MEE Question 2

Carlos, Diana, and Ethan own all the shares of Winery Inc., which is incorporated in State A. They are equal shareholders of the corporation and the only members of its board of directors. They share responsibilities in the corporation's vineyard and winery. They have no shareholders' agreement.

Recently, Carlos and Diana decided that it would be a good idea to change the corporation's business model. In addition to producing wines from the corporation's own small vineyard using sustainable, organic farming methods, they believe that the business should expand to buy grapes from local vineyards that produce grapes using such methods. They believe this new focus will allow them to attract new customers interested in organic wines. They also see this change and expansion to their business as a way to promote environmentally sustainable organic grape cultivation in their region.

To make this shift in the corporation's business, Carlos and Diana have decided that the corporation should become a "benefit corporation." A benefit corporation, authorized by many states, is a type of for-profit corporation that defines in its articles of incorporation a social or environmental purpose. Benefit-corporation law insulates directors from liability for making business decisions that serve this defined social or environmental purpose, even when their decisions may negatively impact shareholder profits.

State A has adopted the Model Business Corporation Act, which does not explicitly provide for benefit corporations. State A courts have held that domestic corporations must seek to maximize shareholder profits.

State B, which is adjacent to State A, also has adopted the Model Business Corporation Act but has modified its corporate statute to provide for the formation of benefit corporations. To form a benefit corporation, the articles of incorporation must indicate that the corporation has opted to be a benefit corporation and must state a social or environmental purpose for the corporation. The State B statute insulates directors from liability for claims that they did not seek to maximize shareholder profits if their decisions are consistent with the corporation's stated social or environmental purpose.

Carlos and Diana have decided that they can best carry out the new business plan by creating a benefit corporation in State B to operate in State A with the stated social and environmental purpose of "promoting sustainable and organic vineyard, winery, and production practices." They will incorporate the new benefit corporation as Organic Wines Corp. and be its only initial shareholders. Once this corporation is created, they will cause Winery Inc. to merge into it with all the Winery Inc. shares converted into shares of Organic Wines Corp.

Ethan is opposed to the plan, but Carlos and Diana support it.

1. Can Ethan block the merger of Winery Inc. into Organic Wines Corp. by voting against it? Explain.

2. If Winery Inc. merges into Organic Wines Corp., does Ethan have a right to demand that he receive payment in cash (instead of receiving shares in Organic Wines Corp.) equal to the fair value of his shares in Winery Inc.? Explain.

3. Assume that Ethan becomes a shareholder of Organic Wines Corp. Could Ethan successfully sue the Organic Wines Corp. directors in State A for promoting sustainable and organic practices at the expense of maximizing shareholder profits? Explain. Do not discuss whether that suit would have to be direct or derivative.

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1. Merger

A merger requires (1) the recommendation of an absolute majority of the board of directors and (2) the agreement of each corporation by an absolute majority of shareholders.

Here, Carlos and Diana, 2 directors out of 3 of Winery Inc. support the merger; thus, the first requirement above is satisfied. In addition, Carlos, Diana and Ethan have no shareholder's agreement, so the default rule (i.e. equal shareholders have equal votes) applies. As the votes by Carlos and Diana constitute an absolute majority of shareholders, the second requirement is also met.

In conclusion, Ethan cannot block the merger of Winery Inc. into Organic Wines Corp. by voting against it.

2. Dissenters' Rights

After a merger occurs, dissenting shareholders opposed to the action may receive payment determined at fair market value of their shares immediately before the merger took place.

Here, Ethan is opposed to the merger which qualifies him to receive payment equal to the fair value.

END OF EXAM