between the rules that apply to Purchase-Money Security Interests ("PMSIs") in inventory versus equipment. So, be realistic about the situations you put the class in. Obviously, this judgment will vary from school to school.

I use my materials as an overlay on top of the Whaley casebook. Some of you may be familiar with that. Doug Whaley⁶ has a nice set of teaching materials that are geared to small problems, and the problems are great to zero in on specific provisions in the code. The facts are very whimsical sometimes, and that is good and bad. But they're not very realistic sometimes either, and sometimes it's just so plain what the issue is, the student doesn't really have the experience in trying to figure out, "Well, what should I be worried

⁶ Douglas Whaley is a Professor Emeritus at the Moritz College of Law, The Ohio State University, from which he retired in 2004. His specialty is commercial law, for which he has written seven casebooks, all published by Aspen Publishers.

about?” I try to correct that deficiency by providing a rich context with built-in problems that will force the students to see the issues in a more organic setting. So, make sure your students know what you’re trying to do because they may get overwhelmed. I give them a file that’s not too different from a file that a new associate might see. It’s somewhat simplified and it’s been tweaked so I can increase the teachable moments, but they might get a little psyched out if you don’t let them in on why you’re doing it. And why am I doing it? I’m doing it because I want to make sure that they appreciate the importance of the facts, that they read the documents, and that they read the Code and apply it to the facts and the documentation they have before them. I know from experience that if you just assign the documents, they won’t read them. They’ll say they did, but they won’t. If you do it my way, where the documents are integral to the hypo, when the discussion in class really ties into the keys off of these materials, you’re more likely to get what you want. Having said that, be prepared to do a little handholding because students will get a little psyched out. Numbers will be involved, and that’s not always their strong suit.

As far as strategies for bar classes, again, be realistic. Appreciate the fact that you’re not going to have this wonderful in-depth upper-level elective. You’re going to have to think of a different way to get across the objectives. One way is to make it personal. I find using car loans is the best way to get students to see a bread and butter transaction. Now, car loans are not ideal because the way one perfects a car loan is different from most of the transactions we will be talking about in the class, but we do talk about titling statutes, so it is not entirely out of the mainstream.

The other thing that psyches students out is when you start bringing in business terms, and I always do. In my opinion, you need to introduce business ideas in order for the students to understand the deal, but business is really jargon-y, so you need to be prepared to de-mystify the terminology. The class eventually will be comfortable throwing around Code terminology, but some of the students who were Political Science majors or English majors are going to get flipped out if you start talking about liquidity or debt coverage ratios or any number of other business things. I always take a little time out to just make them appreciate that usually these concepts aren’t very hard to grasp, it’s just that you need to master them to have the vocabulary. I explain to the class that they are not going to be able to really understand secured transactions or a lot of other things if they don’t have at least a basic sense of how the deal makes money and who’s making money, No one litigates these cases on the basis of principle – it’s always about the money.

For the larger classes, I try to keep it conceptual. For instance, I would be unlikely to bring in financial statements and expect them to do much of anything with them. If we’re going to talk about financial documents at all, it will be “the view from 30,000 feet.” If you have a true upper-level elective where you have a smart self-selected group of eager students, you’re more likely to pull off something that’s more fun for you and more enriching for them. Beware, you’re still going to have a few bar-prep people in there, and you may have some people who just need to take a class that meets at 2:30 on Mondays and Wednesdays. Those folks aren’t fun to teach either, but their along for the ride. With this group, you can dive a little deeper into business ideas. I do give some sample financial statements for this hypothetical company. With the upper-level elective, I feel more comfortable putting in financial covenants in the documentation. And then we’ll see later on when terrible things happen to this company, which is always the case in a secured transactions course, the poor highlighted company is going to face financial difficulties of truly terrible dimensions. We can see if that works out.

I am a true believer in doing most of the instruction through problems and simulations. I spend very little time on the cases. The cases in the Whaley book and the cases that I assign subsequently are mostly there to illustrate a point, to see how a judge applied the code in a situation and more likely, how a judge screwed it up, and get the students to appreciate why this judge, who is a very and capable smart person, but was probably a tort lawyer in practice before ascending to the bench didn't understand the UCC principle that was at issue here, even with the help of his very bright, recently third-year law students who are now his clerks.

One of the things I want them to appreciate is that the commercial litigator is a teacher. This is no small task when you're trying to get across some points to a judge who probably learned the old version of Article 9 and maybe wasn't always a great UCC student to begin with. The other thing about the problems is it's hard to bluster your way through it when we're talking about a particular set of relevant provisions in the Code against concrete facts that are on the table.

I bring in guest lecturers in this class in several situations. The reason I do that is because I want my students to appreciate the business context in which this loan originates. To achieve that objective I assign some readings from MBA texts on commercial banking, like the loan underwriting process, and I bring in the banker's perspective. A friend of mine who's a commercial banker, comes in and writes up a term sheet for this loan that we talk about in class. The students have a chance to ask the banker some questions -- what were the issues that he thought about given the various menu of collateral available to him? What attracted him to some and repelled him from others?

You're going to see in a second that the hypothetical company that I'm going to talk about today is in the business of oyster farming. Is that inventory that's really going to do you much good if you are in a default situation? I also have them work with financial statements a little bit. I bring in a local bankruptcy judge to come in and talk about what happens when this deal ends up in his court. At the end of the semester, I bring in a lawyer from downtown to talk about how these transactions actually closed and the dynamics between borrower's counsel and lender's counsel. We develop a closing agenda. Whenever I'm bringing in the non-legal stuff, I remind the students of what their role as a lawyer is, which is not to do this stuff, but to be conversant enough so they can interact with the people who are doing the work, with the accountant, with the banker, or other non-legal consultants who get involved in the process.

In both big classes and small classes, there might be some mini-lectures that you need to just get out on the table because there are some topics that, in my humble opinion, aren't worth teasing out of the cases or even creating a problem for. So I am not averse to just giving a short and sweet explanation of how some things work, like the difference between a sale of accounts versus using accounts as collateral.⁷ On a very, very simplified level, getting them to appreciate that, here's Farmer Brown. He's owed money by these big supermarket chains. They're good for it. They will pay him eventually, but he needs money now to get his crop in the ground. He can go and sell those three \$10,000 accounts receivable to Nightflyer Finance, but they're going to have to take a discount, since this is an opportunity to talk about risk premiums and things like that. Or he could go to the bank and borrow \$30,000, but the bank is going to want interest and maybe take a discount too. So, I oversimplify, but my goal is to communicate the concept, not technical expertise.

⁷ See Appendix A, slides 7-8.

This is not trying to get them prepared to go out and do this kind of work, but to get lawyers with math phobia to appreciate that it may be that these two different structures really achieve the same financial result or something very similar. I use PowerPoint presentations to illustrate these points. The folks that are sitting in your class are very sophisticated about electronic media, and if you are going to do this kind of work, you've either got to get stuff that is really good or really, intentional, crappy. I find that sometimes just using the really cheesy clip art is a good way to get them kind of on your side.

What about leases versus buying a copy machine.⁸ Buy this copy machine on credit, give the seller a security interest in the copy machine, you're paying interest over five years, total amount sixty-five hundred. What if you just leased it and then at the end of year five, paid a dollar? Again, these are the things that to you and I is so much part of our mental vocabulary, our conceptual understanding of the world that we don't even think twice about it. But, the big challenge for me has always been unpacking my own knowledge because for those 2Ls and 3Ls sitting in my class, this is brand new and somewhat scary stuff for them. So making it plain like this is helpful. That's to sort of set them up, that's to get them invited to the party.

What I've been experimenting with over the last few years is immersing them in something that is not too oversimplified, something that's actually a fair approximation of a routine commercial loan. I did that because I was dissatisfied with all the staccato, specifically focused Whaley problems that were just a little too upbeat contextually and because I wanted them to appreciate how important it is to know what the client does or what the borrower does. It's what the lawyer does.

I've developed what a sort of a language lab approach. I tell the students that the UCC is like a foreign language and if they want to master it they have to speak it. Because just learning about it, hearing other people tell you how you say this phrase and such and such, that is not the same as actually trying to articulate that phrase yourself. So this is the chance to do that. I also find that some of the students come in with very warped perspectives about what business people are like, especially what bankers are like. They have these stereotypical notions of all businesses being bad guys or, conversely nowadays, of the rugged individualistic entrepreneur who does everything on her own. Both stereotypes are inaccurate.

Between those two extremes I try to develop more realistic images of what business people are like and develop some empathy, because the students are actually in the midst of their transactions. Because they're in the midst of their transactions, it's easier for them to kind of make the leap to think, "Oh my gosh! I will be doing this in a relatively short time, and I better take it seriously." Also, the semi-simulation forces the students to digest the statutes and it keeps the class from being too formulaic. Of course, after you've taught the same book a number of times, you know what's coming. But with this, it's a little bit more leeway. As we're talking about a particular issue, the students are going to have different takes on it, and I think there's a little more room for a different path. But I'm lying, because in the end, it is sort of formulaic. It's all theater and in my class I try to think of this as a production. I know how I want it to turn out, and I want them to get to that moment, but think that they got there uniquely in a way that no one ever got there before, and that they reached this epiphany on their own. And then, when I'm on my game, I think that works. Sometimes it doesn't.

⁸ *Id.* at slide 9.

Hypothetical Case Example

So how do I do this? Here's my hypothetical client, Fruit De Mer. It's a company that's engaged in the business of growing oysters in an aquacultural operation. I provide a detailed backstory on the company. There's a website for it that tells how they do their business and what products they produce. They produce fresh oysters, of course. They also process some of the oysters into gourmet oyster sauce for sale at high-end gourmet food stores, and every now and then there are pearls in the oysters. So why do I do that? Well if you've taught Secured Transactions before, you know one of the problems is classifying the collateral. So as these oysters are coming out of the sea, they are farm products. The students will always think they are inventory, and that is a big problem. Once we start applying some manufacturing processes to these raw oysters, they morph from being farm products into being inventory and so forth. So this just gives you an opportunity to test that sort of thing. The initial document package has all kinds of things like maps and site plans, some existing financial relationships, a mortgage through a local bank and an equipment lease, and specification sheets for a boat. Why a boat? Well, they're on the ocean. Turns out those boats might be subject to an alternative federal recording scheme: the Federal Ship Mortgage Act.

The hypothetical company's website⁹ really helps to get them to appreciate the richness of this business. Why does that matter? Well there have been a number of people today who already have talked about the importance of asking about what the client does. It's something that seems obvious if you've actually been a business lawyer, but it often gets lost in the classroom. These are not interchangeable widgets; each business has its own story and what they're going to be doing with the collateral might affect how you lawyer this transaction. In my hypo I provide pictures of them actually harvesting the oysters.¹⁰ Here is the town I grew up in on the Connecticut shore.¹¹ The names have been changed to protect the innocent. It turns out it's also the home base of Fruit de Mer, Inc.¹²

There are some fixtures issues that come up in this case. The big piece of equipment that this company has to grow these oysters is some state of the art stainless steel racks that are anchored in Oyster Cove, and they are held down by cement blocks that weigh two tons each, and the cove is tidal. You can see where I am going with this. There is an equipment lease.¹³ These state of the art racks are leased to the debtor, Fruit de Mer, by Aquatech, Inc. But when you look closely at that lease it looks a lot like a security interest. Now what? If we go to foreclose and the mortgagee has a mortgage on the fixtures, are these things fixtures or are they equipment? It's just a rich opportunity to talk about things like priority contests more organically, more the way that they really happen in practice.

Here's the mortgage.¹⁴ I even put these silly barcodes to try to make it look more like what they'll encounter if they were to go to the registry to do a search or if they looked

⁹ *Id.* at slides 13-15.

¹⁰ *Id.* at slide 15.

¹¹ *Id.* at slide 16.

¹² *Id.* at slide 17.

¹³ *Id.* at slide 19.

¹⁴ *Id.* at slide 18.

online. Here is the equipment lease,¹⁵ and again, a great teaching opportunity. One of the nice things about this course is it forces students to really work with statutes. The UCC has this definition of a lease, and the definition essentially depends on the facts of the situation. That's really the definition – the facts of the situation govern. Then the Code provides a bright line rule: if these things happen, you have a security interest, not a lease. Although the general test is an open-ended, fact-specific rule, students tend to go directly to the bright-line test as if it were the general rule. I want to make the students work with the facts, the law and the documents, so I have a couple of equipment leases at work here. This isn't like a textbook giving you the problem and asking is it a lease or a security interest? This is more like real life where you have to read several pages of a document and think about the economics of the deal in order to reach a conclusion. So here's the boat.¹⁶ Here are the specs on the boat.¹⁷ Why does it matter? The Ship Mortgage Act might require a special filing, otherwise we comply with state law, which may or may not involve a title. Here's the title on the boat.¹⁸ Titles, what a pain in the butt. Some states have titling statutes for boats, others don't.

The lack of uniformity on boat titling statutes provides great teaching and testing opportunities. In my hypo, the principal of Fruit de Mer is Diane Mollusky. She started her business in the nearby state of New Hampster before she moved down to Commercia, and various iterations of this hypothetical New Hampster sometimes has a titling statute, sometimes it doesn't. Commercia also sometimes has a titling statute, and sometimes it doesn't. Guess what? If the original security interest attached in the state that had issued the title, that's going to govern for as long as that title is good, and it's going to be good until another state issues a title. If Commercia never issues a title because it doesn't have a titling statute, then New Hampster law continues to govern, even while the boat is in Commercia on a permanent basis. The operation of interstate secured transactions in goods covered by title is something that causes students to pull out their hair, but it's more fun to teach this way if you have actual documents. There's something satisfying to them about touching these things.

The gourmet oyster sauce is a high-end item that stores are reluctant to buy as part of their inventory. So how do we distribute it? Through consignment. This is the consignment agreement.¹⁹ It's basically a letter. It turns out that the way they've actually pulled things off over the years looks like a security interest, too, because the longer it takes the purported consignee to pay for the stuff, the more he has to pay. And no one has ever actually returned any of the oyster sauce.

And then finally, a pretty simplified balance sheet.²⁰ Depending on my gauge of the class, we might go through to talk about some of the assumptions that go into these numbers. Every now and then I'll have an accountant in the class and I'll enlist his or her help with the accounting. A basic understanding of the financial statements will matter in

¹⁵ *Id.* at slide 19.

¹⁶ *Id.* at slide 20.

¹⁷ *Id.* at slide 21.

¹⁸ *Id.* at slide 22.

¹⁹ *Id.* at slide 23.

²⁰ *Id.* at slide 24.

the decision about whether we should we lease or borrow. The security agreement contains a financial covenant requiring a certain debt coverage ratio, so we at least review that.

So, once I've got this background in place, then it turns out we're going to have a need for additional financing. I bring in my commercial banker friend, he writes up a term sheet, and then we begin the process of documenting the loan. I try to make it a bread and butter kind of transaction. We need a security agreement. We need a financing statement. I'm going to talk about them in a second.

I can also use this as a launching-off point to talk about things like statutory liens. The UCC is not great at dealing with statutory liens. The casebooks are even worse, because one of the things that you need if you're going to really talk about this is the statute that creates the lien. So in this fictional jurisdiction of *Commercia*, where all this is taking place, I have a statute for boat liens.²¹ I have another statute for mechanics liens, depending on what scenario I'm using. So the students have a short and sweet statute that contains some built-in problems of my design.

Deposit control agreements can be difficult to teach in the abstract. I also have a deposit control agreement,²² which is going to be at the center of a competition between the bank that hold the mortgage on this property (they are also the primary depository institution), and other parties who have claims against money in the account by virtue of that money being proceeds of the accounts receivable or inventory. The rules for priority between the banks that maintain the deposit account, and someone who's claiming the deposit account as proceeds or through control, are really persnickety. There are three different scenarios depending on how you established the control, and this allows me to focus on any particular method, and we can have a more sophisticated discussion about if the secured party perfected their interest in the depository account through this method, how do they stand up *vis-à-vis* the bank that maintains the deposit account in a battle over set-off?

There is, of course, a security agreement as well.²³ There is the results of an official UCC-11 search in the document package.²⁴ Although I bring them online to show them the searches, I also give them a printed-out UCC-11.

Then the coup de grace in this approach to teaching is that the materials can become the test. You can just keep rolling with it and turn it into a hypothetical for the exam. The students now are very familiar with these underlying documents. I give them a few more facts on the last day of class, maybe another document or two, and ask them to provide answers to some questions. Like I said, something terrible always happens to this company, often something precipitous because I'm also going to be testing them on preferences.

You need all the elements of a preference for it to be a voidable preference, one of which is that the debtor had to be insolvent at the time of the transfer. We rely usually on the 90-day presumption of insolvency, but it's just a presumption. So if during the 90-day period they started out in good shape, but on day 45 the red tide came and killed all their

²¹ *Id.* at slide 31.

²² *Id.* at slide 29.

²³ *Id.* at slide 26.

²⁴ *Id.* at slide 27.

oysters, or a nor'easter came through and wiped them all out, transfers taken between day 90 and day 45 might actually not be avoidable as preferences.

You can't ask them in a timed, three-hour exam at the end of the semester to go into that, but I don't feel bad asking them on a take-home to think this through, because this is, again, forcing them to read the statute. The magic words in the statute matter and the facts matter. Match them up. So I give them this on the last day of class, and I give them as much time as they want, basically. I make it due on the last day of the exam period. I do that because they've got other things they have to take care of at the end of the year. I don't want to hear any whining about, "Oh, I had three exams in the first week." I don't care. Just get it into me. You have plenty of time. Students who are not good at time management will make a huge mistake and spend all their waking hours for the next two weeks working on this problem. I hope that's a lesson learned.

Anyhow, so they can really dig in. I can make them use the financial statements. Sometimes I have to supplement the record with something like an abstract from a title company to run the real estate records.²⁵ I have, in the past, given them a case on fixtures from our fictitious jurisdiction²⁶ so they can make arguments about that when we're fighting over those racks out in Oyster Cove.

As for pros and cons, on the "pro" side, it's a lot of fun to design and work with these materials. I really enjoy creating this alternate universe, but it's a lot of work. The students, I think, enjoy it. It allows them to synthesize the course. I've gotten positive feedback from the students that I'm targeting in this class. The students who are just the casual taker of the course don't like this very much. The students who really want to master this material eat it up.

Sometimes I allow them to work together. Certainly during the semester, I encourage them to collaborate and sometimes I get really good insightful observations from study groups. The examination, of course, is a test of individual knowledge. I like the take-home exam format because I can page limit it, and it has to be typed, so it's much easier to grade. The downside is that sometimes you make mistakes. I intentionally put mistakes in a lot of the documents, because that's going to be my teaching moment. Almost every semester however, I find there's some other mistake -- which I'm going to tell them is a teachable moment -- but I realize, "Oh man, I didn't mean that."

It really works best in small enrollment upper-level electives. If the students aren't really into the hardcore version of this, it's not going to be as effective. You can import some of this stuff to a larger group, as I tried to set up at the beginning of the course, but to do it the whole nine yards, it's better for smaller groups. For honor code concerns, if students are working together, every school has a different way of dealing with that. When I use it for tests, which I have been, every year you need to rework it to create a different set of issues for testing. The core of this hypothetical stays the same from one year to the next, but with that last bit, you've got to be creative about finding another good way to put them through the paces because you can't give them the same exam twice. So that's what I got for you. I've really enjoyed doing it this way. In another course, I have a setup of this where instead of aqua-culture, it's a company that farms maple trees and taps sap for maple syrup and has a little snack bar and restaurant art gallery.

²⁵ *Id.* at slide 32.

²⁶ *Id.* at slide 33.

KATHY Z. HELLER

TEACHING DEALS THROUGH A FOCUS ON THE ENTERTAINMENT INDUSTRY

I am trying to think of a very clever way to transition from Secured Transactions to Entertainment Law. I don't actually have one, but interestingly, the principles of teaching appear to be very similar.

Today I'm going to discuss a transactional course I teach and a Clinic in which students work directly with clients to put their transactional skills into practice. The course is Negotiating and Drafting Media Industry Transactions. Negotiating and Drafting Media Industry Transactions is the prerequisite course to the Clinic "Working with Filmmakers." Students enrolled in the Clinic work directly with ultra low budget filmmakers who are ready to begin production on feature films.

Negotiating and Drafting Media Industry Transactions: Course Overview

The title and content of this course was determined by surveying the entertainment law and transactional courses offered at a number of schools, and attempting to encompass both the business and transactional material currently available. When I first taught the course I focused primarily on the motion picture industry but the scope of entertainment law has expanded so rapidly that the course is not designed to teach the lawyers role in transactions which occur in various types of media. Because this is currently the only 'transaction' class taught at Chapman and many of the students will work in fields other than entertainment, I am very aware of the need to teach transactional skills that translate to other areas of law. However, Chapman is unique in that it is located in Southern California, where entertainment clients are ubiquitous; it's highly likely that, no matter what the area of practice, an attorney will have entertainment clients at some time during their career. I give two examples, both true – one involves an attorney whose client is one of the largest used car dealerships in California. The client wanted to obtain the rights to a novel for his son to write his first script. The second involves my own estate planning attorney who represents the literary rights to the life story of an academy award winning client who is a film director. No attorney wants to send a client elsewhere because they are unable to do the requested legal work. This course will provide the students with the legal background and drafting skills to assist with projects such as the acquisition of book rights and protection of life rights and literary material.

Although students enrolled in the Negotiating and Drafting Media Industry Transactions course have all completed first year Contracts, they come to this course with a wide spectrum of transactional experience. Some students have work as interns at entertainment law firms or film studios and others have been paralegals. Some are LLMS, who have already passed the bar. And in every class at least half of the students have no experience at all with transactional work.

The first few classes are designed to bring all students in the class to a common point in basic contract and intellectual property law. The review of intellectual property rights includes copyright as well as statutory and common law rights of privacy, defamation, and publicity. These so-called underlying rights must be considered in every media contract and a single mistake or omission can result in a break in what is referred to as the Chain of

Title. The Chain of Title must be correct and complete for financing, distribution and exhibition of any form of media.

The goal of this introduction to media transactions is to emphasize the essential role the attorney plays, not only in documenting the ‘deal’ but in also ensuring that all of the underlying rights are correctly transferred from the point of view of all parties. The next step is to bring the students to an understanding of what a transactional lawyer does. The students’ prior coursework emphasis has been on cases and related adversarial proceedings. As a result, most view the other party as an opponent and their role as that of aggressive advocate. They measure their success in terms of: Who won? Did I get more? Did I trick you into giving me something to make my client happy? So I spend some time explaining what a transaction is; that it’s most likely not about ‘winning,’ and it’s never about ‘tricking’. If the parties don’t have a meeting of the minds on common agreed goals, they probably will not perform, and if they do perform, they likely will do so reluctantly or half-heartedly. They will not enjoy the process and probably won’t be pleased with the result.

It could be argued that transaction case law, particularly in the entertainment industry, is very misleading. Cases tend to involve very deep pocket parties who are very determined to make a particular point. Well drafted transactions do not appear in case law. Even if one of the parties is clearly in breach, the contracts should provide remedies and alternatives to litigation. The class initially discusses the role of the attorney in transactions generally. This includes a discussion of the difference between a business decision and legal advice. The students are also introduced to the difference between being an attorney who is considered a ‘deal maker’ versus one who is considered to be a ‘deal breaker’ – and that the former is more likely to have a successful entertainment practice. Throughout the course there is an emphasis on understanding the environment in which the client conducts their business. Transactions do not occur in a vacuum and negotiations as well as documents will be most effective when an attorney knows the answer to questions such as: What is the standard industry practice? What are the common ‘buzz words’? What terms are generally accepted? What is the relative financial and business strength of the various possible parties? What is the client’s position and likely future in the industry? What is the nature of the client’s business – what does the client do, for how long and what are similar individuals or companies doing? It is essential to understand the industry in which the transaction occurs as well as where the transaction fits in the overall deal. What needs to occur before, concurrent with and completely outside of this transaction in order to ensure an environment in which all parties will perform as agreed? To answer these questions the class looks at the laws, customs, standards of practice and generally accepted terms in the entertainment industry, just as they would look at the used car sales industry for a client in that business.

The class is shown an example of lawyers drafting and negotiating - but seemingly oblivious to their client’s business - in the case of *Main Line Pictures, Inc. v. Kim Basinger*.²⁷ Ms. Basinger had entered into an oral agreement to star in the film “Boxing Helena” and then changed her mind, which was reported in the industry press, and yet for months the attorneys continued to exchange drafts.

I present a chart detailing the steps in the creation of media, from development through financing, preproduction, production, post production and distribution, from the lawyer’s point of view. The class discusses what clients expect from their attorney at each

²⁷ *Main Line Pictures, Inc. v. Basinger*, No. B077509, 1994 WL 814244 (Cal. Ct. App. Sept. 22, 1994).

step and what the attorney can do to prepare and anticipate documents and legal issues. For the remainder of the course we work with precedent contracts from each step.

We begin with a discussion of what a precedent contract is. Many of the students start out thinking of a precedent contract as a 'form'. They want to fill in the blanks with the right answer. And they see clauses in precedent contracts as inherently correct and immutable. It is a big step for many students to understand that a precedent contract is a record of one or more prior transactions and as a result it must contain some clauses which occur in all contracts, some clauses which were unique to one or more prior transactions, and some clause which are simply wrong. The first step in achieving that realization is comparing precedent contracts and finding that there are many variations on clauses labeled "standard terms". So the students review boilerplate clauses and learn that while they are often essential, minor variations in their terms can have a significant consequence. For example, an indemnification clause which includes payment of "attorneys' fees" can cost quite a bit more than one which provides for "reasonable outside attorney's fees. Precedent contracts are also analyzed to identify common deal points. For example, two sets of precedent contracts for the option and purchase of literary material are used to determine the typical deal terms and common clauses for that type of contract.

After reviewing the precedent contracts, students are given the assignment of drafting an agreement based upon a mock client file. They practice using the material in the client file to identify the deal points from the client's perspective and, insofar as possible, from the perspective of the other party. The client deal points together with the contract deal points and sample precedent contracts are the basis for the initial contract drafting in the course. Each student is required to prepare a draft agreement and a cover letter to send the agreement to opposing counsel. The letter is discussed in class, with an emphasis on its importance as an initial step in the negotiation process. The class exercises become increasingly complex throughout the semester and include interviewing a mock client, drafting, redlining, negotiating to agreement, letters to opposing counsel, letters to clients and creation of a client file. I provide each student with detailed comments on each draft, letter and memorandum. And some portion of each class time is devoted to a discussion of the most common errors in drafting and negotiating. Whenever possible, the class hears from practicing attorneys who are asked, among other things, to talk about what they have found challenging and where errors are most often made. For example, "who are the parties" is often answered incorrectly by even experienced attorneys. One of my classes had the opportunity to meet with the attorney who represented the Beijing Olympic Organizing Committee and who was therefore responsible for all contracts related to live performances and underlying rights. Copyright ownership vests at the time of creation in tangible form – so the live Olympic performances presented many challenges. The recording of every performance created intellectual property rights in that recording. He began the explanation of rights ownership under the performer's agreements with the statement: "the first and sometimes most difficult question is: Who are the Parties?"

Other topics covered in the course include attorney etiquette during negotiations and the attorney's role in moving a negotiation to a successful and satisfactory conclusion. At what stage is it appropriate to make a high or low offer? What is the attorney's obligation to include clauses which benefit the other party? When is a particular position a deal breaker? Course time is also devoted to a discussion of ethics – and the challenges that can be presented when representing entertainment clients. We review the sometimes fine line between business and legal matters – and the hazards of confusing the two. Many in the class are fans of the Cable TV show "Entourage" which includes a character named Ari who

is both an attorney and a talent agent. Ari parties with his clients and negotiates with a dramatic flair. Ari's interaction with his clients provides a handy opportunity for the class to discuss regulation of Agents under California and NY law and the rules governing attorneys conduct.

The course ends with a discussion how all of the drafting and negotiation principals work within the context of "new media", including international law and the internet. We end with another student and I using avatars to take the class into "Second Life" where we visit the Second Life Bar Association and avatar's law offices. Can an avatar enter into an enforceable agreement? What law applies? These and other questions make for a lively discussion of the future of negotiations and transactions.

In-Class Assignment Example

On the first day of class, I give the students an in-class exercise, which you have in the materials.²⁸ The exercise includes a document labeled "Certificate of Results and Proceeds. Both the document and the accompanying memo from the client file are based upon an actual situation. In sum, the client was excited because a TV producer used her script to film a pilot for a TV show. He then told her that he needed her signature on the Certificate of Results and Proceeds in order to take the pilot to TV networks in hopes of their turning it into a series. The students are instructed to read the materials and told: "The client can only afford half an hour of your time. Read the document and memorandum and make notes, then divide into small groups and decide what you should tell the client. The advice to the client must be no more than five sentences." The materials end with the client asking if she should sign the "Certificate".

In the following class discussion I ask the entire class, "Did you advise her to sign?" Most of the class says that their advice is: "yes, she should sign it." Their reason is that the client says that what she really wants most of all is (like most entertainment clients) fame and fortune. The students reason that this is an opportunity for her script to be made into a TV series – potentially her big break. She's broke. It's going to be great. How bad can the deal be? Then we analyze the terms of the "Certificate". They typically think that some terms are objectionable such as "work-made-for-hire" and waiving of moral rights of authors. However, both provisions are typically included in writing agreements and in the United States, writers are asked to waive their so-called 'moral rights' for reasons we discuss later in the class.

The Representation and Warranties clauses are useful in that the students often lose sight of the facts. For example, the client says that she has a co-writer so she cannot represent or warrant ownership unless the co-writer also signs the documents.

Further analysis of the document reveals that there is no fame (no credit) and no fortune (no payment). In fact, the document is arguable a gift of all rights in the script to the producer with no corresponding obligation for the producer.

Should the client sign? In addition to an opportunity to discuss the difference between business and legal issues, this exercise presents an opportunity to discuss management of transactions and of clients. What a client says they want should not blind their attorney to the facts or the reality of the transaction.

²⁸ See Kathy Z. Heller, *Teaching Transactional Skills in an Industry Context* (Conference Handouts), http://www.law.emory.edu/fileadmin/Translaw/ConferenceMaterials/2010_Conference_Speaker_Materials/Heller/Heller_Conference_Handouts.docx.

Finally, the students are asked to guess what the origins of this document might be. There is a document commonly referred to and labeled “Certificate of Results and Proceeds” that is often used to secure rights. And many of the other clauses in the document commonly occur in contracts. But this document is entirely one-sided, and poorly drafted, and lacks many essential terms. It’s probably not a stretch to assume that the Producer had access to documents drafted for one or more other transactions which he cut and pasted into this one. The result looks legal – but does not apply to this transaction from our client’s perspective. In addition to being completely one sided, it contains numerous legal deficiencies, including that the script could not be a work for hire under copyright law. So this seemingly legal document which the client is eager to sign serves as a useful starting point for many key goals of the course, including critical analysis of precedent contracts and identification of transaction deal points.

Course Materials and Assignment Structure

The course includes at least three drafting exercises of increasing complexity. For each exercise every student creates a client file which must contain the information necessary to explain the transaction. The file for each transaction must include research material (such as information from the U.S. Copyright office or the Secretary of State), detailed notes of meetings and discussion, all , emails, memorandum, correspondence and anything else which may be relevant for someone who is not familiar with the transaction to understand the contents of the draft and final contracts.

The first class assignment involves drafting an Option and Purchase agreement for the acquisition of the right to make a film or other media from a book. The students are in the role of in-house counsel at a media company and are given a memorandum prepared by the company business affairs department. The memorandum summarizes the basic agreed deal points and related information. From this memorandum the students draft an agreement and send it with a cover letter to opposing counsel.

For many students drafting the cover letter is as challenging as drafting the contract. The letter may not be longer than one page, which requires them to be concise and selective in making their points. The purpose of the letter and its general structure is discussed in class, including:

- identify yourself, your client and the issue;
- list key deal points in order of importance and for each briefly state why your client’s position is fair and should be accepted;
- if possible, anticipate and discourage likely counter-offers;
- end with a statement of what you want.

Many students initially have difficulty discerning what is important and instead repeat the contents of the contract. Others lose sight of the purpose and instead become very argumentative. Thus, the letter serves an opportunity to discuss the first step in negotiations: setting the scope of the terms of the deal and the timeline for negotiations.

The students engage in a series of transactions of increasing complexity, including exchanging drafts and redline comments. For the final exercise they are expected to complete the entire negotiation and drafting process from initial client interview to final agreement. For this exercise I provide actors with detailed briefings. One actor poses as the Film Producer client and meets with half of the class; the other poses as a client who is an

Actor (or a Writer) and meets with the other half of the class. Before meeting with the client, the students each prepare the questions they will ask meet with the half of the class which will interview the client and discusses the questions which will be asked.

The mock clients are instructed to stay in character and to only answer questions that are asked. I provide them with all of the facts needed to answer the attorney/students' questions which are relevant to the exercise. In addition, I give the mock clients pictures of their dogs and cats, of cars they want to buy, the other roles they've done, places they have traveled to, and other irrelevant but possibly interesting information, and they are encouraged to talk about subjects which are irrelevant to the exercise. The students have learned in class that it is the lawyer's job to get the necessary and correct information – not the client's job to guess what information is important. The interview lasts only 20 minutes and the students have no further communication with their 'client'. Half of the students then must each use the client information to draft and negotiate a contract for the Producer to hire the Actor/Writer. The other half of the students must each use the information from their Actor/Writer client to counteroffer and redline until a deal is reached on all points. The client file from the negotiation must include letters between counsel, drafts, redline of drafts, detailed notes of negotiations via phone and email, and a final letter to the client explaining the final negotiated deal.

Although the client interviews occur with a group of students acting as counsel, there are often significant errors and omissions in obtaining information from the clients. For example, some students interviewed a writer client holding a book which she said she wrote but the book has the name of a man as its author. The client told the students the man's name is her pseudonym; none of the students asked her for her real name and all used the pseudonym as the name of the party to the contract. Another common error occurs when students only read their questions and do not listen to the client's responses as suggestions for further inquiry. I always provide the mock clients with copies of email exchanges between the parties which provide very useful information about terms already agreed. If the students don't ask whether there have been any prior communications, they don't have the information for use when drafting – or just one party's attorneys may have the information and the other is at a disadvantage in the negotiation when it does not. A final example of a typical error: the Producer client is instructed to state that his/her father has promised to provide the \$20 million budget for the film and has already put \$100,000 in Producer's production account. Many students draft the contract as if the Producer has more than \$100,000 to spend, thus obligating their client for payments he/she is not able to make, which is a lesson in the importance of identifying and stating a condition precedent (here, funding).

During the negotiations the students also have the opportunity to utilize contract negotiation tools common in media contracts such as deferred and contingent payments, perks and obligations which are 'pro rata', 'pari passu', 'favored nations' or 'tied'.

Real Showbiz Examples

One advantage of using media transactions to teach negotiating and drafting is the abundance and quality of interesting real-life examples. Students are often surprised to learn that the very few disputes which reach the stage of a decided case are anomalies as nearly every dispute is settled or the contract contains mandatory arbitration. So, the class studies a particular clause and then we look at how it is implemented and its effect on the media industry.

Examples of common clause which have made it into the news and had an impact costing many millions of dollars are Turnaround and Right of First Refusal with Changed Elements". A "Turnaround" clause provides that rights revert to a prior owner under specified terms and conditions. For example, under a typical Turnaround clause, if a movie studio purchased a script and failed to turn it into a film within 5 years, the author or prior owner would have the right to sell the script to another movie studio provided that the first movie studio is reimbursed for any costs allocated to the script during the 5 years the it had ownership. "Turnaround and Right of First Refusal with Changed Elements" means that if another studio decides to take on the film project after turnaround and makes any changes in the 'elements' associated with the script when it was owned by the first movie studio, (such as a change in the script, the director or the budget) then the first movie studio must have the first opportunity to take back the script with those 'changed elements'.

The popular TV show "Project Runway" was off the air for many months because of a dispute over 'Right of First Refusal with Changed Elements.' The Weinstein Company, which created the show, had a one year renewable agreement (which had continued for 5 years) with NBC Universal to have the show on its channel. The agreement granted NBC the right to meet any changed elements in the event The Weinstein Company received another offer. The Weinstein Company accepted a \$20 million advance on a \$200 million dollar deal to move the show from NBC. NBC sued, stating that they were never given the opportunity to accept the "changed elements." The Weinstein Company's defense was that, instead of telling NBC that they had an offer of \$200 million, one of its principals told NBC executives that "the offer we're talking about is so huge and stupid that you would be insane to try and match it." The judge referred to the 'changed elements' clause and granted NBC a temporary restraining order. The parties eventually settled. What have we learned? Clearly, "So huge and stupid" is not a proper application of Right of First Refusal and Changed Elements clauses. This example also demonstrates how the media companies do business, and it provides an opportunity for a discussion of the relevant clauses and what might have been done to prevent the lawsuit. The same clause is the reason there will not likely be a sequel to the film "Watchmen." The Watchmen comic book was first published in 1986. Twentieth Century Fox Studios bought the film rights, and after a few years gave producer Larry Gordon the rights with Turnaround, Right of First Refusal, and Changed Elements clauses. Fox also retained the distribution rights and a share of the profits plus recoupment of its costs on the project prior to turnaround in the event the film was made by another studio.

Producer Gordon took the Watchmen project to Universal Studios which hired a writer wrote a draft script but Universal did not make the film. Gordon then took the project in Turnaround to Paramount Studios which paid Universal Studios 10% of its costs and agreed to pay the remaining 90% from profits if it made the film. Paramount hired a new writer. Shortly thereafter, Paramount Studios underwent a management change and everyone associated with the Watchmen Project was fired.

Producer Gordon then took the Watchmen Project to Warner Bros. Studios which hired a new writer and with a new script commenced filming. Paramount sued Warner Bros. saying that it had not transferred the Watchmen film rights to Warner Bros. Warner Bros. responded that Paramount never had the rights because it did not pay Universal the remaining 90% of its costs under its Turnaround agreement. Under a settlement agreement, Warner Bros. gave Paramount 25 percent ownership, plus foreign distribution rights. Fox then sued Warner Bros. stating that it still had the original rights under its Turnaround With Changed Elements agreement with Producer Gordon because Fox was not given the

opportunity to re-acquire the script when changes were made. By that time, Warner Bros. had already spent a reported \$130 million to make the film and had announced its premier and theater dates. The judge denied Warner Bros motion to dismiss, writing that: “Nothing on the base of the complaint of the document establishes the producer ever had any rights on ‘Watchmen’. It’s Fox’s.” Warner Brothers and Fox settled with Warner Bros. giving Fox \$1,500,000 for its development costs and 8.5 percent of box office receipts, including all sequels and spin-offs. So not only does Warner Bros. have to share any profits with its co-producer, Legendary Films, it also has to pay Paramount Pictures 25% of its share, and Fox 8.5% of its share. And Paramount Studios has all of the distribution rights. Despite making over \$177 million dollars, from Warner Bros. perspective the film is a financial failure and it can never be in Warner Bros. financial interest to make a sequel. Roughly, the numbers look like this:

- \$150 million to make the film

- \$177 million US and foreign box office receipts

To be considered a success, a film must make 2.5 times what it cost to make due to additional costs associated with creating prints and advertising. In addition, any money Warner Bros. does make must be shared with Paramount and Fox. So, although Warner Bros. has all of the sequel rights it can never be in its financial interest to make another film.

The Watchmen example once again demonstrates how Turnaround, Right of First Refusal and Changed Elements clauses work. In addition, it provides a very good example of in-house counsel who did not adequately review all of the documents to ensure that the Chain of Title was correct and complete, including counsel at Warner Bros, Paramount and Universal Studios. It provides an opportunity for the class to discuss what Chain of Title documents would have been necessary for the various transactions to have occurred successfully and for Warner Bros to have been sole owner.

The Watchmen example also provides an opportunity to discuss the attorneys’ role when representing entertainment clients. Producer Gordon behaved as many independent producers do – taking a project to studios and hoping to inspire interest. Fox blamed Producer Gordon for its \$150,000,000 fiasco, saying he had lied when he signed documents. Producer Gordon – blamed his lawyer, who he sued for malpractice.

The Clinic: Working with Filmmakers

Students who have taken Negotiating and Drafting Media Industry Transactions can also enroll in the Working with Filmmakers clinic. This is the only clinic of this type and it is possible in large part because we have reached out to the independent filmmaker community. Clinic students are provided with the opportunity to use the skills learned in Negotiating and Drafting in order to do all of the legal work associated with the making of an ultra low budget feature film.

Filmmakers are selected from a pool of applicants whose films meet the following criteria: already fully funded and scheduled to begin filming very soon; full length feature film – not a documentary, student film, short or video; a final budget which meets the requirements to be classified as ultra low by the Screen Actors Guild (the ceiling for ultra low classification is \$200,000

The students begin by conducting a client interview with the Producer to determine what legal work needs to be done. For each film the students typically draft documents to secure underlying rights to a script, book or life rights; set up an LLC; file the script for

copyright; and create documents to hire the writer, director, actors, and crew and for use of locations and copyrighted or trademarked materials on sets. The Clinic students typically complete work on 2 to 6 films each semester. The filmmakers each receive a binder containing all completed documents and corresponding memoranda as well as a DVD containing the documents for use in the event the filming occurs after the semester is over and they need to add crew, actors or locations.

Clinic students have the opportunity to work directly with entertainment clients and prepare a variety of agreements under very strict time limitations, since all must be completed by the end of each semester. Each of the Clinic students receives a credit on the film which they can list on their resume.

Why these clients? Filmmakers provide the Clinic students with a wide range of legal needs, rather than an isolated problem. In addition, the legal requirements to make an ultra low budget feature film do not differ much at all from the legal requirements to make other media, from a webisode on the internet to a blockbuster in the theaters. While some factors such as the length, media or budget may be different, all types of media need a secure chain of title, the legal protection provided an LLC, and enforceable contracts for all involved. Another advantage of the ultra low budget films is that the time from filming to completion can be much shorter than for a film with a bigger budget. In the short time the Clinic has been in existence, the students have worked on films which have achieved many awards and honors, including: the Newport Beach Film Festival Audience Award for Best U.S. Film; Netflix Find Your Voice Film Competition; Denver International Film Festival People's Choice Award; LA Film Festival premier film; Tribeca Film Festival Official Selection; AFI Film Festival Official Breakthrough Selection; Urbanworld Film Festival Narrative Audience Award; Chicago International Film Festival Official Selection, and the Indian Film Festival of Los Angeles.

APPENDIX A

Using Transactions to Teach Secured Transactions

Eric Gouvin
Emory Transactional Conference
June 5, 2010



Slide 1

Challenges of Teaching Secured Transactions

- Rodney Dangerfield Syndrome
- Knowing Your Audience
 - "Bar" Course vs. True Upper Level Elective
 - Different levels of sophistication, interest, appreciation and apprehension
- Creating Context for the Content

Slide 2

Creating Context – Making it Real

- Be Realistic
 - About what your class can do
 - About the situations you put them in
- But if you've got an achievable goal, make your expectations explicit
- Know why you expect what you do
- Be ready to provide backup and reassurance

Slide 3

Strategies for Bar Classes

- Find a way to connect to their personal experience – car loans are good examples
- Reassure them that the business concepts are in many ways easier than the legal ones
- Need to know some business in order to understand the legal dispute
- No one litigates business cases on the basis of principle (but maybe for *principal*)
- Keep it conceptual

Slide 4

Strategies for True Upper Level Elective

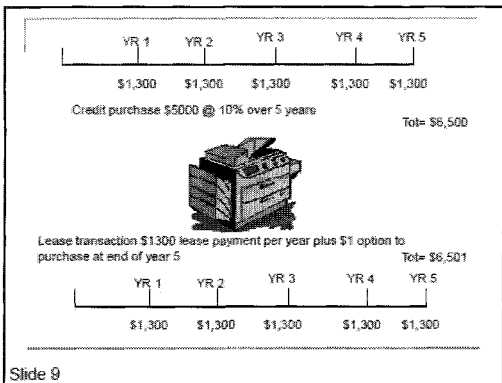
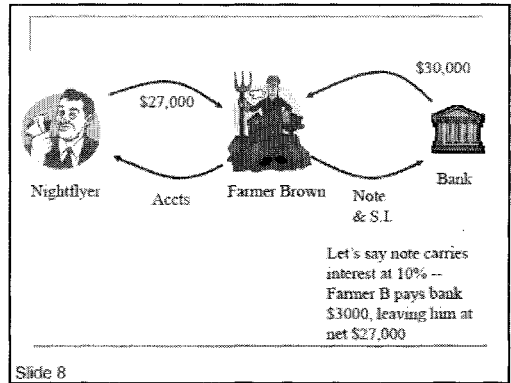
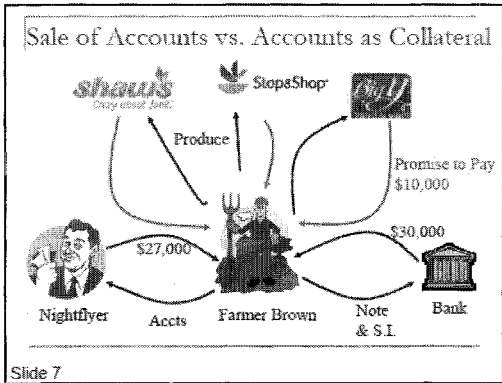
- Audience now is self-selected
 - Beware of the convenient time slot or bar prep
- Can go deeper into business ideas
- Bring in financial statements, if helpful
- Role of problem method and simulations
- Bring in guest lecturers to do heavy lifting and answer practical questions
- Keep lawyer's role in perspective

Slide 5

Mini-Lectures on Key Ideas

- Some things they just need to know:
 - How Banks Look at Credit Applications
 - Article 9 – like transactions:
 - Sale of Accounts
 - Consignments
 - Leases
- IMHO, teasing these ideas out of cases will likely be a waste of time

Slide 6



Primary Strategy – Problems and Simulation

- Problem method is best way to teach this material.
- I designed a rich hypothetical as an overlay on the Whaley book.
 - Whaley's problems nice to illustrate specifics points, but...
 - Wanted to deliver something much more realistic

Slide 10

Why Problem Approach?

- This is the "Language Lab"
- Develops empathy for parties
- Allows students to see themselves in the role
- Makes the issue more "real," less "abstract"
- Forces students to read documents and statute
- Keeps class from being too formulaic
- Aha...but there is a formula – it's all theatre

Slide 11

Meet the Client – Fruit de Mer, Inc.

- On first day, students get a packet with factual background and set of documents:
 - Background information/ website.
 - Maps/Site plans
 - Mortgage
 - Equipment Leases
 - Specification sheet for boat
 - Bill of Sale/Certificate of Title for boat
 - Consignment Agreement
 - Financial Statements of Fruit de Mer, Inc.

Slide 12


Fruit de Mer, Inc.

117 Commercial East
Atlantic City, New Jersey

Fruit de Mer's fresh fruit is brought to the market with safety of choice. Only in Atlantic City, New Jersey, where the quality from the highest sources, under strict supervision, is of the highest quality.


We grow our oysters using modern methods and techniques to insure that our oysters are healthy, clean, and free from any disease. Any disease which might be introduced into our oysters is immediately destroyed by the use of the most modern methods available. We use the most modern methods available to insure that our oysters are healthy and free from any disease.

Fruit de Mer oysters are available for purchase in Atlantic City, New Jersey, and in other parts of the country. We are proud to be the only oyster grower in Atlantic City, New Jersey, who has been awarded the highest award by the State of New Jersey for the quality of our oysters.



Slide 13

Growing Oysters from Seed




From Seed to Shell

It is a long and arduous process to grow oysters from seed. It takes about 18 months to grow oysters from seed to shell. We use the most modern methods available to insure that our oysters are healthy and free from any disease. We use the most modern methods available to insure that our oysters are healthy and free from any disease.



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Slide 14

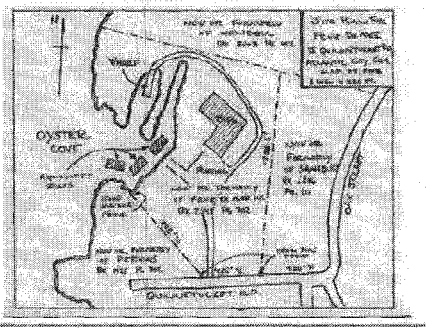
The oysters are grown in the most modern methods available to insure that our oysters are healthy and free from any disease. We use the most modern methods available to insure that our oysters are healthy and free from any disease.



Slide 15

Slide 16



Slide 17

OYSTER FARM, 12 QUANTITIES, PROPERTY, CITY, N.J. MAP BY JOHN J. DEWITT, 1910

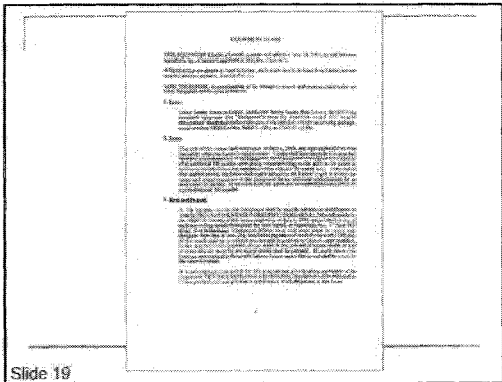
INTRODUCTION

This map is a plan of the Oyster Farm, showing the various ponds, canals, and other features. It is a valuable tool for the management of the farm.

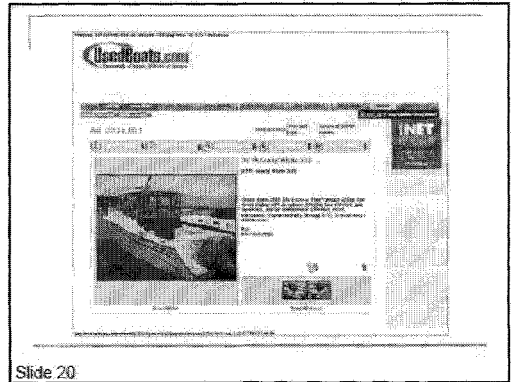
SYMBOLS

The symbols on this map are as follows: a square represents a pond, a line represents a canal, and a circle represents a well. The numbers 1 through 12 represent the different quantities of oysters.

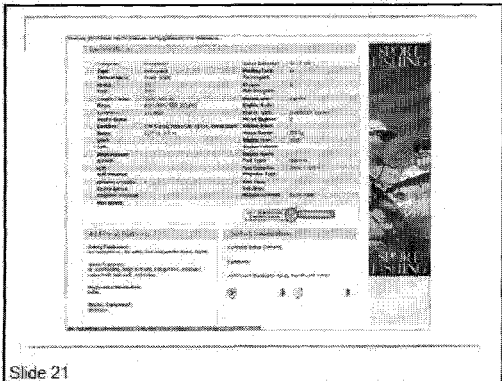
Slide 18



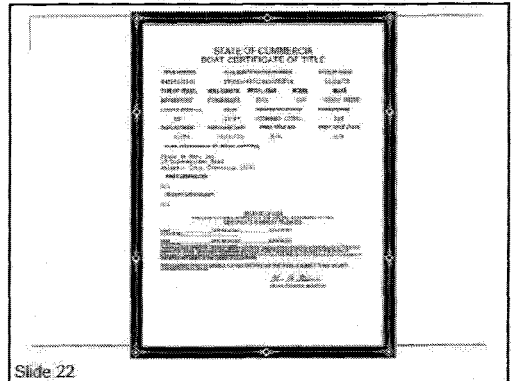
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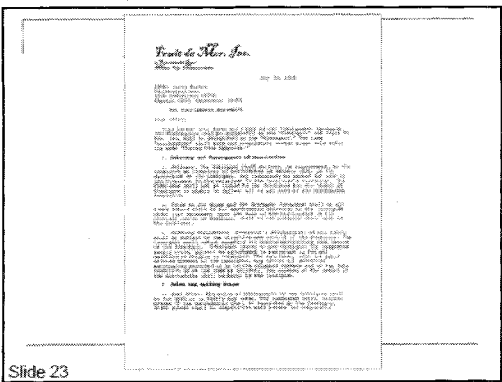
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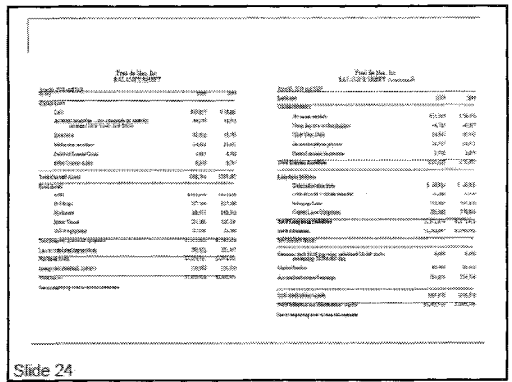
Slide 21



Slide 22



Slide 23



Slide 24

Focusing on Specific Problems

- Once the background is in place, the instructor can provide additional documents to focus on specific issues:
 - Typical secured transaction
 - Statutory liens
 - Deposit control agreements

Slide 25

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Slide 26

Office of the Secretary of State

Office of the Secretary of State

I, *[Signature]*
Secretary of State

Slide 27

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Slide 28

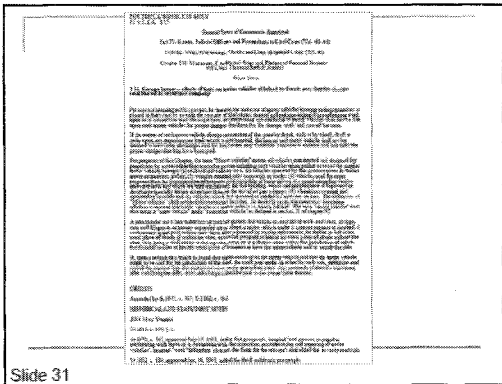
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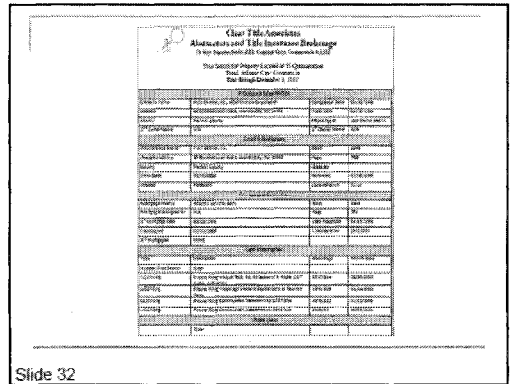
Using the hypothetical for testing

- Building on the material the students have been working with all semester, you can ask a last set of questions as the exam.
- I give a few more facts and a few more documents on the last day of class.
- Take home exam gives students a chance to dig in to the material
- Statutes, cases can be invented

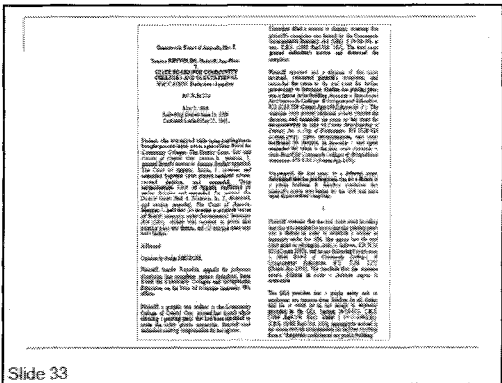
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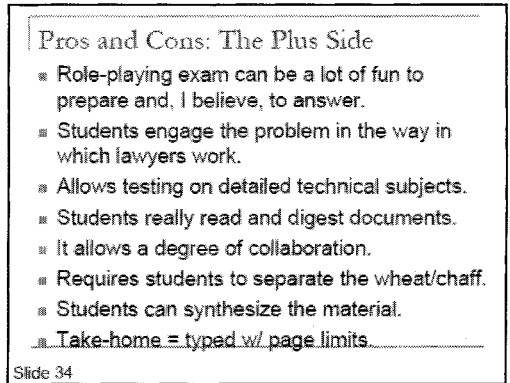
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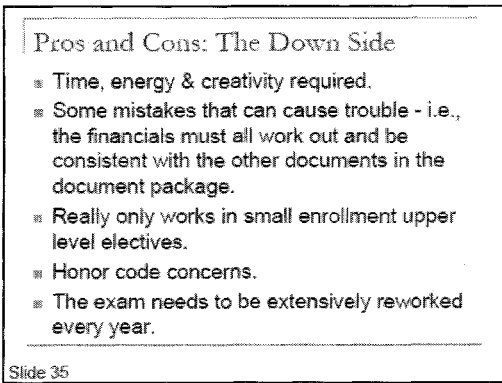
Slide 32



Slide 33



Slide 34



Slide 35