Business Organizations II – Section 1

HYBRID

Spring 2025

Professor: M. Egenthal

General Instructions:

Answer Three (3) Essay Questions.
Total Time Allotted: Three (3) Hours
Recommended Allocation of Time: Equal Time per Question

Business Organizations (Corporations)

Spring 2025

Final Exam

Background facts that apply to all three exam questions:

Ink, Inc. ("Ink") is a California corporation with business activities throughout the US and is registered as a foreign corporation in many states. It is the largest supplier of ink to the printing industry as well as other industries. It is a public corporation registered on the NYSE. Its shares currently trade for $50 per share, and it has 10,000+ shareholders. It has a board of 10 directors, 9 independent, and one who is the original founder of the company and holds 5% of the shares. Its year end is December 31, so its annual shareholders' meeting is April 20 of the following year.

Question 1

25 of the shareholders would like Ink to adopt a policy on environmental, social and governance (ESG) issues, as Ink does not have such a policy now. The shareholders are particularly concerned about the lack of diversity in the management, as well as the recent tank explosion at the main plant in California that caused a large spill into the Salinas river. The shareholders come to you to ask for instructions on how to approach the directors to add this issue to the proxies for the next shareholders' meeting. They also want to see the corporation's records on its safety and prevention expenditures as support for their request. Please provide them with the procedure for accessing the records as well as the proxy request. They are a well-educated group so make sure to provide the legal support and authority.

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Question 2

Ink's directors feel the time is right to expand and would like to acquire Laser, Inc., ("Laser"), a California corporation that manufactures, sells and repairs laser printers. Laser has been the defendant in a number of lawsuits for safety issues (the machines seem to catch fire easily.) There are lingering and possible future liabilities in Laser's books. The same group of shareholders as above come to you wanting to know if they can stop the purchase. Please explain to them, including reference to the relevant law, the powers of shareholders in this area, as well as the responsibilities of the directors.

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Question 3

Tarquin, one of Ink's directors (an independent director) recently met a college friend who told him about his new business creating and producing vegetable dyes and ink for textiles and packaging. The company, named Clean, is still in the startup phase, but there will be a big demand in many industries. (Ink uses only semi-toxic chemicals for its products.) Tarquin comes to you to ask about whether he can invest in his friend's business. He has not spoken to any of the other directors of Ink, and he would really rather not share this opportunity with them. Please explain the California corporate laws that apply to his situation, including his responsibilities and liabilities.

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ANSWER 1 (OUTLINE)

20% Organization (Similar headings – boldfaced below)

20% Issue (Spot all issues)

20% Rules (Name all rules – underlined below)

20% Analysis (Apply law to facts – all non-underlined, non-italicized font below)

20% Conclusions (Provide correct conclusions – as *italicized* below)

Issues: Procedure for viewing records, procedure for adding to proxy, procedure if directors refuse

Do the shareholders have a right to view the corporation's documents?

Shareholders have limited rights with regard to the control of the corporation. In addition to voting for board members and any items during the annual meeting, they also have rights regarding the inspection of corporate records.

Under CA Corp Stat 1601(a), The accounting books, records, and minutes of proceedings of the shareholders and the board and committees … shall be open to inspection … upon the written demand on the corporation of any shareholder or holder of a voting trust certificate at any reasonable time during usual business hours, for a purpose reasonably related to the holder's interests as a shareholder.

In this case, so long as the shareholders make a written demand and follow the other requirements noted in section 1601(a), they may view the records for any purpose related to their interests.

Accordingly, the shareholders may make a written request to inspect the records with regard to the safety history and the ESG policy (or lack thereof).

What is the option if the directors refuse?

In accordance with California Corporate section 1604: In any action or proceeding under Section 1600 or Section 1601, if the court finds the failure of the corporation to comply with a proper

demand thereunder was without justification, the court may award an amount sufficient to reimburse the shareholder or holder of a voting trust certificate for the reasonable expenses incurred by such holder, including attorneys' fees, in connection with such action or proceeding.

1605: If any record subject to inspection pursuant to this chapter is not maintained in written form, a request for inspection is not complied with unless and until the corporation at its expense makes such record available in written form.

Should the directors of Ink refuse, the shareholders have the option of requesting the superior court to assist.

Accordingly, if the directors refuse, the superior court may order the directors' compliance with the request, and award expenses to the shareholders and production of the record in written form.

Do the shareholders have a right to request an additional issue is added to the proxy for the annual meeting?

SEC section 14(a)(8) of the Securities Exchange Act of 1934 provides a framework allowing a public company shareholder to request that a proposal be included in the company's proxy statement, to be voted upon at a company's shareholder meeting.

In order to have a proposal included in the proxy, the shareholders must be current shareholders of record.

Under the same rule, the directors may exclude a proposal that "deals with a matter relating to the company's ordinary business operations." The purpose of the exception is "to confine the resolution of ordinary business problems to management and the board of directors, since it is impracticable for shareholders to decide how to solve such problems at an annual shareholders meeting.

In this case, the shareholders will need to claim that their proposals are outside the ordinary business, and if refused, may take action through SEC filing.

The shareholders of Ink have a right under SEC rules to request these additions to the proxy, and the directors may not refuse unless they deem, using the business judgement rule, that the matters are of ordinary business, and thus not appropriate for the proxy and shareholders' vote.

ANSWER 2 (OUTLINE)

20% Organization (Similar headings – boldfaced below)

20% Issue (Spot all issues)

20% Rules (Name all rules – underlined below)

20% Analysis (Apply law to facts – all non-underlined, non-italicized font below)

20% Conclusions (Provide correct conclusions – as *italicized* below)

Issues: derivative action, business judgment rule for directors.

Under California corporate law, Directors have fiduciary duties to act in good faith and with care. Under section 309, directors must take actions only in the best interests of the corporation.

Business Judgment Rule (BJR), recognized under statute and case law in California, is a presumption that when directors make a decision, they act "on an informed basis, in good faith, and in the honest belief that the action taken was in the best interests of the company", and the director(s) may not have a financial interest in the outcome.

The burden of proof lies with the shareholders when bringing a derivative action, such that they must overcome the presumption that the directors acted using good business judgement in reaching their decision.

In this case, there are a number of safety and financial "red flags" regarding the target company. The shareholders may use these issues to prove that the directors acted recklessly and thus without judgement.

Depending on the timing, the shareholders may request an injunction to prevent the purchase, or damages if post-purchase. As this is a derivative action brought by the shareholders on behalf of the corporation, any actions or damages belong to the corporation.

Accordingly, if the shareholders can overcome the presumption of the business judgment rule, they may bring a derivative action against the directors to stop the purchase.

ANSWER 3 (OUTLINE)

20% Organization (Similar headings – boldfaced below)

20% Issue (Spot all issues)

20% Rules (Name all rules – underlined below)

20% Analysis (Apply law to facts – all non-underlined, non-italicized font below)

20% Conclusions (Provide correct conclusions – as *italicized* below)

Issues: corporate opportunity, disclosure, director voting

Will Tarquin usurp a corporate opportunity by purchasing an interest in Clean

- California law requires directors to act in the best interests of the corporation and adhere to their fiduciary duties of care and loyalty and avoid self-dealing.
- Corporations have a prior claim to opportunities that are sufficiently connected to the corporation's business, or the acquisition of the opportunity is accomplished through disloyalty and unfairness to the corporation.
- Usurping a corporate opportunity is not permitted without following specific procedures such as disclosure to the board and allowing the board to determine whether to adopt the opportunity. The board may vote, but only disinterested directors' votes will be counted.
- Under California section 310, directors must not engage in an opportunity personally if that opportunity may have a material interest to the corporation.
- In this case, Clean will produce vegetable ink which may be used in the same industries and Ink, and may even substitute and thus overtake Ink's market. Hence, Ink would have a material interest in acquiring the opportunity.
- Tarquin would usurp the opportunity by purchasing an interest in Clean without allowing the corporation the chance to investigate and possibly pursue it.
- In addition, the vegetable ink may have a negative impact on the market for the corporation in that they would be in direct competition.
- *Accordingly, Tarquin would violate his duties under Section 310 by not disclosing the opportunity and by not acting in the best interests of the corporation.*
- *While Tarquin may argue that he found the opportunity while in a personal situation, this argument would fail in light of the close relation to the products of the corporation.*
- *In order to avoid liability, Tarquin must fully disclose all relevant information to the board and the board must vote whether to adopt the opportunity, or to forfeit it to Tarquin. In the vote, Tarquin's vote would not be counted as he is an interested party and only disinterested directors' votes will be counted.*

What procedure must the board follow under California rules?

- Under California law, the board may vote to adopt the corporate opportunity, or forfeit it to the interested director.
- Under section 310, only those disinterested directors' votes will be counted, so long as the number of the disinterested directors constitutes a quorum as required by the bylaws.
- In this case, the board must determine whether the opportunity should be adopted by the corporation. In taking the vote, only the five disinterested directors' votes will be counted. As there are ten directors, six would constitute a quorum if the corporation's bylaws define the necessary quorum for such votes as a simple majority.
- *Accordingly the board must vote whether to adopt the opportunity, forfeit it, or possibly take action against the interested director for a violation of his fiduciary duties to the corporation.*

30/33

Focus on the call of the question — DO NOT BACKGROUND KNOWLEDGE dump.

1)

A Corporation

A corporation is a legal entity, distinguished from its owners (the shareholders). A corporation has several distinct characteristics. It has a corporate person hood which means that as a legal entity on its own, a corporation can hold property, issue securities (both equitable and debt securities), it can sue or be sued, it can potentially exist in perpetuity (unless otherwise defined by the articles), is generally governed by the state law or RMBCA, or for Publicly traded corporation, like here in our hypo, by the SEC. One of the most important characteristics of a corporation is that it has limited liability. meaning the Directors, officers, or shareholders, provided that they do not exceed their authority and thus to not "pierce the corporate veil" can enjoy limited personal liability. This is one of the most attractive aspects of forming a corporation. Furthermore, there are several tax benefits for certain corporations such as S-corps that avoid double taxation.

Formation of a Corporation

A corporation can be formed by filing the articles of incorporation with the appropriate governmental agency (The Secretary of State in CA) and by filing all the applicable fees. The articles itself is critical as it must state several mandatory provisions. It must contain the name of the corporation which must entail "Inc., or Limited, or Corporation" so that people who engage in transactions with the corporation are put on notice about the character of the business. Most importantly, this is to ensure that the world knows this is a limited Liability entity. The articles must state the incorporatort's names and addresses, the Agent for Service or notice, names of directors (if the corporation has it already - but is sometimes decided on at the first meeting), a statement of purpose, the number of authorized shares, and depending on the jurisdiction and the state, any relevant, material information.

Statement of Purpose & Ultra Vires

Under common law, a corporation was bound only to engage in actions that were within the scope of their business purpose ("ABC Inc. is in the business of buying and selling flowers"). Hence,m any action outside of what the stated purpose was could be void under the doctrine of Ultra Vires. However, with the dynamic and continuous expansion of the business word, statements of purpose are nowadays rather generalized ("ABC Inc. to engage in any lawful business"). Therefore, Ultra Vires claims are generally rare. There are however three instances that such a claim can be brought up (1) By the shareholders against the corporation; (2) By the corporation against its officers or agents; (3) of by the state against the corporation (could be in a *quo warranto* claim to ensure legal activity)

Continued Duties

The corporation must adhere to strict statutory formalities such as holding meetings, continuous reporting and filing with appropriate governmental bodies (annual reports) and ensuring that any and all fees associated with maintaining the corporate status (governmental fees) are paid on time. Any such failure to communicate with the governmental body (sec of state here in CA) could result first in a 60-day notice to cure, if the matter is not resolved, an issuance of administrative dissolution that will last for 120 days. Corporations ought to avoid any such incidents and thus ensure that their compliance is at a solid 100%.

Post-Filing of The Articles of Incorporation

Once all relevant documents have been filed with the appropriate governmental agency/body and all associated fees have been paid, the corporation attains a De Jure status. One can think of it as the birth of a new legal entity. The corporation then can operate generally by having their first Board of Directors meeting, creating and finalizing their corporate bylaws, and can enjoy all the amenities that a corporate status bestows.

The corporation can then receive an EIN number from the IRS with which they can then open a bank account, they may start issuing stocks depending on how many authorized stocks that they have put down on their articles.

There are instances where a corporation can receive a corporate status despite defects in formation such as De Facto Corporation (when there was a good faith belief that the corporation had been formed, the incorporates, directors engaged in all relevant corporate formalities *meetings, opening bank account, putting up business sigs with the name of the corporation "inc") while not knowing that due to some defect or error de jure status was never granted. This hypo does not get into this, hence we will focus on the matters at issue.

Publicly traded Corporation vs Closely Held Corporations

While open (public) corporations are easier to get into as an investor (because they are openly traded on the market) and thus freely alienable, closed corporations may, via declaration on the articles impose other restrictions to maintain control of their corporation such as First Right of Refusals, Prior Approvals, conditions that may trigger a sale, or outright prohibition against certain sales of stocks so long as the condition and prohibition are reasonable.

Here, we have an open corporation with 10K+ outstanding shares. This is a public corporation subject to federal and state oversight.

Annual & Special Meetings

Annual meetings must be conducted either 6 months after the end of the corporate fiscal year or 15 months after the last annual meeting. Generally, it is during these meetings that shareholders will be able to vote on electing directors, reviewing corporate performance,

and voting on other matters the articles have deemed appropriate for shareholders to vote on. It is important to note that shareholders in a public corporation do not manage or "run" the company. There are however instances, if outlined by the articles that a shareholder agreement may be created and adopted by resolution that if the board becomes ineffective due to death, conflict, or other conditions, the shareholders may enter the managerial arena (It is important to note that while shareholders are generally not personally liable for the debts and liabilities of the corporation if they act in a capacity of a director, they can expose themselves to personal liability for any wrongdoing or illegal conduct). The Board or shareholders who have 10%+ of corporate shares can also initiate Special Meetings.

It is important to note that 10% or more of controlled share does not mean that only one person can hold these shares, shareholders can create shareholder agreements to reach that threshold. This is a great way for minority shareholders to voice their concerns or even vote together on a matter. Sometimes, if the articles allow, shareholders can engage in cumulative voting (but this has to be conspicuous). Thus the word "majority shareholder(s)" focuses on "control"

Record Date (Shares & Voting Rights)

Before Notices can be sent out to the shareholders, the corporation must ensure who has the right to vote on the matter to be discussed. While not all shareholders have the right to vote, one can think of shares as a "bundle of sticks". This common law metaphor, driven from the Property law truly captures the essence of the different types of stocks. Generally Common stocks have the right to vote where preferred stocks do not. The distinction of the different types of stocks along with their rights must be clearly written on the articles as well as on the certificates issued to owners. This is true so long as we have at least one class of shareholder with full voting rights and at least one class of shareholders that can receive corporate property (in the event of a dissolution)

Hence, The corporation must review their records and see who will be eligible to vote at the upcoming annual meeting. This is where record date comes in. There is a 70 day rule which means that the names of the owners eligible to vote at the upcoming meeting must be finalized and verified no longer than 70 days before the actual meeting. This way, the records will reflect the most reasonably accurate information. This must also be shared with the owners at least 10 days before the meeting or at the meeting so that proper accuracy in the voting structure is ensured.

Notice Requirement

Once the record date is noted and provided, Notices for annual meetings must be sent out no no later than 60 days before the meeting (so you cannot sent the notice 100 days before the meeting) and no less than 10 days before the meeting. The meeting can be held at any place, but generally the main place of business for the corporation is strategically a better location as all the personnel, documents, and records are at that location but this is not mandatory when it comes to location.

The notice will entail the "proxy materials". These include, the time, date, and place of the annual meeting, the topics of discussion, any and all relevant information pertaining to the matters to be voted on so that shareholders can review them and thus either further look into the maters or use these provided facts to make an informed decision. Furthermore, if there are any conflicts of interest on the board regarding an occurrence or a transaction, these too must be clearly stated as part of the fiduciary duties owned to the shareholders. The proxy materials will also have a proxy card (used for owners to assign a proxy who can then vote in their place - Struct Full disclosure rules apply to solicitation of proxies - Perhaps the 25 shareholders wish to assign a proxy). And, relevant to our hypo, the proxy materials will have a request sheet for shareholders to propose items of discussion on the upcoming annual meeting. Generally, a shareholder who owns $2000 or 1% of the shares and had them for three years may propose a 500 word or less topic of discussion so long as the topic is not a personal grievance and is deemed appropriate (generally day to day

activities of the corporation are defined by the bylaws and while shareholders may move the corporation to change the bylaws, the purpose must be significant in nature), Furthermore, shareholder(s) who have had $15,000 of the outstanding shares for 2 years and or shareholders with $25,000 of outstanding/issued shares and have continuously held them for more than one year may make such proposals.

Our 25 Shareholders

Here, the facts are silent as to the percentage of the shares these shareholders hold. Provided that they meet the threshold, there are two issues at hand: (1) the envirenmental grievance - surrounding the large tank explosion and a large spil into the Salinas river; and (2) the social grievance (lack of diversity in management). These are two very valid proxy requests.

When there is a concern that impacts the environment, or social grievances due to lack of equality, these could seriously hurt the corporations reputation, but also financial status. Hence the corporation should seriously look into this proxy request. An spillage into the river could have devastating public ramifications for the corporation and the shareholders, as the owners with present and existing future interest in the corporation have a right to voice their concern . Furthermore if it is shown that the corporation, via its board members who are in charge of the management of the corporation have delegated duties to their officers and or agents to engage in any discriminatory acts (or if the actions are from several rogue officers), this could have a huge negative impact on the PR of the corporation and thus the shareholder's investment. Shareholders are generally not liable for the debts and liabilities of the corporation (unless shareholder agreements exist as we discussed above) hence their "skin in the game" is the amount that they have invested. It is not only reasonable, but prudent and sound for shareholders to voice environmental and socially impact full matters of concern.

Hence, there is a valid reason for a proxy request. In fact, it would be surprising if the corporation had not or wished not to address the matter (at least via a report) to the shareholders in which they would note what steps they have done for the public regarding the spillage.

Counsel should advise the shareholders to include with their proxy request, any and all relevant documentation and information for the corporation to review. This would strengthen their request to be given the podium

Counsel should also advise the shareholders regarding the claim of lack of diversity that such as claim such be substantiated by evidence. personal grievances or allegations will likely not survive the standard for appropriate purpose. Hence, their request should be backed up with the necessary information to support their position.

Provided that the shareholders adhere to counsel's advise, the two reasons for their proxy request are valid and if supported by appropriate material, would be a valid topic at the annual meeting

Right to Inspect

Desire to see the corporation's records on its safety and prevention expenditures as support for their request. As noted above, if the shareholder have their own material in support of their position, that would be recommended to include. However, the shareholders now wish to see the records that are held by the corporation.

This too is a very valid reason. Shareholder's have a right to inspect documents relevant to their role and capacity as the corporation's sharehodler. Provided that these requests are not private in nature, a valif request must be made in writing, at least five days in advanced and state the purpose. Here, the purpose would be the explosion and spillage in the river as well as potential hiring procedures or safeguards.

It is noteworthy to mention that shareholders have certain unqualified rights (meaning these are automatic) provided that they adhere to the notice requirement (5 days and proper purpose). These include, the right to review articles and bylaws, names and addresses of directors and officers, meeting minutes, communication between the corporation and the shareholders. Directors on the other hand have a wider power o inspect. they dont have to giove a five day notice and can inspect almost everything as part of their duty of oversight.

In conclusion, the shareholders have a right to inspect the requested documents provided that they make a timely, written request and state a valid purpose (the purpose seems valid here). If they are not granted this request, they may seek and revieve equitable remedies from a court (a court order)

What if directors refuse? file in sup. ct for costs.

2)

Board of Directors = Director = D

Shareholder = SH

Board Management, Quorum and Meeting

SHs will be guided that there is a process that is required to be followed to acquire Laser. The decision of acquisition can be taken only at the board meeting. Majority of SHs will be given notice of such meeting with the information on time, date, venue and purpose of the meeting. If special meeting is called then 2 days advance notice will be given explaining purpose of such meeting. Decision on acquisition of the Laser can take place after the majority of the directors approves the acquisition by taking into consideration the benefits and liabilities of the deal. Quorum is required for the proposed action to go through and for voting. At least 1/3rd of the directors is required to be present to vote. SHs may express the concern via proxy in such meeting and reject the proposal with majority voting. SHs have right to vote in major decisions that may impact corporate existence, operation and SHs rights.

The acquisition will require majority of D's vote, Notice to SH and SH's approval in order the deal to go through. SHs may present below grounds to reject the acquisition.

Duty to request records

SHs has right to access business records like board meeting minutes and financial records

Here, SHs will be guided that they can request board meeting minutes to find out what was discussed in the board meeting and also get some information on decision and reasoning behind acquiring Laser. Such records will be very useful to understand if there is any violation and hard to the corporation due to such decision based on the reasoning

behind the acquisition decision. Additionally, SH may request financial documents of Ink corporation to understand if financial health of Ink is good to get into the acquisition deal by finding if Ink will struggle in existence after acquisition or be undercapitalized already. These can be grounds of rejecting the acquisition deal or at least grounds for bringing SH's derivative suit.

Duty of Care

Directors has fiduciary duties towards other SHs to make sure that they act in the interest of corporation and other SHs. BOD shall act in good faith and fair dealing in the best interest of corporation and SH interest. BOD shall act in good faith and fair dealing as a reasonable prudent person would in similar situation and comparable circumstances and in a manner D believes is reasonable in the interest of the corporation.

Here, the decision of acquiring Laser must be deliberate in the best interest of corporation. D may argue that Ink is a corporation which is already largest supplier of ink to printing industry. D shall make sure that acquiring Laser is in the best interest and beneficial to corporation because they manufacture, sells and repairs laser printers whereas Ink is supplier to printing industry. This merger will give better footprint to Ink in the industry and will result in high revenue and profit to the corporation if the footprint of prints are higher than the Ink distributed by Ink, then Ink can likely remove competitors Ink from those printers and use their own Ink resulting in better revenue for the corporation. If D feel the time is right to expand and acquire Laser then D must also consider any pros and cons of the acquisition, consult lawyers and business consultant to make sure this acquisition is in best interest of corporation. D must also make sure use all relevant, adequate information available to them and exercise due diligence in coming up to the decision of acquisition. On other hand, SH may argue that the decision of acquisition is not in the best interest of corporation because Laser has been D in number of lawsuits for safety issues and their machines seem to catch fire easily. Additionally, there are lingering and possible future liabilities in Laser's books. Such a risky deal with

Good!

tons of liabilities cannot be in best interest of corporation. SH may assert that D shall also consider the safety issues with the Laser and its printers as well as present and future liabilities that Laser may encounter. After having all these adequate information, analyzing it and discussing with lawyers, business consultants and deliberating it with the board if the decision is still weighing more towards acquisition, they may go ahead with the acquisition. D must not overlook the liabilities, compliance, risks, mismanagement and make a reckless decision by disregarding the truth. That may result in violation of duty of care.

Business Judgement Rule (BJR)

BJR is defense to Duty of care violation where there is presumption that D decision taken with available and adequate information is valid even if the decision later turns out to be unreasonable.

Here, court does not interfere with the business decision of the board whether to acquire or not to acquire Laser unless SHs show that decision was under fraud, reckless and in complete disregard to truth. D may argue that this acquisition is in best interest of corporation as Ink does not sell and repair laser printers and such printers may not have Ink's. On other hand, SH may argue that laser printers dont need or require ink for printer, they are called laser printers which are not ink based printers and hence such acquisition is not in favor of the Ink corporation and the decision is not a common sense decision but rather hints towards some fraud or omission of material information.

Duty to avoid corporate waste

D has duty to avoid corporate waste by involving in mergers and acquisition which are not in favor of corporation interest and wasting money and resources as well as assets of the corporation which may result in harm to corporation's existence, operations and SH's interest.

Here, D have to make sure that their business judgement is thought through with all relevant information and a reasonable judgement to acquire Laser. D shall take into consideration the impact on corporation finances and balance sheet due to this acquisition and share not jeopardize corporate existence, operations and SH's interest or result in bankruptcy and waste corporate money just to keep the other subsidiary alive and in business.

Duty to Disclose Material Information

D has duty to disclose material information to SH's and take their majority vote in order to move head with the acquisition if D reasonably believes that such acquisition will be material to SHs to make investment decisions.

Here, SH has right to know the material information and reasoning of the acquisition as this may impact the investment decisions of the SHs or decide whether to ask for appraisal rights or sell or buy the stocks once the information of acquisition is made public.

Duty of Loyalty

D have a fiduciary duty of loyalty towards corporation to act in best interest of corporation and must not be involved in self-dealing, Usurpation and insider trading.

Self-dealing - duty of loyalty is violated if D are involved in self-dealing and benefitted personally from the acquisition.

Here, SHs may look into an angle of self-dealing. Considering Ink is in the business of supplying ink to the printing industries whereas Laser is in the business of manufacturing, selling and repairs of laser printers. Both the business though in the same category but Laser's business model is not beneficial to Ink because laser printers dont use ink, they are laser printers hence the decision of acquiring Laser must be scrutinized further if any of

the BOD has personal interest or benefit in the acquisition. If it is found then the duty of loyalty is violated. SHs shall find out from the business records that they have right to, and understand if Ink is planning to expand its footprint toward laser based printers or also get into the business of manufacturing and repairs of printers. This will help SHs to determine if there was any violation of the duty. Good!

Fundamental Change (FC)

Fundamental corporate change is structural alteration in the corporation that affect the existence, operation and SH rights. This involves Mergers, acquisition, share exchange, disposition of substantially all assets, conversion and dissolution of corporation. The process involves majority of D's vote, Notice to Sh about the change and SH's majority voting approving the fundamental change.

Here, acquisition of Laser may result in different types of fundamental change to the corporation

1) Merger - where parent corporation acquires all the assets and liabilities of the other corporation and the acquired corporation dissolves and does not exit after merger.

Here, SH can find out if the acquisition is a merger. If it is then D are not required to take votes from majority SHs as the other entity will not exists after the merger. If this takes place then SHs will have to rely on Duty of care and Duty of loyalty violation in order to make D responsible for the liability to corporation.

2) Share Exchange - acquisition which results in Ink corporation acquiring majority of the shares of the Laser corporation such that Ink owns >90% of the subsidiary Laser corporation while still keeping both the corporation as operating separately. Not a! Short form merger.

Here, if SH finds this is the type of merger than they may ask for the SH's voting rights to approve such acquisition resulting in fundamental change to Ink corporation. In such Its a target co. at arm's length.

acquisition the majority votes of SHs of the corporation that is being acquired is required. Hence, SH may demand BOD to follow the fundamental change procedure or they may also rely on violation of fiduciary duties on the part of board to bring actions against them.

Appraisal Rights

If SHs oppose such FC then they may assert appraisal rights where they may demand the corporation to buy back the SH's shares at a fair value. This is the exclusive remedy for the dissenter of the FC unless there is showing of fraud or misrepresentation or procedural irregularity. Procedure involves Notice to SH, SH intent of demand for payment, dissenter notice to SH after vote in 10-60 days, SH demand for payment, Corporation payment, SH if they object the valuation of shares and court action by Corporation if no resolution.

Market out Exception

If the corporation is publicly traded and has 2000 SHs and 20m of market cap then there are no appraisal rights.

Here, Ink corporation is public corporation registered on the NYSE with 10k+ SHs but there is no information on what is the market cap. If its >20m then SHs have no appraisal rights but if its <20m then they will have appraisal rights to demand for share buy back.

SHs suits - Above violated then SH's can bring Derivative suit on behalf of corporation or direct suit for the injury caused to them personally.

Direct Suit

If SHs rights are violated in any of the above, and if SHs are personally injured then they may bring direct action against the Corporation and BOD.

Here, if the shares of INK is $50 per share and after acquisition if it drops to $5 per share due to fraud or misrepresentation resulting in personal harm to SHs, then they will have right to direct action against corporation. This can only be determined after the acquisition or any evidence of fraud. SHs will have to keep an eye on this to exercise their powers and rights in this area.

Piercing the corporate Veil

BODs are not liable for the harm to SHs but the corporate veil can be pierced if there is a finding of fraud, alter ego or undercapitalization.

Here, if SHs find that some BOD has personal interest and are simultaneously on the board of Ink and Laser then there might be finding of alter ego where board has ignored corporate formalities and made Laser as an alter ego of the boards. It is necessary to find the relationship between BOD and the Laser and see that none of the board of directors are serving on the board of Laser as well or has any ties or investment or personal benefit in the acquisition. If there is then SHs can pierce the Ink corporate veil and make board liable for the harm caused to them.

Derivative Suit

Here, SHs will be guided that they have power and right to bring lawsuit against the D if D breaches any of the Duty of care or duty of loyalty resulting in harm to corporation then SHs has right to bring derivative suit against the BOD on behalf of the corporation for injuries sustained to the corporation. For such lawsuit SHs must submit a demand to board unless the demand is futile. Futility doctrine excuses demand to board if the board is involved in wrongdoing or if board does not have disinterested directors. This can be found if the acquisition is approved and goes through.

SEC - Insider Trading

Insider who possess material non public information, trades based on such information and derives benefit.

SHs will be guided that they shall refrain from trading Ink's stocks due to such acquisition news unless the news gets public. Such information may be considered material. SHs are identified as insider possession material non public information, Tippee if they give this information to someone else and they personally benefit through it and if Tipper trades based on such information knowing that SH has breached their fiduciary duty, then SHs may be liable for such trading disgorging all profits and other penalties for violation. OK! good.

Creative way to bring this in.

32/33

3)

Responsibilities and Liabilities of Tarquin (T) As a Director (D)

Public corporation: Trade securities on national and public market. They are C-corp for taxation purposes. Corporation is a distinct legal entity apart from its owners, the shareholders. Shareholders (SHs) have limited liabilities. SHs have power to vote and fire or hire directors (for cause or no cause), and to vote on fundamental changes.

Here, Ink is a public corp and it's SHs have limited liability and will not be personally liable for the corp's obligations meaning they would only be liable up the amount of their investment. However, T could be personally liable for breach of his fiduciary duties.

Duty of Care:

Ds have the duty to act with care as a reasonable prudent person and in the best interest of corp. Ds also have the duty to supervise the officers and implement policies to avoid any harm to the corp.

Here, if T invest in Clean, he would not be acting as a reasonable prudent person because he is failing to care for Ink's interest rather than a competing business. He would also not be acting in the best interest of Ink because he is putting his money and effort in a company that could be possibly competing with Ink in a close future. Therefore, T would be breaching his DOC.

Defenses to DOC: Ds could defend their action by claiming that the SHs voted on the matter or business judgement rule (BJR) which infers that Ds are not liable for unreasonable decisions that they made in good faith as long as it was for the best interest of the corp.

Here, T can't use BJR because his action is not for furthering Ink's interest and in fact it would be hurting Ink's interest because there will be a big demand for Clean's products in many industries. T is not acting with good faith either because he is only thinking about his interest and not Ink's, therefore, BJR does not apply and T would be liable for breach of DOC.

Separate Duty

Duty of loyalty:

Ds have the duty to put corp's interest above their own and not compete with the corp or usurping corp opportunities or self-deal. Ratification by board of Ds or SHs is a defense. Usurping corp opportunity means that the D is taking advantage of a business opportunity that should have been offered to the corp first. Remedy for usurping business opportunity is disgorgement of profits and conveying the business opportunity to the corp. Self dealing means D is dealing with the corp as 3rd party and can benefit or lose as result of the deal. Conflict of interest arise when there is a conflict between D's (or his close family member) interest and corp's interest and the D is forced to put his interest above the corp's interest.

Line of business rule is used to assess whether DOL was breached meaning the business opportunity was in the same line/field as the corp and the corp had the finances to take advantage of the opportunity. Some jurisdiction have a fairness test to assess whether the usurping of the opportunity was fair to the corp.

Here, Clean is producing vegetable dyes and ink or textiles and packaging. Considering the fact that Ink is the largest supplier of ink to the printing industry and other industries, Clean and Ink could be competing in close future. Since there will be a big demand in many industries for Clean's products, Ink might detrimentally suffer as result of this competition. If T decides to invest in Clean, he will be breaching his DOL because he is

usurping corp opportunities. He should offer the opportunity to Ink first because taking it because Ink and Clean are in the same industry of making Ink and Clean's product could further Ink's business and make them a lot more profit. Ink is a big corp and is most likely financial able to take this opportunity and will not pass on to T. If T decides to invest in Clean, he must give his notice to resign to the board otherwise he will be breaching his DOL because he has put his own interest/ Clean's interest above Ink's interest and might be competing with Ink at some point in future. The decision to stay or be personally liable for breach of DOL is up to T. If stay, T would be potentially liable profit gained from Clean and must convey this business opportunity to Ink and he might still get fire from Ink.

or just act as "interested" director, barred from a vote of the board approving the transaction. Then, quorum reqs: consider the director has the CONFLICT of Interest?

Defense:The SHs or Ds could also ratify Ds' action that could have hold him liable for breach of DOL only after all material information was disclosed to them.

Here, T could claim that he could ask for ratification however, because of the intensity of the upcoming competition, there is no way Ink's Ds or SHs will ratify T's investment or not want to take advantage of this opportunity. T may argue that his college friend only let him invest because they knew each other and would not want a big corp to know or become a part of Clean and would never sell Clean to Ink. However, the decision to buy is up to Ink and the decision to sell or cooperate is up to Clean's SHs and not T. T must disclosed all material facts to Ink anyway and this would not be an affirmative defense.

Duty of good faith and fair dealing

Ds must act in good faith with subjective honestly and deal fairly on behalf of the corp.

Here, if T decides to invest in Clean and not tell the Ink Ds, he is breaching the duty of good faith and fair dealing because he is on the directors' board and making business decisions while he is also making business decision at clean, which is a competing business. T would be failing to act with subjective honesty if he decides to hide his investment. Therefore, he will be breaching this duty as well.

Duty of Disclosure

Ds have the duty to disclose any material facts that any other Ds or SHs would find important when voting on a relevant matter.

Here, if T decides to invest in Clean and not tell the Ink Ds, he is breaching the duty of disclosure because he is on the directors' board and this is a material fact since their inside (non-public) information could be used at clean and in consequence harm Ink. Therefore, T could be liable for breach of duty of disclosure as well.

Security exchange codes: SEC 10(b)5: is an anti-fraud law that also include inside trading meaning it is unlawful for anyone, directly or indirectly, breach the duty of confidence and trust owed to the issuer corp, issuer SHs, by trading non-public information that is material to a prospective investor.

Here, if T decides to leave Ink and join Clean, Ink could hold him liable for self trading or inside trading if he starts using or sharing non-public information that he has learned while working for Ink. Ink had a duty of confidence and trust in T as a director and allowed him to learn inside information that would be illegal for T to share with others.

Voting procedure

To set up a meeting for Ds, that is not their annual meeting, a notice with the date and time must be sent to them at least 2 days in advance and quorum required. Quorum means the majority of the Ds must be present at the meeting to vote, except if the bylaws require lower or higher quorum but it can't be less than 1/3.

Here, if the Ds find T liable for breach of fiduciary duties, they can set up a meeting to decide whether they want to fire him or keep him as a Ds. Of course T would not be able to vote since he is an interest D. Therefore there will be 9 Ds in the meeting which means quorum is met and majority of them must vote in favor of firing T, in order for T to get fired.

Direct suit by Ink against T: Corp is a distinct legal entity from SHs and can sue and be sued. A suit could be brought by the corp against the a D for breach of his fiduciary duties.

Here, Ink could being a suit against T for breach of his fiduciary duties as a director and can recover any profit gained by T as result of this breach and must convey the business opportunity to Ink.

In conclusion, if T decides to stay at Ink and not invest at Clean, he would not be breaching any fiduciary duties. However, if T decides to invest in clean and not disclose this information to Ink's Ds or SHs, he would be liable for breach of DOC, DOL, duty of good faith and fair dealing, and duty of disclosure. Ink would most likely fire him (Ds voting on it) and must disgorge all profits as result of this breach and must convey the business opportunity to Ink.