

4) Please type the answer to Question 4 below.**Â**

When finished with this question, click to advance to the next question.
(Essay)

The facts state that Retail, Inc was properly incorporated. Therefore, no issues relating to corporate formation seem to exist.

1. ON WHAT LEGAL THEORY CAN SUPPLIER (S) REASONABLY SEEK TO RECOVER AGAINST ART (A)

Here, S is owed \$10,000 for computer equipment. However, because Retail, Inc only has \$5,000 cash in assets, S has to seek alternative methods in order to recover his full \$5,000 amount in the case of Retail's bankruptcy. One method is detailed below.

Piercing the Corporate Veil

A corporation is afforded limited liability by virtue of it being a separate entity from its shareholders and owners. However, a creditor can 'pierce through the corporate veil' if the corporation does not follow sufficient formalities - such as failure to hold board meetings or shareholder meetings; and most importantly, if the owners of the corporation using company funds and property as their own. When the corporation owners and personnel start blurring such lines, that is when a creditor can reach through the corporate formalities to come after the owners of the corporation.

Here, the facts indicate that Retail is a close corporation consisting of just A and two family members in the Board of Directors (Board), and with just himself as President of the corporation. While such situations are common in close corporations, it is problematic that A bought 30% of XYZ Co. Inventory (a company also owned by A) without Shareholder approval. In addition, A started taking home some of Retail's Inventory without paying for it.

With A using Retail's property as his own, S can argue that this was a sufficient blurring of formalities that would allow S to go after A's personal assets in order to seek what he is owed from A. In addition, S can also claim that with Retail's distinct lack of formalities (inconsistent board meetings and no shareholder meetings) - this also contributes to the fact that A is running Retail as though he is the only one making the decisions and that A is treating Retail as an extension of his own.

Therefore, depending on the extent that A took home Retail's inventory, S could pierce the corporate veil to go after A's personal assets to recover the debt owed to him.

2. BARBARA (B)'S CAUSE OF ACTION AGAINST A

Derivative

Under Corporate Law, a derivative shareholder lawsuit is bought on behalf of the Corporation, and not the Shareholder him/herself. Such lawsuits are bought in situations where the Shareholder feels as though the company has been run in such a manner that is detrimental to the well-being of the corporation. However, monetary recovery in this situation does not go to the Shareholder personally, but to the Corporation at large.

Here, the facts state that B has 20% of Retail's stock, with the remaining 80% presumably belonging to A. This makes A the majority shareholder.

While there are several causes of action that B can bring against A and Retail, it is probably better for her to bring them against Retail and A personally in order to receive monetary damages.

Personal

Failure of Retail, Inc to hold Shareholder Meetings

A corporation is legally obligated to hold at least one Shareholder meeting an year to elect the Board of Directors, go over accounting of the business, and to go over other fundamental changes to the corporation. While such meetings can be waived by Shareholders, or Shareholders can skip personal attendance of the meetings by writing unanimous written consent forms, none of any of the formalities described above seem to have happened here.

Here, the facts state that the corporation was incorporated 'Years Ago' by A, and that B bought 20% of the stock subsequently. However, nothing in the facts state that any sort of shareholder meeting happened in the years since then. While it is the case that A is the majority shareholder and thus, he would have more voting power than B, it is still important to follow these corporate formalities in order to maintain a legitimate corporation.

Since this is a breach of fundamental corporation duties, B can bring a cause of action against A for the failure of Retail, Inc. to hold Shareholder Meetings.

Failure of Retail, Inc to seek Shareholder Permission while making Significant Corporate Decisions

As mentioned above, Corporations are required to seek Shareholder approval while making significant corporate decisions. There are at least two situations where A failed to hold a meeting. The first one being when Retail's board approved a contract to buy 30% of the inventory from XYZ, Co. Depending on how significant this was, it could be a breach on Retail and A's part for failing to hold a Shareholder meeting. However, if it was just buying inventory, than the court is unlikely to view this as a fundamental corporation decision. The second one is when Retail ceased business. In the process of dissolution, it is also important to hold a shareholder meeting to gain shareholder permission.

However, the facts do not state any of the sort occurred, therefore B can bring a cause of action against A for the failure of Retail, Inc. to seek Shareholder

Permission when making significant corporate decisions.

Breach of the Duty of Care by A

Another cause of action that B can bring against A is for him breaching the duty of care for failing to hold shareholder meetings or to seek shareholder permission when making significant corporation decisions.

In addition, A also breached his duty of care when Retail's board approved a contract to buy 30% of the inventory from XYZ, Co. - which is another company owned by A. When such situations occur, there is a presumption of self-dealing going on in the transaction, since by entering in such a contract, A is presumed to better himself over the company.

Therefore, B can bring a cause of action against A for breaching the duty of care owed to the corporation.

Failure of Retail, Inc to seek Shareholder Approval for Self-Dealing Transactions

In corporate law, self-dealing transactions can be allowed if it is presented to the shareholders and explained to them what it entails and how they plan to avoid any sort of self dealing. Again, even though A is the majority shareholder, it is still important for him to partake in such corporate formalities.

However, none of the sort happened in this case. Therefore, B can bring an action against A for failing to seek shareholder approval.

3.WILL A BE ABLE TO COLLECT FROM RETAIL ANY PORTION OF HIS LOAN?

Dissolution and Winding Up

When a corporation is in the process of dissolution, any assets left over will be used to fulfill any outstanding debts that the company owes to outside parties.

In this situation, Retail is left with \$5,000 in cash assets. However, because Retail still owes \$10,000 to S, all of that \$5,000 shall be used towards fulfilling that amount. Therefore, A will not be able to collect from Retail any portion of his \$50,000 loan.

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