A TRIBUTE TO THE SCHOLARSHIP OF PROFESSOR DALE OESTERLE

by

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I. INTRODUCTION

Dale Arthur Oesterle—professor, scholar, lawyer, husband, father, grandfather, *race car driver*. Wait . . . What? That was my reaction when I discovered that Professor Oesterle was more than just a remarkable legal scholar and teacher. During his illustrious career, he has proven nothing short of brilliant and dynamic, a scholar unafraid to confront difficult issues head on and challenge orthodoxy. And he is a race car driver to boot? How can the rest of us mere mortals possibly compete?

My journey to Professor Oesterle, in general, and his scholarship, in particular, began with my background in mergers and acquisitions. Having practiced in the M&A area at both Cravath, Swaine & Moore and later at Latham & Watkins, it was natural for me to teach the M&A course when I entered academia after accepting a professorship at New York Law School. Having been tasked by the administration with teaching an upcoming M&A class, I immediately went on the hunt for the best M&A casebook available. After looking through all the available candidates, it became crystal clear to me that Professor Oesterle's M&A casebook was head and shoulders above the rest. What I later learned, and what is still inconceivable to me, was that Professor Oesterle did not have a traditional M&A background. Thus, his authoring the top-selling M&A casebook was about as likely as me authoring a top-selling casebook on Space Law.

If you read through Professor Oesterle's extensive list of scholastic achievements—from books to articles to book reviews to monographs—you encounter the sheer breadth of his remarkable scholarship. The purpose of this tribute is two-fold. First, I will attempt to demonstrate the tremendous breadth of his scholarship by reviewing three of his most disparate articles. The first is *Viewing CERCLA as Creating an Option on the Marginal Firm: Does It Encourage*

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[1] Professor of Law, New York Law School. Professor Haas has the privilege of being a co-author with Professor Oesterle on two books: DALE A. OESTERLE & JEFFREY J. HAAS, THE LAW OF MERGERS AND ACQUISITIONS (5th ed. 2018); DALE A. OESTERLE & JEFFREY J. HAAS, MERGERS AND ACQUISITIONS IN A NUTSHELL (3d ed. 2019).

Irresponsible Environmental Behavior?[2] The second is *Structuring the Ballot Initiative: Procedures That Do and Don't Work.*[3] The last is *Tax-Free Reorganizations: The Evolution and Revolution in Triangular Mergers.*[4]

Second, I will use those articles to highlight Professor Oesterle's healthy skepticism of our governmental institutions, whether at the federal or state level. Although I have no independent verification of this, I suspect he would warmly embrace President Ronald Reagan's famous statement from 1986: "The nine most terrifying words in the English language are 'I'm from the government, and I'm here to help.'"[5] Indeed, Professor Oesterle is unabashed in his criticism of our governmental institutions when he believes criticism is warranted.

A. Option Theory, Limited Liability and CERCLA

In his article *Viewing CERCLA as Creating an Option on the Marginal Firm: Does It Encourage Irresponsible Environmental Behavior?*,[6] Professor Oesterle focuses his attention on the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA).[7] CERCLA is a federal statute designed to impose cleanup costs on the parties responsible for contamination caused by their release of hazardous substances. In his article, he underscores that the "government ultimately must pick up the tab"[8] when firms default on their environmental cleanup obligations. Because of this, he believes "the government is playing the role of sucker."[9] As you can see, pulling punches is not the way Professor Oesterle rolls.

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[2] Dale A. Oesterle, *Viewing CERCLA as Creating an Option on the Marginal Firm: Does it Encourage Irresponsible Environmental Behavior?*, 26 WAKE FOREST L. REV. 39 (1991).

[3] Dale A. Oesterle & Richard B. Collins, *Structuring the Ballot Initiative: Procedures That Do and Don't Work*, 66 U. COLO. L. REV. 49 (1995).

[4] Dale A. Oesterle & Stephanie Hoffer, *Tax-Free Reorganizations: The Evolution and Revolution in Triangular Mergers*, 108 NW. U. L. REV. 1083 (2014).

[5] Ronald Reagan, President of the United States, News Conference at Illinois State Fair (Aug. 12, 1986).

[6] Oesterle, *supra* note 2, at 39.

[7] Comprehensive Environmental Response, Compensation, and Liability Act, 42 U.S.C. §§ 9601–9675 (1980).

[8] Oesterle, *supra* note 2, at 39.

[9] *Id*.

In support of his belief, Professor Oesterle highlights the interplay between option theory and the business law concept of limited liability. An option, according to option theory, is a derivative instrument, the subject matter of which is an underlying asset—stocks, land, commodities, etc.[10] An option has two counterparties: the option writer and the option holder.[11] The option writer receives an option premium from the option holder. This premium is the consideration the option holder pays to the option writer for issuing the option in the first place.[12] The option holder, by contrast, has the right, but not the obligation, to exercise the option if the economics of doing so make sense.[13] Alternatively, the option holder can simply let the option lapse thus losing the option premium she has previously paid to the option writer. As Professor Oesterle points out, the parties enter into the "[option] contract because they are acting on differing predictions as to the future value of the underlying [asset]."[14] "When the [option] holder profits, the [option] writer loses, and vice versa."[15]

The particular form of option to which Professor Oesterle is referring is a call option. The holder of a call option is betting that the value of the underlying asset (the "spot" or "market" price[16]) will rise above the option's strike or exercise price during the term of the option.[17] Thus, a call option represents the option holder's bullish bet that the price of the underlying asset will increase during the term of the option.

If the value of the underlying asset does indeed rise above the strike or exercise price of the call option during the term of the option, the option is said to be "in-the-money."[18] The option holder will therefore exercise the call option by paying the strike or exercise price to the option writer. If the call option is physically-settled, the option

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[10] *See* JEFFREY J. HAAS, CORPORATE FINANCE HORNBOOK 132 (2d ed. 2021).

[11] *See id*. at 133.

[12] *See id*. at 132.

[13] *See id*.

[14] Oesterle, *supra* note 2, at 41.

[15] *Id*.

[16] *See* HAAS, *supra* note 10, at 133.

[17] *See id*. The other type of option is the put option. The holder of a put option is betting that the spot price of the underlying asset will fall below the option's strike or exercise price during the term of the option. Thus, a put option is a bearish or negative bet on the price movement of the underlying asset during the term of the option. *See id*. at 134.

[18] *See id*. at 133.

writer must deliver the underlying asset to the option holder.[19] Thus, the option holder will receive an underlying asset having a market value that exceeds the price the option holder has paid. If the call option is cash-settled, as many are, the option holder will receive cash from the option writer rather than the actual underlying asset.[20] The cash amount will equal the positive difference between the underlying asset's market value and the strike or exercise price the option holder has paid. However, one must factor in the option premium that the option holder has previously paid to the option writer when calculating the profit the option holder has made.[21]

If the value of the underlying asset does not rise above the strike or exercise price during the option term, the call option is said to be "out-of-the-money."[22] In that case, the option holder will let the call option expire, while the option writer will pocket the option premium she received for writing the option in the first place. When the value of the underlying asset exactly equals the strike or exercise price, the call option is said to be "at-the-money."[23] However, if the term of the option has not yet expired, the option holder will not exercise the call option as she could buy the underlying asset in the open market at that price without losing the option premium she paid to the option writer. If the call option expires when it is "at-the-money," the option holder will lose the option premium.

Turning to the business law concept of limited liability, Professor Oesterle explains that certain entities, most notably the corporation, provide to their owners—shareholders in the case of the corporation—a shield of limited liability. If a firm fails while still owing debts to creditors, those creditors normally must satisfy their claims solely from the assets of the firm itself. Shareholders of a corporation will, of course, lose their investments in the corporation as those investments are part of the assets of the corporation. However, subject to certain exceptions such as veil piercing, the limited liability veil of the corporate form will shield shareholders' personal assets from the claims of unpaid corporate creditors.

Professor Oesterle then brings option theory together with the concept of limited liability first in the context of the debtor-creditor relationship. The debtor in question is the corporation, while the

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[19] *See id*. at 136–37.

[20] *See id*. at 137.

[21] *See id*.

[22] *See id*. at 133.

[23] *See id*.

creditors are holders of the corporation's outstanding debt securities (most notably bonds).[24] He argues that ownership of a firm that has debt securities, such as bonds, held by investors can be viewed through the lens of option theory. Indeed, he posits that "bondholders can be said to have written [a call] option to the equity holders on the firm itself."[25] Thus, the underlying asset supporting the option is the corporation that has issued bonds, and the value of that underlying asset is the total value of the firm as it undulates over time. The strike price of this "Bond Option" is "equal to the repayment obligations on the bonds."[26] He adds:

> On the maturity date of the bonds, the shareholders can choose to pay off the bonds or throw the firm into bankruptcy, in which case the firm will pass to the bondholders. Even if the firm itself has insufficient assets or income to pay off the bonds, the shareholders are not personally liable on the bonds [due to the limited liability the corporate form provides to them]. Accordingly, the shareholders will choose to pay off the bonds only if the ongoing value of the firm exceeds the amount needed to pay off the bonds at the time of the bonds' maturity.[27]

In sum, shareholders will exercise their Bond Option on the firm only if the value of the underlying asset on which that Option was written (*i.e.*, the value of the firm itself) has risen above the strike or exercise price of that Option (*i.e.*, the amount still owed on the bonds). Otherwise, they will abandon ship.

Ownership viewed through the Bond Option lens showcases the built-in incentive for corporate management to engage in "strategic behavior"[28] in order to maximize firm value. If successful, the value enhancement exceeding the fixed cost of debt flows solely to the shareholders. If unsuccessful, the bondholders and other creditors are left holding the bag. Given this bargain, corporate management is more likely to pursue high-risk projects and/or leverage the firm through the

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[24] As Professor Oesterle notes, "Fischer Black, John Cox, Robert Merton, and Myron Sholes, in a series of articles on option pricing circulated in the early 1970's, suggested the correspondence between corporate debt and options." Oesterle, *supra* note 2, at 39 n.1.

[25] *Id.* at 41.

[26] *Id*. at 42.

[27] *Id*. at 41.

[28] *Id*. at 46.

incurrence of additional indebtedness than it otherwise would.[29] Fortunately, creditors including bondholders can protect themselves prospectively: "Bondholders protect themselves from increasing volatility with indenture covenants [*i.e.*, through contract] or by pricing the risk of [managerial strategic] behavior when they buy the bonds."[30]

Professor Oesterle then takes the next logical step (a "short step"[31] in his mind) by applying the interplay between option theory and the concept of limited liability to CERCLA obligations. He boldly asserts that "[l]imited liability and environmental obligations [both] create an option [the "CERCLA Option"] on the firm."[32] A CERCLA Option is similar to the Bond Option discussed above:

> When a firm incurs environmental cleanup costs, its equity holders can be said to hold an option. If the costs exceed the value of the firm, the equity holders will let the firm take bankruptcy. That is, the equity holders will let the option lapse, since maintaining ownership is not cost-efficient and they are not personally liable on the debt. If the costs of cleanup are less than the value of the firm, the equity holders will exercise the option, pay the costs, and claim the underlying asset, the firm.[33]

Under Professor Oesterle's CERCLA Option theory, the primary option writers consist of the various government entities that must step in to save the day by assuming the cleanup obligations of defaulting corporations.[34] Of course, that ultimately means us—the taxpayers—are mostly footing the bill,[35] which one can infer Professor Oesterle finds deeply distressing. He further notes that on a more limited scale private parties who are injured by environmental

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[29] *See id*. at 44.

[30] *Id*.

[31] *Id*.

[32] *Id*. at 39.

[33] *Id*. at 44–45.

[34] *See id*. at 45.

[35] A trust fund called the "Superfund" is responsible for cleanup expenses when defaulting corporations cannot pay their obligations. The money for the Superfund comes from three sources: (1) amounts Congress appropriates from general tax revenues; (2) the proceeds from a corporate environmental tax and from excise taxes on petroleum products and other inorganic chemicals; and (3) monies collected from identifiable, solvent parties responsible for contamination. *See id*. at 45–46.

contamination are potential creditors as well and, therefore, potential option writers, assuming those parties cannot collect from a government fund for their damages.[36] Like in a traditional option context, the government receives an option premium for the CERCLA Options it writes. That premium consists of the taxes the government collects from parties who are potential contaminators.[37]

Professor Oesterle spends time describing the important differences between the CERCLA Option and the Bond Option.[38] The most substantive difference in my mind relates to the ability of the option writer to protect itself. In the context of a Bond Option, bondholders can protect themselves prospectively by "negotiat[ing] call premiums and covenants in individual cases."[39] In other words, bondholders are well aware of the potential strategic machinations in which corporate managers may engage, and thus they take prophylactic steps to protect themselves accordingly. Moreover, Professor Oesterle states that the option premium charged by prospective bondholders "is more substantial if the firm has a poor reputation for abusing its debt holders or is heavily leveraged . . . . [M]arginally solvent firms pose the greatest risk that option holders, the shareholders, will choose not to exercise their option by refusing to pay the mature debt."[40]

At least when it comes to CERCLA liabilities, our government as an option writer is clearly less astute at protecting itself than bondholders. Indeed, according to Professor Oesterle, the "government . . . is an ineffectual negotiator at best. The government's inability to protect itself as an option writer from strategic behavior by the option holder, the firm's investors, is perhaps the single most important limitation on the future success of environmental statutes like CERCLA."[41] He adds that "[u]nfortunately . . . our government is an easy mark that does not, and cannot, charge full value for its services as an underwriter."[42] He expands on this problem thusly:

> In contrast [to bondholders], the government is a painfully gullible writer of options. The government

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[36] *See id.*

[37] *See id.*

[38] *See generally id.* at 46–57 (discussing the two important differences between Bond Options and CERCLA Options).

[39] *Id.* at 46.

[40] *Id.* at 51–52.

[41] *Id.* at 46.

[42] *Id.* at 51.

> neither effectively prices the risk of opportunistic behavior by option holders nor effectively negotiates for risk-reducing covenants. Firms with a thin equity cushion that are in jeopardy of not being able to pay their environmental obligations are taxed the same as firms that maintain a sufficient equity cushion. . . . No individual firm pays more taxes because it has a higher risk of defaulting on its environmental obligations than do other firms. That is to say, the [option] premiums paid by option holders are not priced according to risk. . . . Moreover, there is no specific legislation aimed at promulgating the equivalent of risk-reducing option covenants to protect the government as an option writer. Firms that produce hazardous waste do not, for example, need to acquire special insurance or maintain asset reserves as a guarantee that they will meet their environmental obligations.[43]

In light of this, Professor Oesterle asserts CERCLA creates "a significant distortion in incentives for marginally solvent firms. With no price penalties or covenants to restrain them, marginally solvent firms have an incentive to maximize the value of their option at the expense of the government."[44] One way these firms do so is by purposefully increasing the volatility of their returns. This allows the option holder to reap all the potential upside without having to worry about the potential downside. Indeed, the government bears the downside. These firms also can "loot [their] firm[s]"[45] by "first separat[ing] the firm's valuable assets from its environmental obligations and then distribut[ing] those assets to themselves"[46] before their environmental obligations mature. Of course, state legal capital statutes, fraudulent conveyance laws, and state corporate provisions on dissolution help protect from looting. However, Professor Oesterle believes "the effectiveness of these protections is limited by our legal system's (and our accounting system's) refusal to require that potential environmental claims be reflected in a firm's current balance sheet."[47]

Fortunately, Professor Oesterle offers solutions to this quagmire. One potential solution would involve the government itself.

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[43] *Id*. at 52–53 (footnote omitted).

[44] *Id*. at 53.

[45] *Id*. at 55.

[46] *Id*.

[47] *Id*. at 56.

The Superfund could be supported by a special excise tax that is priced based on an individual firm's risk profile. Thus, riskier firms would pay an option premium higher than that paid by less risky firms. However, this approach is quickly dismissed by Professor Oesterle:

> Even if we charge our government with such responsibility, we are bound to be disappointed. The government, being the only option writer, will not have the benefit of an active competitive market to establish its price. It does not seem likely that the government could field experts who have the savvy to price risk outside a competitive market. Furthermore, political considerations . . . will eventually influence the pricing decisions. Firms in one state will enlist their elected congressmen to reduce their environmental tax in an effort to gain a competitive edge over firms in another state.[48]

Not surprisingly, Professor Oesterle favors a private market solution—what I will call the "environmental insurance approach"—to the CERCLA Option problem:

> The best alternative may be the forced creation of a private insurance market for environmental obligations. The government could charge admittedly excessive firm-specific environmental taxes (based on very liberal predictions of future environmental charges for any one firm) but allow firms to escape this tax completely by negotiating a private insurance policy for all cleanup charges. In other words, the government would view itself as an insurer of last resort and extract fees sufficient to encourage insurance companies to enter into the business of writing policies that cover default on environmental obligations. The firms could opt out of the government assessments by purchasing a specific type of insurance coverage. Although this would not eliminate the troubling considerations concerning the government's ability to set risk-related environmental assessments, it would help. If the government's rates are high, even though a bit arbitrary, a competitive private insurance market that

[48] *Id*. at 58.

> develops underneath the government will significantly reduce the government's participation.
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> For an ongoing firm, the qualifying insurance policies would be different than traditional insurance because the insurance company would pay only if a firm defaulted on its environmental obligations. The firm itself would remain the primary obligor. . . .[49]

While largely underwriting CERCLA risk through the private market for insurance is certainly a sensible solution, Professor Oesterle realizes this solution is imperfect. Insurance companies have been known to collapse financially when confronted by large claims, and thus insurance companies playing in this sandbox would need to have a minimum net worth in light of the environmental policies they underwrite. This would require special legislation.[50] In addition, international firms not facing this insurance requirement in their home countries would have a leg up competing against domestic firms. Indeed, he realizes that "[j]obs and capital"[51] could certainly move offshore. However, at least our government would be "out of the business of agreeing to cover, without adequate compensation, future cleanups for insolvent corporations."[52] This, in the mind of Professor Oesterle, is clearly a salutary goal.

B. *Supercharging Our Democracy through the Ballot Initiative*

Pivoting from CERCLA liability to citizen-based ballot initiatives is certainly a complete 180, but so goes Professor Oesterle's scholarship. In his article *Structuring the Ballot Initiative: Procedures That Do and Don't Work*,[53] Professor Oesterle notes that "[t]he [ballot] initiative empowers citizens, by petition, to require a popular vote on whether to adopt a statute or constitutional amendment they have drawn up."[54] Labeling these initiatives as a form of "direct democracy,"[55] he adds that "[t]he initiative device has become a major outlet for citizens dissatisfied with their governments, and its use is likely to increase, both in frequency and geography."[56] He therefore

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[49] *Id.*

[50] *See id*. at 59.

[51] *Id*. at 60.

[52] *Id*. at 67.

[53] Oesterle & Collins, s*upra* note 3.

[54] *Id*. at 49.

[55] *Id.*

[56] *Id*. at 48.

sets out to provide important recommendations to state governments, in general, and the state government of Colorado,[57] in particular, on how best to structure ballot initiatives.

Professor Oesterle explains that initiatives can be either direct or indirect. The direct initiative allows the proponents of the initiative to go directly to a popular vote, subject to first having obtained a qualifying number of voters' signatures on a petition.[58] By contrast, "[t]he indirect initiative requires that citizens first petition the [state] legislature. Only if rebuffed [by the legislature] may they force a popular vote, although at that point the citizens' proposal has the same right to popular enactment as under the direct initiative."[59]

Professor Oesterle also explains that most states that embrace initiatives allow initiatives to enact statutes and/or to amend state constitutions. However, "[w]hen initiators have a choice between enacting a statute or amending the state constitution, they incline strongly toward entrenching their handiwork in the constitution."[60] Indeed, "[t]he constitutional initiative is the dominant form of state-wide initiative today, and it presents the most controversial issues about the initiative and its uses."[61] Professor Oesterle explains the import of this development thusly:

> The state-wide, constitutional initiative works a significant change in the traditional American concept of governmental structure. Differences between constitution and legislation are much reduced. The notion of a constitution as fundamental law that is seldom changed, and only with substantial consensus, is gone. Constitutions are amended often and by voting majorities that are typically a minority of a state's adult population. The role of the state's judiciary is reduced, and the executive veto is bypassed.[62]

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[57] Professor Oesterle was a tenured professor at the University of Colorado School of Law at the time he co-authored this article, and thus I surmise that his interest in local politics helped motivate him to write the article.

[58] *See* Oesterle & Collins, *supra* note 3, at 70.

[59] *Id*. at 50 (footnotes omitted).

[60] *Id*. at 52.

[61] *Id.*

[62] *Id*. at 52–53 (footnote omitted).

While reserving judgment on whether this is a positive or negative development,[63] Professor Oesterle does acknowledge the development's oddity:

> State constitutions filled with provisions that look like ordinary legislation, and easily amended by a small percentage of the voters, diverge greatly from what most Americans think a constitution is. By our traditions, a constitution establishes the structure for government to act subject to basic and general prohibitions in a bill of rights. It is supported by consensus and should seldom need amending. Constitutional language is broad and general, destined to endure.[64]

To the largely uninformed, myself included, ballot initiatives have tremendous appeal—at least superficially. Viewing initiatives as a form of direct democracy in particular has a resonating quality:

> Proponents often claim that the initiative is a more democratic way of governing than representative elections, that it is a way of perfecting democracy. We sometimes say that representative democracy is indirect democracy, while initiatives are a form of direct democracy. It is natural to assume that direct is better, more nearly perfect, than indirect—that the ideal of consent of the governed is better achieved by consenting to the laws themselves, rather than to representative lawmakers. This argument from the logic of democracy surely has much to do with the initiative's popularity.[65]

Not surprisingly, the biggest proponents of direct democracy seek to have very modest procedures attach to the initiative process. They argue that there should be no limits on the content of initiatives. The government should be required to subsidize petitions and their publication. Government officials should be prohibited from commenting on initiatives or becoming involved in the campaign to pass them. Low qualifying thresholds for accessing the ballot should be the norm, and a simple majority of votes cast should be sufficient

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[63] *Id*. at 53.

[64] *Id*.

[65] *Id*. at 55.

to pass initiatives. Once passed, initiatives should be protected from repeal or revision by elected officials.[66]

Of course, opponents believe that initiatives represent the "tyranny of the majority and [are a] threat to the republican form of government."[67] Indeed, they believe much more in representational democracy. For them, limited ballot access for initiatives should be the norm. Higher voting thresholds for their passage should be required. Only the indirect form of initiative, rather than the direct form, should be allowed. Government officials should be able to amend or even repeal passed initiatives with ease.[68]

As Professor Oesterle astutely points out, most of the tug of war between initiative proponents and opponents is over the procedural elements associated with the ballot initiative. Throughout his article, he shines a bright light on these procedures.[69] He states that the error most make is their "assumption that all initiative processes are indistinguishable. . . . Some initiative processes work substantially better than others. The adequacy (or inadequacy) of procedure is central to the debate over whether initiatives are useful or harmful."[70] Ultimately, "[t]he impact of the initiative process on a representative system is controlled by these procedural choices."[71] Indeed, "[a]buses of the initiative are largely caused by structural and procedural flaws. If they are corrected, the initiative can work as an important check on representative and administrative government."[72]

Professor Oesterle then sets forth his main recommendation for creating, in his view, "the best mix of representative and direct democracy."[73] Whether you agree or disagree with him, it is hard to argue that his recommendation is not thoughtful. Overall, he argues that initiatives should be viewed simply as a check on representative government—a "safety valve, but not a substitute or even an equal partner."[74] Of course, with that recommendation he has immediately

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[66] *See id*. at 104–05.
[67] *Id*. at 49 (footnote omitted).
[68] *See id*. at 105.
[69] *See id*. at 64–104.
[70] *Id*. at 49 (footnote omitted).
[71] *Id*. at 105.
[72] *Id*. at 126.
[73] *Id*. at 105.
[74] *Id*. at 106.

lost the hyper pro-initiative crowd. However, he backs up his recommendation with a healthy dose of common sense:

> When discontent with elected officials reaches high levels of intensity on selected issues, the initiative process provides a pressure release. The threat of an initiative, even when unused, has some effect on aligning the interests of elected officials and their electorate. Those who believe that policy-setting through the initiative process ought to dominate or be an equal partner with policy-setting through representative government run afoul of the process's basic and unavoidable paradox: The more the populace uses the initiative process, the less effectively it works.[75]

Unfortunately, Professor Oesterle leaves unanswered some important questions relating to his "safety valve" approach to initiatives. For example, exactly how "high" must the level of intensity reach before the citizens can engage in the initiative process? In addition, how many initiatives must be presented to citizens before the initiative process starts to work less effectively? He suggests a "flood"[76] of initiatives would overwhelm the citizenry, but otherwise provides no guidance. Clearly, there is a diminishing marginal returns explanation as to why the citizenry is overwhelmed when confronted with too many initiatives. However, I suspect the lack of interest in at least some of the initiatives is likely due to the substance of the initiatives themselves. Indeed, hotly contested issues bring voters out in droves. Just see Trump versus Biden 2020.

Professor Oesterle then presents five recommendations relating to the procedural aspects of initiatives that would bolster his safety valve approach. First, he believes that only indirect initiatives should be allowed. Indirect initiatives involve the legislature as gatekeeper. By requiring proponents to present their proposed initiative to the legislature first, the legislature can hold hearings on that initiative and deliberate over it. This will help ensure that the proposed initiative is drafted in a clear and understandable manner and that unintended consequences relating to it can be eliminated. Legislators can also

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[75] *Id*. (footnote omitted).

[76] *Id*. at 106 n.279.

share any intense points of disagreement they have with the proposed initiative with the initiative's proponents.[77]

Second, Professor Oesterle seeks safeguards on initiatives that would amend a state constitution. This would ensure that amendments to the constitution were made infrequently through the initiative process, clearly an outcome that he favors. A minimum vote, such as a super majority vote of the votes cast, would be required to pass an initiative that amended the constitution. By contrast, only a traditional majority vote of the votes cast would be needed to pass a statutory initiative. In addition, constitutional initiatives would be strictly limited to a single subject and limited in length to five hundred words overall. Lastly, he recommends that constitutional initiatives be drafted by the state's attorney general, legislative counsel or other official.[78] Of course, having one of these "governmental professionals" draft initiatives would seemingly lessen or even eliminate the need for the single subject and word count requirements. But I guess, in this context at least, Professor Oesterle believes in wearing both a belt and suspenders.

Third, Professor Oesterle suggests that state legislatures be empowered to amend initiated statutes, noting that opposition to allowing them to do so is "based on an unrealistic fear of legislatures."[79] Oddly, he himself seemingly lacks full trust in legislatures as well, as he suggests that their ability to amend initiated statutes be limited in two substantive ways. First, in order to achieve clarity of purpose and transparency, a given legislature would not be allowed to combine a proposed amendment to an initiated statute with any other legislation. Second, the ability of the citizenry to vote on a referendum to rescind, in turn, what the legislature has done to an initiated statute would be made easier. According to Professor Oesterle, having these two checks in place would likely lead to advance negotiations between proponents of the initiated statue the legislature is seeking to amend and the legislators themselves, which he clearly views as a positive.[80]

Fourth, Professor Oesterle advocates for a "single-issue rule"[81] applicable to a given initiative, whether statutory or constitutional in nature. Allowing initiators to combine multiple subjects within a single

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[77] *See id*. at 107.

[78] *See id*. at 108–09.

[79] *Id.* at 110–11 (footnote omitted).

[80] *See id*. at 111.

[81] *Id*.

initiative, as is currently allowed, results in voters having to cast an all or nothing vote. Indeed, "voters must decide whether to swallow the bitter to get the sweet." Under the "single-issue rule," each subject would be voted on separately. In order to keep costs down, however, multiple subjects could be joined in a common petition, but voters would be entitled to vote on each subject separately.[82]

Lastly, in order to bolster the initiative process, Professor Oesterle suggests that the time periods within which to qualify an initiative be expanded to a one- or two-year period.[83] Moreover, during the qualifying period, reasonable procedures must be put in place. These procedures would allow "for review of draft [initiatives], public notice and hearing, consultation among proponents, officials, and opponents, and opportunities to amend proposals or to withdraw them in favor of legislative substitutes that are satisfactory to proponents."[84]

All in all, Professor Oesterle's article represents his deep belief that democracy can be improved through the elimination of the flaws and abuses inherent in ballot initiatives. Doing so would allow ballot initiatives to provide "an important check on representative and administrative government."[85] By promoting this admirable goal, "Citizen Oesterle" is truly benefitting all of us.

C. Harmonizing the Taxation of Corporate Reorganizations

The last article I will address is *Tax-Free Reorganizations: The Evolution and Revolution in Triangular Mergers.*[86] The M&A underpinnings of this article are near and dear to me. The tax aspects not so much. But whether you are a tax lawyer or simply a taxpayer, applying our federal tax laws in a neutral and consistent way is a worthy goal indeed. Through his article, Professor Oesterle exposes one glaring situation where neutrality and consistency is lacking—the taxable treatment of triangular mergers. Beyond this, his article argues that "difficulties in the taxation of triangular mergers are [but] a microcosm of larger structural problems in corporate tax law—namely, difficulties created by conflicting conceptualizations of corporate personhood and Congress' inability to nimbly respond to changes in business."[87]

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[82] *See id.*

[83] *See id.* at 112.

[84] *Id.*

[85] *Id.* at 126.

[86] Hoffer & Oesterle, *supra* note 4, at 1085.

[87] *Id.* at 1084–85.

Before addressing the substance of Professor Oesterle's article, some background on mergers is in order.[88] As a general matter, the consummation of a merger between two corporations requires a favorable vote of the shareholders of each constituent corporation participating in the merger.[89] A favorable vote of the shareholders of the corporation merging out of existence is generally assured if the consideration offered in the deal is appealing to those shareholders.[90] A favorable vote of the surviving corporation's shareholders, however, is much less of a certainty. Those shareholders may simply dislike the deal and vote no. Perhaps, for example, they believe the surviving corporation is overpaying for the other corporation. It is also typical for at least some surviving corporation shareholders to fail to vote at all simply due to apathy.

The possibility of an unfavorable vote at the surviving corporation level creates deal risk. This risk can largely (but not completely[91]) be avoided by effecting a triangular merger where the acquirer itself is not a constituent to the merger, but rather one of its subsidiaries is. Take the situation where two corporations (X Corp and Y Corp) decide to merge, with X Corp being the surviving corporation. X Corp can avoid the need for a vote of X Corp shareholders by forming ("dropping down") a new, wholly-owned subsidiary and having it, rather than X Corp itself, consummate the merger with Y Corp. The new subsidiary is capitalized with either cash or shares of X Corp stock (depending on the deal), which Y Corp shareholders will receive as merger consideration.

By "dropping down" a subsidiary and having it, rather than X Corp, participate as a constituent to the merger, X Corp shareholders are not entitled to vote on the merger under applicable state corporate

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[88] The description of mergers that follows was largely taken from HAAS, *supra* note 10, at 498–99.

[89] *See, e.g.*, DEL. CODE ANN. tit. 8, § 251(c) (2022); MODEL BUS. CORP. ACT §§ 11.04(b) & (e) (1969) (AM. BAR ASS'N, amended 2016).

[90] For purposes of this discussion, I will assume the deal consideration consists solely of shares of common stock of the acquirer. Taxation of deals using all cash are much more straight forward, as nonrecognition principles do not come into play.

[91] If the number of shares of acquirer stock being issued in connection with a triangular merger is significantly dilutive to the acquirer's existing shareholders, and assuming the acquirer's shares are listed for trading purposes on either the New York Stock Exchange or Nasdaq, then acquirer shareholder approval of the deal is needed under stock exchange listing rules regardless of whether a vote under state corporate law is required. *See* NYSE Listed Company Manual § 312.03(c)(1); *see also* Nasdaq Listing Rule 5635(a).

law.[92] Rather, shareholders of the new merger subsidiary are entitled to vote, because that subsidiary is now a party to the merger. However, because X Corp owns all the shares of the subsidiary, the favorable vote of the subsidiary's shareholder (*i.e.,* X Corp) is a *fait accompli*. Indeed, that vote is controlled by the board of directors of X Corp, and that board wants the deal to happen.

Because of the existence of three companies—X Corp, its merger subsidiary and Y Corp—the merger is called a triangular merger. There are two types of triangular mergers: forward and reverse. If Y Corp merges with and into the subsidiary (and thus the subsidiary survives), the merger is referred to as a forward triangular merger. If the subsidiary merges with and into Y Corp (and thus Y Corp survives), the merger is referred to as a reverse triangular merger. As explained below, in both cases Y Corp ends up as a wholly-owned subsidiary of X Corp at the end of the day.

In a forward triangular merger, it is easy to visualize Y Corp becoming a wholly-owned subsidiary of X Corp. Pursuant to the merger, all of the assets and liabilities of Y Corp are subsumed within the merger subsidiary by operation of law. The merger subsidiary—which is already wholly-owned by X Corp—then changes its name to "Y Corp." Thus, through the merger "Y Corp" is transformed into a wholly-owned subsidiary of X Corp.

In a reverse triangular merger (where the merger subsidiary merges with and into Y Corp and thus does not survive), Y Corp also becomes a wholly-owned subsidiary of X Corp, although it is not so easy to visualize. A reverse triangular merger is typically the second step in a two-step acquisition, with the first step being a tender offer.[93] Once the tender offer is completed, the terms of the second step merger will provide that shares of Y Corp common stock owned by Y Corp itself (*i.e.,* treasury shares), as well as those held by X Corp and its merger subsidiary (such shares having been purchased through the first step tender offer), are canceled and retired for no additional consideration. Shares of Y Corp common stock in the hands of third parties who tendered their shares into the first step tender offer

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[92] *But see supra* note 91 (explaining that a vote of the acquirer's existing shareholders may be required under applicable stock exchange listing standards).

[93] *See* HAAS, *supra* note 10, at 499. In general, a tender offer is a public announcement by an offeror to buy securities (most typically common stock) of a publicly traded company from the holders of those securities at either a set cash price and/or in exchange for a set value of the offeror's securities. Tender offers are regulated by the Securities Exchange Act of 1934, as amended.

received the tender offer price. Those who did not tender have their Y Corp shares converted through the merger into the right to receive the merger consideration (subject to appraisal rights, if available). Also pursuant to the merger, all of the issued and outstanding shares of the merger subsidiary's common stock (all of which are owned by X Corp) are converted into a single share of common stock of Y Corp, the surviving corporation in the merger. Thus, after the merger, the only outstanding share of common stock of Y Corp with voting and dividend rights will be the single share of Y Corp stock held by X Corp. As a result, X Corp alone will own Y Corp post-merger as a wholly-owned subsidiary.

Both the forward and reverse triangular merger result in Y Corp becoming a direct, wholly-owned subsidiary of X Corp at the end of the day. However, that exact same result could be achieved through another form of acquisition, to wit the "stock-for-stock" acquisition. In a stock-for-stock acquisition, X Corp seeks to purchase all the outstanding shares of stock in Y Corp directly from the Y Corp shareholders. Assuming X Corp is successful in doing so, the end result is that Y Corp becomes a direct, wholly-owned subsidiary of X Corp.

Substance versus form in the context of the taxation of corporate reorganizations is the primary focus of Professor Oesterle's article. He highlights that Subchapter C of the Internal Revenue Code "focuses heavily on the form of corporate transactions rather than on their substance."[94] Because of this, the door is open for businesses to "lodge novel substance within existing forms."[95] Congress, of course, cannot predict every new form that acquisition planners and state legislatures can conjure up. Even if it could do so, it lacks the required nimbleness to stay ahead.

Whether a particular corporate reorganization generates taxable income or not is a threshold question. Assuming that it does, should that income be taxed immediately or granted nonrecognition status? Under a nonrecognition regime, the buyer corporation is not taxed on any gain generated when it exchanges its appreciated stock for either shares of stock or assets of a target corporation. Moreover, the target corporation itself is not taxed on any gains arising from its receipt of buyer stock. The target's shareholders, in turn, are not taxed

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[94] *See* Hoffer & Oesterle, *supra* note 4, at 1085.

[95] *Id.*

on any gain arising from their receipt of buyer stock in exchange for their target stock.[96]

Section 368 of the Internal Revenue Code lies at the heart of the debate over the taxation of triangular mergers. That Section provides for "three classic forms of tax-preferred reorganizations[,]"[97] affectionately referred to as A, B, and C reorgs, based on the particular subsection of Section 368 to which a given reorg relates. A traditional A reorg is a stock-for-stock merger whereby the target company merges with and into the acquiring corporation.[98] Former target shareholders receive stock in the acquiring corporation as merger consideration. A traditional B reorg is a stock-for-stock acquisition whereby the acquiring corporation uses its stock to acquire the target stock held by the target's shareholders.[99] Lastly, a traditional C reorg is a stock-for-assets acquisition whereby the acquiring corporation uses its stock to acquire substantially all of the target's assets.[100] Typically, the target will then liquidate and distribute the acquiring corporation's stock to target shareholders in the form of a special liquidating dividend.

Each of the three classic forms of tax-preferred reorg is subject to two substantive requirements. First, the acquirer either must continue at least one significant line of the target's previous business or use a significant portion of the target's assets in its business. This is referred to as the "continuity of business enterprise" (COBE) requirement. Second, at least forty percent of the transaction consideration received by target shareholders must be shares of the acquirer's stock. This is known as the "continuity of proprietary interest" (COI) requirement.[101]

The classic forms of tax-preferred reorganization initially did not allow for a triangular structure—*i.e.*, the use of a dropped down subsidiary of the acquirer. However, over the years Congress ultimately relented and allowed the use of an acquisition subsidiary in the context of the classic forms so long as the other requirements of the IRC were met.[102] This provided the market with "more latitude in

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[96] *See id.* at 1086–87.

[97] *Id.* at 1088.

[98] *See* I.R.C. § 368(a)(1)(A).

[99] *See* I.R.C. § 368(a)(1)(B).

[100] *See* I.R.C. § 368(a)(1)(C).

[101] *See* Hoffer & Oesterle, *supra* note 4, at 1089.

[102] *See id.* at 1089–90.

choosing tax-favored reorganizations."[103] However, triangular mergers themselves were still excluded from the nonrecognition party.

Beginning in the late 1960s, Congress finally addressed forward and reverse triangular mergers. Congress set forth specific definitions for forward and reverse triangular mergers in Sections 368(a)(2)(D) and (E), respectively. Because both transactions involve statutory mergers, Congress required each of them to meet the requirements for A reorganizations in order to qualify for nonrecognition treatment. Thus, in addition to a given transaction qualifying as a forward or reverse triangular merger under the applicable statutory definition, it also had to meet the requirements for an A reorganization in order to receive nonrecognition treatment.[104]

While Congress ultimately did address forward and reverse triangular mergers, Professor Oesterle is critical of its approach:

> Congress's road to triangular mergers, while paved with good intentions, failed to provide consistency, reduce complexity, or focus on substance over form. . . . Congress's elevation of form over substance is bizarre, particularly since all acquisitive reorganizations share defining characteristics outside of their form, and since it has long been the IRS's policy to penalize taxpayers who elevate form over substance in other areas.[105]

Indeed, Congress took "a remedial approach ex post to address the evolution of corporate acquisition practice[.]"[106] Instead, according to Professor Oesterle, it should have taken "a normative approach ex ante"[107] which would have focused less on form and more on "aspects common to all deals that are relevant to realization and recognition."[108]

The overlapping and inconsistent nature of tax provisions relating to corporate reorganizations create unnecessary and artificial hurdles to those planning acquisitions. In this regard, Professor Oesterle has stated:

> The awkward evolution of the tax rules on triangular mergers—now the most popular deal structure—has

[103] *Id.* (footnote omitted).
[104] *See id.* at 1093.
[105] *Id.* at 1095 (footnotes omitted).
[106] *Id.* at 1108.
[107] *Id.*
[108] *Id.*

> [caused those planning acquisitions] to unduly discriminate between triangular mergers and direct mergers, and between forward and reverse triangular mergers. . . . [T]ax considerations should not affect the choice between straight and triangular forms or between forward and reverse forms of merger.
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> . . .
>
> By distilling the history of tax treatment of reorganizations to its essence, we find rules that have struggled to keep up with acquisition practice over the years. Tax law irrationally penalizes reverse triangular mergers by significantly limiting the forms of consideration that an acquirer can offer the target's shareholders; however, it does not similarly penalize the forward triangular merger. And the penalty for using any type of triangular merger rather than a straight merger—application of the substantially-all test—not only creates nonneutrality among merger forms but is also redundant in light of the IRS's interpretation of "merger," which prohibits nonrecognition for divisive transactions. In short, federal tax law has failed to keep up with the evolution of state corporate law on acquisitions.[109]

In an attempt to clean up this tax mess, Professor Oesterle proposed a pragmatic control test that is explicitly pro-deal in that all classification conflicts are resolved "in favor of tax-preferred treatment for the deal."[110] Specifically, he advocates that Congress "decouple tax treatment of shareholders from that of the target corporation and . . . move away from [the] continuity of interest and continuity of business enterprise tests towards a bare control test in triangular mergers."[111] Thus, preferred tax treatment for triangular mergers would be granted if, as a result of the transaction in question, the parent corporation has purchased legal control of the target corporation, regardless of whether that was accomplished through a forward or reverse triangular merger.[112] As to when legal control over the target has changed hands, Professor Oesterle adds:

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[109] *Id.* at 1096, 1098–99.

[110] *Id.* at 1099.

[111] *Id.* at 1101.

[112] *See id.* at 1106.

> In the reorganization context, one could argue that a legal control test, resting on the percentage of stock necessary under state law to elect a majority of the target's directors, should suffice. Or, in the alternative one could use a control test that rests on the percentage of stock necessary under state law to pass fundamental changes to the target's business structure, such as amendments to a company's charter, a merger, an asset sale, or dissolution. One could also argue that the target's nonvoting common stock ought to be added to the test, which would require a percentage of the target voting stock to be matched by a similar percentage of all equity (or equity minus nonvoting preferred stock) by total value. Including nonvoting stock in the measure of control would prevent the parties to a reorganization from covertly dividing the target through a creative use of nonvoting shares.[113]

Professor Oesterle concludes with a final recommendation for the future of taxation of corporation reorganizations: "In its next one hundred years, Congress should strive to pry the corporate income tax free from state laws on corporate personhood and governance, focusing not on form, but instead deciding on substance what income is, to whom it should be attributed, and when it should be taxed."[114] Can I hear an "Amen"?

II. CONCLUSION

Through this tribute, I have attempted to demonstrate that Professor Oesterle—throughout his illustrious career—has been unafraid to tackle difficult issues thoughtfully through his scholarship. Many of the issues he has addressed do not appear to naturally fall within his wheelhouse. While tackling foreign issues may scare off more timid scholars, Professor Oesterle admirably embraces the challenge head on. Additionally, through his scholarship he has expressed—sometimes through blunt but often humorful language—his deep skepticism of our governmental institutions. All in all, Professor Oesterle's approach to scholarship is, indeed, fearless. Of course, this is not surprising given that he is, after all, also a race car driver.

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[113] *Id.* at 1106–07 (footnotes omitted). *See also id.* at 1107–12 (where Professor Oesterle also proposes a normative response that more globally addresses the issue of nonrecognition in the context of corporate reorganizations.).

[114] *Id.* at 1113.