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1. Upon what theory or theories may the Pick Shareholders bring claims against Alex and Baker and what is likely the result?

Is PickWinners Inc. (Pick) a formal corporation?

Corporation

In order to have a valid corporation, there needs to be an entity that has filed the articles of incorporation with the state, it needs to have a board of directors, as well as shareholders who have shares in the corporation.

Here, Pick has a board of directors that consists of Alex, Baker and Cate. The board of directors were elected by the shareholders, and Pick has shareholders.

Thus, Pick is a formal corporation.

Action by Shareholders

Derivative suit

In order to bring a derivative suit in court, the shareholders first need to show 1. that they wrote a demand to the board asking for action to be taken to correct the injury sustained by the corporation due to the actions or inactions of the board and 2. that the board failed to respond or take action to correct the injury to the corporation.

1. Written Demand

In order to bring a derivative suit in court, the shareholders first need to show 1. that they wrote a demand to the board asking for action to be taken to correct the injury sustained by the corporation due to the actions or inactions of the board and 2. that the board failed to respond or take action to correct the injury.

Here, prior to the derivative suit, the shareholders wrote a demand letter asking for remedial action to be taken on behalf of the actions of Cate. The demand letter was denied by Alex and Baker. Given the denial letter, the shareholders are allowed to bring a derivative suit.

Thus, the shareholders are allowed to bring an action for a derivative suit.

2. Denial of Written Demand

Since the board did not respond to the written demand the shareholders can bring their derivative suit and argue that Pick sustained injuries due to the breach of fiduciary duty of care, and the duty to maintain a diverse portfolio by the board of directors (which will be discussed below).

Duty of Care

The board of directors have a duty of care to the corporation.

Duty of care is defined as a fiduciary duty of the board of directors to act in the best interest of the corporation and have a duty to not act against the corporation.

Here, the shareholders are going to argue that Alex and Baker, did not act in the best interests of the corporation because they denied Cate's proposal based on information they had from an analyst 2 months ago. Given Pick is in the business of trading stocks online, it is common knowledge that the stock market is constantly changing. Alex and Baker should have exercised their duty of care, and failed to do so by not further investigating this proposed business venture. On the other hand, Alex and Baker are going to argue that the revenue lost is not due to their inaction but due to the state of the market. As they told Cate, "Pick's decline just mirrors the overall recent decline of the stockmarket."

However, Alex and Baker not following up on Cate's proposed business venture cost Pick money. When Cate created E-Save company, her company began to thrive and Pick's market continued to decline.

Thus, there was a breach of fiduciary duty of care by Alex and Baker and there was an injury to Pick, by costing the corporation to lose revenue. Therefore it is likely the court will find that the shareholders are correct and Alex and Baker did breach their duty of care and injured Pick by doing so.

Duty to maintain a diverse portfolio

There is a duty to maintain a diverse portfolio, the corporation has to look for different opportunities to expand or grow and keep track of their shares, and interests. The board of directors has to constantly keep the portfolio up to date.

Here, Alex and Baker have failed to keep a diverse portfolio for the corporation. As stated, they focused exclusively on "Wealthy investors" and ignored average consumers, which lost them the low priced end of the trading market to other companies. The shareholders are going to emphasize that as part of the board Alex and Baker broke their fiduciary duty to maintain a diverse portfolio. They only focused on one aspect of revenue, which was the wealthy investors, without looking at other opportunities like the average consumers. The shareholders will argue that by Alex and Baker not diversifying Pick's portfolio, they cost Pick revenue and the price of their stock. Alex and Baker might argue they did not have a duty to diversify the business portfolio because their analyst told them that there was no money in it.

Thus, the court would find that there was a breach by Alex and Baker for not maintaining a diverse portfolio for Pick and it cost the corporation revenue.

Business Judgement Rule

The business judgement rule can be used as a defense by directors, there is a presumption is that directors act in the best interest of the corporation unless proven otherwise.

Here, Alex and Baker are both going to use the business judgement rule to try and defend themselves by stating that the shareholders have a duty to overcome the presumption that they acted in bad faith and not in the best interest of the corporation. However, as previously stated Alex and Baker, declined the demand to go against Cate for creating E-Save and they did not follow up on the business venture due to outdated information.

Thus, it is unlikely for the court to find that the presumption of business judgement Rule applies to this case given the actions of Alex and Baker, but even if it did it would be overcome by the breach of the duty of care by Alex and Baker.

2. Upon what theory or theories may the Pick shareholders bring claims against Cate and what is the likely result?

Derivative Suit (Supra)

Here, Similar to the argument above, when the board declined to address the initial demand by the shareholders, this allowed for a derivative suit to be brought, even against Cate for the breach of her fiduciary duty of loyalty to the corporation and for causing injuries to the corporation.

Thus, the shareholders are allowed to bring suit against Cate.

Duty of Loyalty

The board of directors owe a duty of loyalty to the corporation, meaning they cannot self deal or take business opportunities from the corporation.

Here, the shareholders are going to argue that Cate was self dealing when she decided to start a competing company E-Save. However, Cate is going to argue that she was not self dealing because before even starting E-Save, she presented the board with the business opportunity first. Cate will emphasize that the board decided to not take the business opportunity and as such she did not breach her duty of loyalty by starting her own company (see below).

Business Opportunity Rule

The business opportunity rule states that any director who is offered or has a potential business opportunity that they know is 1. similar to the corporation 2. can create revenue for the corporation. 3. cannot take the opportunity without first offering it to the board. If the board declines it then they are able to take the opportunity for themselves.

Here, Cate is going to argue that she was not self dealing because before she even started E-Save she gave the business opportunity to the board of directors. Cate knew that E-Save, was an opportunity was similar to Pick and that there was a potential for revenue, which is why she offered it to Alex and Baker in their board meeting. However, Alex and Baker completely declined to further look into the opportunity of creating E-Save. As such, Cate will emphasize that she fulfilled her obligation as a director by not taking the opportunity immediately and taking it to the board first as a potential business venture. However, when the board declined the opportunity, Cate will argue she no longer had a duty to not take the opportunity and as such she did not breach her duty of loyalty to Pick.

Thus, the court would find that there was no breach of duty of loyalty by Cate given she offered the opportunity to the board and they refused to take it.

Duty to Not Compete

There is a duty to not compete with the corporation when you are a director.

Here, Cate as previously mentioned decided to take on the business opportunity to create E-Save for herself. She was in the same business as Pick, just with a difference audience. As such the shareholders are going to argue she breached her duty of care by setting up the competing company E-Save, when she previously worked with Pick. However, Cate is going to argue that she did not breach her duty, because she offered it to Pick first and they refused to take it. The shareholders will argue, regardless if Alex and Baker did not take the opportunity she still should have not become a direct competitor of Pick.

Thus, the court would find for Cate because even though Cate is in the same business, she has a different audience, and therefore is not direct competition to Pick. Pick's board rejection gave Cate the opportunity to expand on her own without breaching her duty to Pick.

Question #1 Final Word Count = 1582

END OF EXAM