

Question MEE 3 – February 2022 – Selected Answer 1

1. Amy and Bill did have the authority as members of the board to vote to approve their trip to Belgium at corporate expense because they not only had the majority vote to approve the trip, but the trip was also a part of the corporation's ordinary course of business.

Under the Model Business Corporation Act (MBCA), members of the board of directors of a corporation only need a majority vote to approve of actions to conduct that are a part of the corporations ordinary course of business. Unless a corporation's articles of incorporation or bylaws state otherwise, a majority vote by members of the board is all that is required for voting to approve of a matter in the ordinary course of business.

Here, Amy and Bill traveled each year for the benefit of the corporation to places around the world for ideas to keep up in the brewing industry. As stated in the facts, this practice was considered to be in the ordinary course of business and the facts also stipulate that this type of travel to brewery conventions around the world expensed by employers was common practice in their industry of business. As board members and the individuals operating the everyday activities in the business, they had authority to vote to approve their trip to Belgium at their regularly scheduled meeting since their votes were in the majority.

Thus, Amy and Bill had the authority as board members to vote to approve their trip to Belgium at Corporate expense.

2. Amy and Bill did not violate the duty of loyalty by having the corporation pay the expense of the trip.

Under the MBCA, members of the board owe a duty to the corporation (the shareholders) not to act in a way that is against the interest of the corporation or to its detriment. The duty of loyalty is not violated in a corporation when judged under the business judgment rule that states that members of the board are able to make decisions in good faith for the benefit of the corporation. Courts give great deference to board members of a corporation as to fulfilling their duty of loyalty to the corporation when assessing decisions made by the board that was approved by vote and in light of the business judgment rule.

Here, Amy and Bill have not violated the duty of loyalty to the corporation and its shareholders (Amy, Bill, and Sharon) when viewing their decision through the lens of the business judgement rule in that their decision based on majority vote for the trip

to take place and at the corporation's expense was made in good faith for the benefit of the corporation to infuse new ideas for their products to ultimately increase revenue and product selection as well as keeping up with the competition. Based on the facts stating that the majority of their competitors engage in the same practice and that it is done in the ordinary course of business to keep up to date and competitive in the market, Sharon's opposition did not amount to a violation of their duty of loyalty to the corporation by having the corporation expense the trip.

Thus, Amy and Bill did not breach the duty of loyalty to the corporation by expensing the trip under the MBCA and when viewed against the requirements of the business judgment rule.

3. Assuming that Amy and Bill had violated their duty of loyalty by expensing their trip to Belgium at the corporation's expense, Sharon would not be able to personally recover from the expenses of the the current trip to Belgium.

Under the MBCA, a shareholder that sues a corporation for a breach of the duty of loyalty is not entitled to recover personally. Here, Sharon may bring suit against Amy and Bill for the current trip, however she is unlikely to succeed on her claim given the history of such trips made for the benefit of the corporation. A court would likely use the business judgment rule (see in (2)) to determine if Sharon was entitled to recovery personally, and although it would be unlikely she would succeed based on her losing the vote, she still would not be able to recover personally and any recovery would be awarded to the corporation itself.

Thus, Sharon is not likely to be able to recover personally from a breach of loyalty for the expenses of this trip.

4. Assuming that Amy and Bill had violated their duty of loyalty by expensing their trip to Belgium at the corporation's expense, Sharon would not be able to bring a derivative action suit against them to recover for prior trips to Germany.

Under the MBCA, a derivative action suit brought against a corporation is done so when a shareholder has a good faith basis to make a claim against the corporation for a breach for which the corporation should be compensated for. Under a derivative action suit, should a shareholder claim win, the award of judgment is awarded to the corporation, not the individual shareholder. In addition, a shareholder cannot bring a derivative action claim for claims of a breach of loyalty prior to becoming a shareholder or member of the board.

Here, should Sharon bring a derivative action claim to recover for Amy and Bill's prior trips to Germany under a breach of loyalty, she is unlikely to succeed since she had not say in how the corporation operated or allocated expenses before becoming a shareholder or board member.

Thus, Sharon would not recover in a derivative action claim for a breach of loyalty paid by BC related to prior trips to Germany since she was not a shareholder or board member then and was not owed any such duty of loyalty.

Question MEE 3 – February 2022 – Selected Answer 2

1.

Under the MBCA, boards of directors can agree on any ordinary business decision upon majority vote, with quorum, held in a regularly scheduled meeting. Extraordinary decision, such as mergers, recapitalization, and significant amendments to articles of incorporation, amongst others, require additional, more onerous requirements. Quorum for a board of directors meeting requires that a majority of the board be present at the start of the meeting, and at the time of the vote. Directors are agents of the corporation, and as such are authorized to take binding decisions for the corporation withing the regular course of ordinary business.

Here, a decision to fund a trip to Belgium is a normal, regular part of BC business. None of the major, extraordinary decisions requiring further procedures were present, and both BC itself and its competitors in the industry regularly go on such trips. Further, they are typically treated as "ordinary and necessary" parts of the business. Though in the past the trips have been to Germany, traveling to Belgium is substantially similar in nature, since it is for the same purpose and to a nearby destination that does not appear likely to generate expenses beyond past trips to Germany. Because the decision is a regular business decision, it only required the votes a a majority of the board of directors. All three directors were present at the meeting, so there was quoruam, and Amy and Bill together constitute a majority of the board. Thus they had authority to vote to approve the trip to Belgium.

2. Corporate directors owe a duty of loyalty to the corporation. This duty prohibits self-dealing at the corporation's expense, such as signing contracts between a personal business and the corporation, or taking profitable opportunities away from the corporation. While most corporate decisions are give wide latitude by the business judgment rule, which presumes that reasonably informed decisions are made in the best interest of the corporation, that rule does not apply in cases of duty of loyalty.

Here the issue is that Amy and Bill are expressly using part of the trip for personal pleasure, such as for sightseeing. This certainly involves the use of corporate funds for private gain, but such use is not wholly prohibited. Corporate funds may be used for reasonable personal expenditures such as dinners, golf outings, and company retreats. There is no suggestion here that a majority, or even a substantial amount, of the BC funds are being used for unrelated pleasure activities. Seeing a historical site or museum does not cost substantial time or money, and it is very clear both from industry practice and Amy and Bill's statements that the primary purpose of the trips is to learn about relevant industry techniques. The reasonableness of this trip is demonstrated by its widespread adoption by other brewers. Further, there is not indication at all that Amy and Bill are signing any contracts to their personal benefit, competing with BC in any way, or otherwise self-dealing. Thus they did not likely violate their duty of loyalty.

3. Individual claims from shareholders against corporate directors are proper when the violation of duties by those directors directly impacted the rights of the shareholder. Here, assuming Amy and Bill violated their duty of loyalty to BC, Sharon would have to demonstrate that this violation harmed her personally, either in her rights as a director or as a shareholder. Shareholder harms can be shown by demonstrating that the violation of duties owed to the corporation caused a loss in the value of the shares by reducing the value or funds of the corporation. This will be difficult for Sharon to show, because, even if the trip breached Amy and Bill's duties of loyalty, the only reasonable claim would be that it was their side-trip sightseeing that did so. Barring any extravagant expenses on these trips, it is very unlikely that any actual harm to Sharon's stock value occurred. Further, her rights as a director to object to the trip were exercised, she was simply outvoted, and her rights as a shareholder did not encompass prohibiting the trip, but only precatory statements discouraging it. So unless there is demonstrable harm to the value of her shares (which does not appear in the facts), Sharon would not be able to personally recover all the expenses of the trip.

4. Derivative claims are those brought by shareholders on behalf of a corporation, when the corporation itself does not or will not defend its own interests. They can be brought by a shareholder with standing, but only after first making a demand with the board of directors that the corporation file a suit or take other appropriate remedial action, unless such a demand is likely to be useless because ignored by the board. Further, a majority of the board of directors can, after a good faith investigation, determine that a derivative suit is against the best interests of the corporation and request that it be dismissed.

Here, Sharon does not have standing because she was not a shareholder at the time of the trips to Germany. While she was a shareholder during the Belgium trip, she was

not one during the prior trips to Germany. Thus she has no standing. Further, she has not made a clear demand to BC that they take action to recover the spending from that trip, though she could reasonably argue that such a demand be futile. Even if so, the rest of the board would likely request that any dispute be dropped. But because Sharon has no standing, she cannot bring a derivative suit for the trips to Germany.

Question MEE 3 – February 2022 – Selected Answer 3

1. Did Amy and Bill have authority as members of board to vote to approve their trip to Belgium?

Amy and Bill did have authority as members of the board to vote to approve their trip to Belgium. The issue is whether a quorum was present at the board meeting to approve the trip.

Board members run the day to day business of a corporation. Board meetings are held to further vote upon issues related to the running of the corporation. In order to pass a vote at a board meeting, a quorum of the board members must be present. A quorum is a majority of the members. For issues within the ordinary course of business, only a majority of board members need to approve.

Here, Bill and Amy represented a majority of the board, thus establishing a quorum at the monthly board meeting. The trip was arguably within the ordinary course of business as they traveled to trade shows to get ideas for the company. With 2 out of 3 voting for the trip to be approved, the vote is valid.

2. Did Amy and Bill violate the duty of loyalty?

Amy and Bill did not violate the duty of loyalty. The issue is whether the trip to Belgium by Amy and Bill was in the best interests of the corporation.

The duty of loyalty requires board members to put the interests of the corporation first. They are not to put their own self-interests or interests of other corporations first. Members are not to undercut the corporation in anyway.

Here, Amy and Bill are arguably not violating the duty of loyalty. Amy and Bill originally started traveling for the company "to learn about the latest in craft brewing." They were going to Belgium instead of Germany because Belgium "is where innovations in craft brewing are happening now and [they] want to bring back fresh ideas for [their] business. They were intending to take trips to other breweries to

further any ideas that would help their own. The biggest issue is using the trip to see museums and other sites while on these trips. It is arguable that this violates the duty because it uses company money for personal gain. However, the duty of loyalty is not violated because the main purpose of the trip is to improve the corporation. The interests of the corporation are still put first through these trips. There is no competing going on with another company. The best interest of the corporation is the purpose thus there is no violation of loyalty.

3. Can Sharon Recover personally?

Sharon cannot recover personally from Amy and Bill for violating the duty of loyalty. The issue is whether Amy and Bill as board members and shareholders are liable personally.

A corporation is itself an individual entity. Shareholders are not held personally liable for the acts of the corporation. Similarly, board members are not held personally liable for the acts of the corporation. Board members acts as agent for the corporation, thus leaving liability in the corporation itself.

Here, Amy and Bill cannot be held personally liable. As agents for the corporation, the corporation will be held liable for the acts of its members. Amy must go after the corporation to recover.

4. Derivative claim.

Sharon may not bring a derivative claim to recover from Amy and Bill the expenses paid by BC to their prior trips to Germany. The issue is whether Sharon has standing to bring such a claim.

A derivative claim is either brought on behalf of the corporation or against members of the corporation for violating the duty of loyalty. When a member brings a derivative action against members of the corporation, the misconduct must have previously been brought to the attention of the corporation and the corporation failed to do anything about it.

Here, Sharon was concerned about the trips to Germany every year at corporate expense. She stated at a board meeting that "the practice must stop." This statement brought the misconduct to the attention of the board. The board, namely Amy and Bill, failed to do anything to correct the action. Instead of going to Germany, they switched locations to going to Belgium for the same purpose. Sharon cannot bring a derivative action against past Germany trips because she was not a board member at

the time those trips occurred. The first trip to occur with Sharon on the board was to Belgium. this eliminates her standing to bring a derivative action.