

2015

## Business and Financial Literacy

Dwight Drake

*University of Washington School of Law*, [djdrake@uw.edu](mailto:djdrake@uw.edu)

Follow this and additional works at: <https://digitalcommons.law.uw.edu/faculty-chapters>



Part of the [Legal Education Commons](#)

---

### Recommended Citation

Dwight Drake, *Business and Financial Literacy*, in *BUILDING ON BEST PRACTICES: TRANSFORMING LEGAL EDUCATION IN A CHANGING WORLD* 407 (Deborah Maranville, Lisa Radtke Bliss, Carolyn Wilkes Kass & Antoinette Sedillo López eds., 2015). Available at: <https://digitalcommons.law.uw.edu/faculty-chapters/10>

This Article is brought to you for free and open access by the Faculty Publications at UW Law Digital Commons. It has been accepted for inclusion in Chapters in Books by an authorized administrator of UW Law Digital Commons. For more information, please contact [cnyberg@uw.edu](mailto:cnyberg@uw.edu).

## J. BUSINESS AND FINANCIAL LITERACY

By Dwight Drake<sup>1</sup>

### 1. Introduction

Law practice continues to become more complex and demand a broader range of specialized knowledge. Business and financial literacy skills, once viewed as only important in business school or for law students who intend to become lawyers representing business owners or entities, are being viewed differently by legal educators who desire to ensure that law students are prepared for practice. The world is driven by business, and core business and financial issues routinely surface in various types of legal disputes, transactions, and planning challenges. At a minimum, knowledge of basic business and financial concepts will help a lawyer deal with personal consumer, credit, financial, investment, and business challenges and enhance the lawyer's ability to serve others, even when retained for a non-business matter. The importance of understanding core business and financial concepts is heightened for the lawyer who wants to serve business owners or executives at any level.

BEST PRACTICES FOR LEGAL EDUCATION did not address the need for business and financial literacy.<sup>2</sup> Given the growing recognition of this as a potential area for curricular development, it is a best practice for schools to identify whether students have opportunities in the curriculum to learn the knowledge, skills, and values of this subject. This section explores why such knowledge, skills, and values are important and aims to identify the core elements of business and financial literacy for educators exploring this topic.<sup>3</sup>

### 2. Why Financial and Business Literacy?

Many law students graduate today with little to no understanding or appreciation for what they do not know about the world of business and how that deficiency in their education might hamper their professional development, their effectiveness in servicing others, and their ability to manage their own financial affairs. Such students may not have received business-related training before entering law school or received any in law school. Student understanding of basic business and financial concepts is a prerequisite to developing the capacity to meaningfully assist future clients in the processes of identifying and prioritizing specific business objectives. Many business owners and executives, even some of the brightest, find it challenging

---

<sup>1</sup> Readers for this section were Nathalie Martin, Alexander Meiklejohn, Alex Ritchie, Toni Robinson, and Robert White.

<sup>2</sup> ROY STUCKEY AND OTHERS, BEST PRACTICES FOR LEGAL EDUCATION: A VISION AND A ROAD MAP (2007) [hereinafter BEST PRACTICES]. In giving examples of how to articulate outcomes, BEST PRACTICES used examples taken from the Diploma in Legal Practice Program from the Glasgow Graduate School of Law in Scotland. Some of the relevant examples were Accountancy for Lawyers, Financial Services and Tax, and Practice Management.

<sup>3</sup> For a discussion of such elements, see DWIGHT DRAKE, BUSINESS AND FINANCIAL LITERACY FOR LAW STUDENTS (2014). See also ROBERT W. HAMILTON & RICHARD A. BOOTH, BUSINESS BASICS FOR LAW STUDENTS: ESSENTIAL CONCEPTS AND APPLICATIONS (4th ed. 2006).

to identify and articulate specific objectives without the aid of a knowledgeable advisor. They need help to understand the legal significance of an issue and identify facts and considerations that have consequences to their specific objectives relative to the issue. Because of conflicts and inconsistencies triggered by competing business objectives, clients may need assistance in identifying and ranking priorities. Lawyers can more effectively advise clients if they can collaboratively engage in a balancing analysis of business factors, strategic options, and trade-offs. Thus, a solid grounding in business and financial matters is needed.

Law schools can meet this need by offering students training in basic business and financial concepts that will advance their professional development. Such training helps students achieve a deeper understanding of the business world and an enhanced ability to interface with business owners, executives and those who serve the business community.

### 3. Which Students?

All students who study business organizations should be exposed to the business and financial literacy concepts identified as “core” in the following section. The emphasis should be on breadth and real-world relevance and promoting awareness and a basic understanding of foundational issues. Although the objectives, priorities, teaching styles, and time constraints of teachers who teach business organizations vary widely, this exposure can often be accomplished by restructuring a traditional business organizations course to incorporate supplementary materials and related student problems.<sup>4</sup> Of course, such a restructuring may not be possible or desirable in many situations. As an alternative or addition, a school may offer the equivalent of a two-credit, one-semester course that covers core concepts as well as the broader business and financial literacy topics described in the following section. Such a course would be suitable for any student, but would be particularly helpful to those students who anticipate a career in the private practice of law.

### 4. Scope of Subject Matter

The core elements of business and financial literacy include foundational topics that often fall outside the scope of a traditional course on business organizations or corporations. Incorporating such topics will expand a course’s relevance, broaden the business literacy of the students, and complement the entity and doctrinal concepts covered in the course. Teachers or institutions seeking to incorporate core concepts might choose to teach all or a portion of the following suggested topics, which identify important knowledge and skills for lawyers:

- **Basic Business Differences, Classifications, and Characteristics.** Business is never a “one-size-fits-all” game. Businesses differ based on the type, mix, and number of their owners, and each business has specific characteristics that define the nature and role of the business and reveal its

---

<sup>4</sup> For an example of such supplementary materials, see DWIGHT DRAKE, *BUSINESS FUNDAMENTALS: ESSENTIAL CONCEPTS ALL LAWYERS SHOULD KNOW* (2014), a short book that is designed as a supplement, covers the ten core topics described herein, and includes eighteen student problems.

uniqueness, strengths, weaknesses, market position, vulnerabilities, and a host of other important factors. These characteristics are key indicators of the business' growth potential, most significant risk factors, and long-term survival prospects. An understanding and appreciation of such differences and characteristics is the key to comprehending business developments and challenges. Lawyers should understand that it is a mistake for a legal advisor to assume that businesses are essentially the same and that all owners and executives share the same basic objectives and require the same essential structural plans.

- **Core Accounting Concepts and Financial Statements.** Lawyers should know core concepts that underlie financial statements, the components of each of the key financial statements, how to read financial statements, how the statements relate to one another, how key transactions impact financial statements, and the role and limits of the audit process and standard safeguards. Knowledge of sophisticated financial and accounting principles is not necessary. However, students should begin to develop a working knowledge of the basic concepts that drive all businesses. Accounting is the language of business, and financial statements, the scorecards of business, routinely surface in numerous types of legal disputes and challenges.
- **Basic Business Concepts and Performance Measures.** A lawyer should understand basic business concepts and performance measures: income, EBITDA (“Earnings Before Interest, Taxes, Depreciation and Amortization”), cash flow, opportunity costs, fixed and variable expense structures, economies of scale, depreciation, capitalization rates, return on equity, going concern value, etc. These concepts help explain and illustrate how well a business is performing. Without an understanding of these concepts, a student going into practice will struggle to comprehend business objectives and participate in intelligent, business-focused conversations.
- **Leverage and Debt Basics.** Lawyers should understand the basic concepts and vocabulary of common creditor-debtor transactions that are important to consumers and businesses: simple vs. compound interest, installment obligations, notes and amortization schedules, security interests, covenants, mortgages vs. deeds of trust, recourse vs. non-recourse obligations, the role of the FDIC and the Federal Reserve, LIBOR vs. prime rate vs. Wall Street Journal Rate vs. Federal Funds Rate, lines of credit, letters of credit, bonds, etc. Ongoing debt leverage is a challenge for most consumers and the norm for nearly all successful businesses. Creditor-debtor relationships are created regularly to fund enterprises, finance specific transactions, and generate yields on investable assets.
- **Time-Value-of-Money Concept.** Business executives often have to make decisions that require a comparison of dollar values at different points in time. These decisions require an application of basic concepts related to the time value of money. The key for most lawyers is to focus on the relevant concepts, the variables necessary to apply select concepts, and how to effectively use a calculator (handheld or online). Simple technology has

stripped away the mathematical challenges of decisions that incorporate time-value-of-money concepts.

- **Basic Business Valuation Techniques.** Lawyers should have an understanding of the vocabulary and basic techniques of business valuations. The issue of value is an essential factor in most important planning situations, and business valuation issues often arise in a broad range of litigation contexts, including marital dissolutions, bankruptcies, breach of contract battles, dissenting shareholder and minority owner oppression disputes, economic damage computations, and many other situations. At the most basic level, such an understanding makes intelligent conversation possible with business owners, executives, and managers. Knowledge of valuation factors and techniques also will make a lawyer a better negotiator.
- **Elementary Microeconomics Concepts.** For those who study antitrust law, an understanding of elementary neoclassical microeconomics concepts is a must. But the need to know extends to any lawyer who wants a basic understanding of how certain market forces work and how many business owners approach decisions to maximize profitability. Lawyers should have at least a rudimentary understanding of supply and demand concepts that are so often used to justify or explain a specific event, decision, or course of action.
- **Business Funding Challenges.** Law students should be introduced to the challenges of funding a business enterprise: going public realities and processes, how stock markets work and the related lingo and common trading strategies, start-up capital funding sources, and the importance of securities law registration exemptions and related dangerous misconceptions. Capital formation is a key prerequisite for success in nearly all businesses. A lawyer should have a basic understanding of the practical and legal challenges of capital formation and how markets function.
- **Business Entity Taxation.** The importance of business and corporate taxes throughout the world cannot be overstated. They directly affect the stability and strength of nations and communities, the scope and quality of governmental services, and the growth and development of economies that provide jobs and markets for goods and services. Lawyers should have a basic understanding of the role of business taxes throughout the world, the challenges of transfer pricing, and rudimentary concepts of C corporations, S corporations, partnership-taxed entities, and self-employment and payroll taxes. A study of business organizations is incomplete without an introduction to the general concepts of business entity taxation.
- **Choice-of-Entity Concepts.** Students should be introduced to the key business factors and collateral consequences that often impact the all-important choice-of-entity decision for a business. A threshold challenge for all businesses is to select the best form of business organization. The challenge is not limited to new ventures. A mature business sometimes needs to re-evaluate its business structure to maximize the benefits of the enterprise for its owners.

Beyond these core concepts, a course on business and financial literacy could be expanded to include three additional categories of important topics. The first category includes the numerous business factors that directly impact core legally-related challenges faced by businesses. Often a law student is introduced to a technical concept of business law without ever being exposed to the important business factors that must be considered in applying the concept. The student, for example, is taught how to form a corporation with no mention of the numerous business operational factors that co-owners of the new business should consider in the design of their organizational documents. Common legally-related business challenges are driven by key business factors. A grasp of these business factors and challenges defines business literacy and is the key to bridging the gap between legal concepts and business objectives. The best lawyers instinctively bridge that gap with their core business knowledge.

The second category includes foundational knowledge about business-related areas of the law that regularly impact businesses and their owners and executives. The goal is to promote awareness and an appreciation of why the business challenges associated with these areas of the law are so important. Key topics included in this category are the role and limits of antitrust, employee benefits (including healthcare reform), executive compensation, securities law risks (including insider trading), intellectual property protections, employment practices and rights of employees, and the role and evolution of multi-entity planning.

The third category includes business-related ethical challenges, including the importance of identifying and clarifying the client relationship, representing multiple parties, serving as an officer or director, investing with a client, and handling attorney-client privilege issues.

## **5. Best Approaches for Teaching Business and Financial Literacy Topics**

Naturally, the teaching practices articulated in *BEST PRACTICES* and throughout this book apply to teaching business and financial literacy topics. These topics should be presented in a straightforward, understandable manner designed for students who are not trained in business. The discussions should focus on core concepts and eliminate extraneous materials and nonessential complexities. The reading materials should be concise, explain the practical relevance of each topic, and include numerous examples.

Ideally, reading materials on business and financial topics should include problems that test student comprehension by challenging students to analyze and apply the substance of what they are reading to specific fact situations. Such student problems can be used to efficiently broaden the scope of the subject matter and help students deepen their understanding of the concepts they are learning. This area is also ripe for law teachers to incorporate teaching of teamwork, ethics and professionalism, writing, and presentation skills.

## 6. Conclusion

In the increasingly complex and expanding range of skills needed to practice law effectively, law schools must teach students the substantive knowledge and practical skills they need for contemporary practice environments. Regardless of whether a student intends to specialize in business or finance law, a basic understanding of business competency and financial literacy is essential to the modern practice of law. By offering courses that focus on the core concepts of business and finance and how those concepts influence a lawyer's decision making, law schools can further the primary goal set out in BEST PRACTICES: to develop more practice-ready attorneys.