**Corporations**

1. **Corporate Formation**
   1. **Pre-Incorporation Contracts**
      1. **Promoters**: person acting on behalf of a corporation not yet formed.
         1. **Corporate Liability**: the corporation becomes liable on a promoter’s pre-incorporation contract when the corporation adopts the contract by (1) express board resolution or (2) implied adoption through knowledge of the contract and acceptance of its benefits.
         2. **Promoter Liability**: retains liability until novation—an agreement between promoter, corporation and third-party replacing promoter.
         3. **Fiduciary Duty**: promoters are fiduciaries of each other and of corporation, and cannot make secret profit in dealing with them. If promoter acquires property *before* becoming promoter, she can sell to corporation and profit so long as price if FMV. If promoter acquires property *after* becoming promoter, cannot profit at all from resale to corporation, even if FMV.
      2. **Subscribers**: persons or entities who make written offers to buy stock from a corporation not yet formed. A *pre-incorporation* offer to buy stock is *irrevocable* for 6 months.
   2. **De Jure Corporate Status**
      1. **Incorporator**: person merely signs and files articles of incorporation.
      2. **Articles of Incorporation**: must contain all 5:
         1. **Authorized Shares**: *maximum* number of shares the corporation is authorized to issue.
         2. **Purpose**: a general purpose and perpetual duration are valid and presumed in the absence of a specific purpose or limited duration. A specific purpose or limited duration is valid, but anything beyond would be *ultra vires*, in which case (1) state can enjoin the ultra vires act and (2) corporation may sue its own directors and officers for losses cause by act. If not enjoined, act can be valid, but damages still available for losses.
         3. **Agent**: name and address of registered office.
         4. **Incorporators**: names and addresses.
         5. **Name**: must contain indicia of corporate status.
      3. By-Laws: Articles *need not* contain by-laws.
   3. **De Facto Corporation**: if you fail to achieve de jure status but made good faith, colorable attempt to comply with formalities and had no knowledge of lack of corporate status, treated as a corporation.
   4. **Legal Significance of Corporate Form**: generally, corporation is a separate legal person. Generally, shareholders are not personally liable for debts of corporation.
   5. **Piercing the Corporate Veil**: courts will pierce to avoid fraud and unfairness, and to render a shareholder liable for corporate liability, if either (1) alter ego or (2) undercapitalization. Courts likely to pierce for tort victims against controllers.
      1. **Alter Ego**: controlling owner fails to observe sufficient corporate formalities.
      2. **Undercapitalization**: fails to maintain sufficient funds to cover foreseeable liabilities at time of formation.
   6. **Foreign Corporations**: to engage in regular intrastate business, must file Cert. of Authority with Sec. of State which includes same information required in Articles.
2. **Issuance of Stock by Corporation**
   1. **Consideration**: what must corporation receive for issuing own stock?
      1. **Par Value Stock**: at least *par value*—minimum issuance price. Can be cash, or other consideration if Board values to be at least par value. If shares issued for less than par, corporation can recover from directors, who are liable for authorizing below-par issuance. \**Can also recover from buyer.*
      2. **No Par Stock**: valid, and for this stock need only get consideration deemed *adequate* by Board.
      3. **Treasury Stock**: stock previously issued but reacquired by corporation. Upon resale, deemed *no par* stock, even if called “par”.
   2. **Shareholder’s Preemptive Right**: right of an existing shareholder to maintain her percentage of ownership by buying up to that percentage whenever corporation issues new shares for cash. \*No right unless expressly granted in Articles.
3. **\*Directors & Officers**
   1. **Directors: Statutory Requirements**
      1. Must have board with at least 1 member.
      2. Shareholders elect directors, and can remove with or without cause.
      3. Valid Board Meeting: unless all directors consent in writing, a meeting is required.
         1. Notice must be given, but can be in bylaws.
         2. Proxies are not allowed, nor voting agreements.
         3. Quorum for Meeting: majority of *all* directors must be present.
         4. Voting: to pass resolution, need only majority of those present.
         5. Each director presumed to concur in board action unless dissent/abstention is recorded *in writing* (e.g., minutes).
   2. **Officers**: as agents, they may bind corporation by their authorized activities. Directors have virtually unlimited power to select and remove officers.
   3. **\*Liability of Directors & Officers to Corporation & Shareholders**
      1. **Duty to Manage**: may delegate to committee of one or more directors that recommend actions.
      2. **Duty to Disclose**: material corporate information to other directors.
      3. **Duty of Care**: must act with care a prudent person would use in managing his own business in like circumstances, unless Articles have limited liability for lack of care, which is valid.
         1. **BJR**: presumption that directors manage the corporation in good faith and in best interests of corporation and shareholders. Under BJR, directors not liable for innocent mistakes of business judgment, even if colossal.
      4. **Duty of Loyalty**: may not receive an *unfair benefit* to the detriment of the corporation or its shareholders. Conflicted/Interested transactions breach the duty of loyalty unless (1) there has been *disclosure* of all material terms and *independent ratification*, or (2) the transaction was fair to the corporation.
         1. **Self-Dealing**: receipt of unfair benefit in transaction with corporation. Remedies: transaction can be enjoined or set aside, and damages may be sought equal to profit.
         2. **Usurping Corporate Opportunity**: director may not divert a corporate business opportunity to himself without first giving corporation an opportunity to act. Corporation must have interest or expectancy in opportunity, but lack of financial ability is not a defense. Remedy: recovery of profits or compel transfer of opportunity to corporation under constructive trust theory.
         3. **Independent Ratification**: if approved by (1) majority of independent directors; (2) majority of committee of at least 2 independent directors; or (3) majority of shares held by independent shareholders.
      5. **Indemnification**: corporation’s duty to indemnify
         1. Never: for directors/officers who *lose* lawsuit with *corporation*.
         2. Always: for directors/officers who win lawsuit against *anyone* .
         3. May: for director/officer loss to other or settlement with corporation: if director/officer shows she acted in good faith and in corporations best interest, permissive indemnity may be granted by decision of: (1) majority vote of independent directors; (2) majority vote of committee of at least 2 independent directors; (3) majority vote of shares held by independent shareholders; or (4) special lawyer’s opinion recommending.
4. **Rights of Shareholders**
   1. **Shareholder Derivative Suits**: shareholder is suing to enforce the *corporation’s* cause of action. Ask: could corporation have brought suit itself. Requires: contemporaneous stock ownership, adequacy, and demand.
      1. Contemporaneous stock ownership: at time claim arose and, in most jurisdictions, throughout litigation.
      2. Adequacy: shareholder must fairly and adequately represent the corporation’s interest.
      3. Demand: must be made and rejected by the board or at least 90 days must have passed since demand was made.
   2. **Voting**
      1. **Who Has Right**: only “record date” owner votes—voter eligibility cutoff date set by board on any day within 70-day period before meeting. Right to vote even if no longer own the shares!
      2. **Proxy Voting**: must be (1) writing (fax/email valid); (2) signed by record shareholder; (3) sent to secretary of corporation; (4) authorizing another to vote shares. Valid for 11 months only.
         1. **Revocation**: proxies are revocable unless (1) labeled irrevocable *and* (2) coupled with an interest (e.g., sale of shares to proxy after record date).
      3. **Where to Vote?**
         1. **Annual Meeting**: every corporation must have annual meeting at which at least 1 director slot is open for election. Notice must include time & place.
         2. **Special Meeting**: meeting to vote on proposals or fundamental corporate changes. Notice must include meeting’s special purpose, and nothing else can take place at meeting.
      4. **Quorum for Meeting**: a majority of all *shares* (not shareholders) must be represented in person or proxy when meeting starts.
      5. **Vote**: if quorum present, action approved if votes cast in favor exceed votes cast against.
      6. **Pooled or Block Voting**: agreements to vote alike
         1. Voting Trusts: formal *written* delegation of voting power to a voting trustee for *up to 10 years*.
         2. Shareholder Voting Agreements: *written* agreement to vote shares as required by the agreement which is binding on all signers.
      7. **Cumulative Voting for Directors**: may multiply number of shares by number of open slots and use in one election in which top vote-getters will win. Right does not exist unless expressly granted in Articles.
   3. **Examine Books & Records**: upon 5 days’ written notice + proper purpose
   4. **Dividends**: declared in *board’s discretion* unless corporation is or would be rendered insolvent by dividend. Board members liable for unlawful distributions, but have defense of good faith reliance on financial officer’s representations regarding solvency. **Priority of Distribution**:
      1. Preferred With Dividend Preference: paid specified dividend preference, remainder given totally to common. Do not share in common dividend.
      2. Preferred With Dividend Preference & Participation: paid specified dividend preference and then participate as common for next round.
      3. Preferred With Dividend Preference & Cumulative: paid specified dividend for this year and each unpaid prior year, remainder given totally to common. Do not share in common dividend.
      4. Common: paid last and equally.
   5. **Shareholder Agreements to Eliminate Corporate Formalities** (Closely-Held Corporation). Requires: (1) unanimous shareholder election evidenced in the articles, bylaws, or a filed agreement, and (2) some share transfer restriction. Consequences: (1) no piercing even for failure to observe corporate formalities and (2) possible Subchapter-S corporation status (which allows option of partnership, rather than corporate, tax treatment). To be S-Corp, can have no more than 100 owners of stock and one class of stock.
   6. **Professional Corporations**: a corporation of licensed processionals.
      1. **Requirements**: (1) organizers file Articles with name designated “Professional Corporation” or “PC”; (2) shareholders must be licensed professionals; and (3) corporation may practice only *one* designated profession.
      2. **Consequences**: professional are liable personally for their own malpractice, but not liable for debts of other professionals or the corporation.
   7. **Shareholder Liabilities**: generally, shareholders not liable for corporate obligations, absent veil-piercing. However, a controlling shareholder cannot unfairly prejudice minority. While it can generally accept premium unavailable to minority, it cannot (1) sell to looter, and must conduct reasonable investigation, (2) sell corporate assets, or (3) sell board positions.
5. **Fundamental Corporate Changes**
   1. **Recognized Fundamental Changes**:Merger (A becomes B); Consolidation (A & B become C); Dissolution (A dissolves); Fundamental (not ministerial) Amendment of Articles; Sale (not purchase) of Substantially All Corporate Assets.
   2. **Procedural Steps**
      1. **Resolution** by Board at Valid Meeting
      2. **Notice** of Special Meeting
      3. **Approval** by Majority of All Shares Entitled to Vote, and by Majority of Each Voting Group Adversely Affected. Exception: no approval required for short-form merger (parent owning 90% or more of sub merges with sub).
      4. **Dissenter’s Appraisal Right**: a shareholder who does not vote in favor of a fundamental change has the right to force corporation to buy her shares at fair value if (1) before vote, filed written notice of objection and intent to demand payment, (2) does not vote in favor, and (3) makes prompt written demand. If no agreement as to FMV, court can appoint expert appraiser, and appraisal will be binding on parties.
      5. **File Notice With State**
6. **Federal Securities Laws**
   1. **Anti-Fraud: Section 10(b) of SEA**: requires (1) scienter—intent to deceive, (2) deception, and (3) in connection with *actual* purchase or sale of securities. For money damages, must also prove (4) reliance and (5) loss causation.
      1. Deception
         1. Misrepresentation/Omission (Despite Duty) of Material Fact
         2. Insider Trading
            1. Misappropriator: misappropriates and uses material non-public information to purchase or sell.
            2. Tipper: tips for *personal benefit* to another who trades.
            3. Tippee: receives inside information and trades with knowledge that disclosed in breach of tipper’s fiduciary duty.
      2. Reliance: investors actually relied or invested at price infected by fraud.
      3. Loss Causation: fraud caused actual economic losses.
   2. **Strict Liability for Short-Swing Trading Profits: Section 16(b)**
      1. **Application**: applies only officers, directors, or more than 10% shareholders of a reporting corporation (listed on a national exchange or with at least 500 shareholders and $10 million in assets.
      2. **Rule**: defendant may not profit from buying and selling corporation’s stock within any 6-month period. For D/O, purchase/sale before becoming D/O is excluded, but those after ceasing can be included. For shareholders, must have already been more than 10% owner both at time of initial and subsequent transaction. No fraud required. Corporation may recover profit.
   3. **Sarbanes**-Oxley Act: CEO’s and CFO’s of reporting companies must certify that based on their knowledge, reports filed with the SEC are true. Willful violation punishable by up to $5 million and 20 years.
      1. If false reports must be corrected and restated, corporation can recover from officer’s benefits made from trading shares of the company within 12-months after the false reports filed, and may recover incentive-based compensation received during that period.
      2. Corporations may also recover any benefits made by officers from trading corporation’s stock during “black out” periods or when employees are prohibited from trading in their retirement plan’s securities.