**Agency**

**Formation** – Agency is a fiduciary relationship that results form the manifestation of consent by one person to another that the other shall act on his behalf and subject to his control. A principal must have contractual capacity, but the agent does not. Agency law requires no writing but the statute of frauds may.

**Actual express authority** – Express authority is that authority contained within the four corners of the partnership agreement and any authority expressly granted by vote of the partnership.

**Actual implied authority** – Implied authority is authority that the agent reasonably believes she has as a result of the actions of the principal. Absent an agreement to the contrary, all partners have equal rights in the management of the partnership business. Actual implied authority can be necessarily incidental to express authority or implied from acquiescence.

**Termination of actual authority** – Actual authority will be terminated (1) after specified time or event or after reasonable time, (2) by change of circumstances, (3) by a breach of agent’s fiduciary duties, (4) by a unilateral act of either the principal or the agent, or (5) by the death or incapacity of the principal or agent.

**Apparent authority** – Apparent authority exists if the partnership holds a partner out as possessing certain authority, thereby inducing others reasonably to believe that authority exists. The third party must reasonably rely on the holding out by the principal. Under RUPA, the act of any partner for apparently carrying on in the ordinary course of the partnership business or business of the kind carried out binds the partnership unless the partner had no authority to act for the partnership in the particular matter, and the person with whom the partner was dealing knew or had received notification that the partner lacked authority. Apparent authority is based on the principal’s manifestations to a third party; it cannot be created by the mere representations of an agent.

**Power of Position** – Apparent authority as well as actual implied authority may be established through an agent’s title or position.

**Lingering authority** – Where an agent’s actual authority has terminated, he will have apparent authority to act on the principal’s behalf as to all third parties with whom the principal knows he dealt unless and until the third parties receive either actual or constructive notice of the termination.

**Ratification** – A relationship is created by ratification when an “agent” purports to act on behalf of the principal without any authority at all, but the principal subsequently validates the act and becomes bound. For ratification to occur, the principal (1) must known or have reason to know all material facts, (2) accept the transaction, and (3) have capacity. But note that ratification cannot be used to alter the rights of intervening parties.

**Liability Rules on Contract** – The principal is liable on the contract and the agent is not if actual authority, apparent authority, or ratification is present. But if the principal is undisclosed or partially disclosed, the agent is also liable.

**Agent’s Fiduciary Duties to Principal** – An agent owes (1) a duty of care to carry out agency with reasonable care, (2) a duty of loyalty which includes (a) accounting to principal any profits made while carrying out instructions, (b) acting solely to benefit principal and not benefit himself, (c) not dealing with principal as adverse party, (d) not competing with principal concerning subject matter of agency, and (e) not using the principal’s property including confidential information. The agent also owes (3) a duty of obedience for all reasonable directions of his principal (note that principal will still be liable for agent’s acts in violation of directions).

**Principal’s Duties to Agent** – Not fiduciary in nature. Principal has a duty to indemnify the agent if the agent incurs expenses or losses and duty to compensate the agent for his services.

**Tort liability** – An employer is liable for a tort committed by an employee or servant in the scope of employment. The master and servant are jointly and severally liable to the third party. A person is subject to the control of another as to the means used to achieve a particular result. By contrast, if in control as to results only, then independent contractor. Factors include skill required, tools and facilities, period of employment, basis of compensation, business purpose, or if the person has their own distinct business. Generally, an employer is not liable for the intentional torts of an employee unless (1) it is natural from the nature of the job, (2) motivated to serve the employer, or (3) the employer specifically authorized. Likewise, an employer may be liable for torts of an employee during a minor deviation or detour, but not for a substantial deviation or frolic.

**Partnership**

**Formation** – A partnership is formed as soon as two or more persons associate to carry on as co-owners of a business for profit. The most important factor in deciding whether a partnership exists is sharing of profits, which is presumed to be a partnership unless the profits were received in payment of a debt, as wages or other compensation, as rent, or as interest on a loan. The partnership need not be in writing but the statute of frauds may require one.

**Partnership Agreement** – No agreement is required to form a partnership, but it an agreement allows the partners to contract around almost all statutory provisions. The agreement may be written, oral, or implied.

**Partnership voting and management** – All partners have equal rights in the management of the business and equal votes. Matters within the ordinary course of the partnership require a majority vote while matters outside the ordinary course require consent of all partners. There is no right to salary or compensation other than profits.

**Partnership financial rights** – Profits are shared equally and losses follow profits.

**Limited partnership** – A limited partnership (LP) is composed of one or more general partners and one or more limited partners. The general partners are personally liable for partnership obligations, while the limited partners generally do not have any liability beyond the liability to make agreed-upon contributions. In order to validly form an LP, a certificate of limited partnership must be filed with the secretary of state.

**Limited liability partnership** – To become a limited liability partnership (LLP), a partnership must file a statement of qualification with the secretary of state. A partnership becomes an LLP at the time of filing of the statement or on the date specified in the statement. The advantage of operating as an LLP is that the partners are not personally liable for the LLP’s obligations. However, a partner remains personally liable for his own wrongful acts.

**General partnership** – A general partnership (GP) is an association of two or more persons to carry on as co-owners a business for profit. There is no requirement that the parties subjectively intend to form a partnership, only that they intend to run a business as co-owners. Moreover, there are no formalities required to form a GP. Courts generally look to the intent of the parties to determine whether a GP exists. In a GP, all partners are jointly and severally liable for all obligations of the partnership, whether the obligations arise in contract or tort. Partners are also liable for any torts committed by a partner or by an employee of the partnership in the ordinary course of the partnership business or with authority of the partnership. Where one partner is compelled to pay or satisfy the whole of a partnership obligation, he is entitled to indemnification from the partnership. If the partnership is unable to indemnify, then he can seek contribution from the other partners.

**Partner** – To be a partner in a general partnership, one must agree with at least one other person to carry on as co-owners a business for profit. A person who receives a share of the profits of a business is presumed to be a partner. However, the presumption does not arise in certain circumstances, such as when the profits were received in payment of rent or when it is actually gross returns – not gross profits – that are being shared.

**Vicarious Liability** – Partners are liable for torts committed by an employee of the partnership in the ordinary course of partnership business or with authority of the partnership.

**Liability in contract (partners)** – Partnership is liable for contracts entered into on its behalf by partners with actual or apparent authority. Real property transactions are treated differently. Transfers of real property are binding on third parties if the statement of partnership authority is filed with the secretary of state and recorded. All other transactions are binding on the partnership but not on third parties.

**Fiduciary Duties of Partners** – Partners owe (1) duty of loyalty to account to partnership for any benefit derived in conducting partnership business or using property, to refrain from dealing adversely partnership, and to refrain from competing with the partnership. Partners also owe (2) a duty of care to refrain from engaging in grossly negligent or reckless conduct, intentional misconduct, or knowing violation of the law. Finally partners owe (3) duty of disclosure without demand for any information concerning partnership business and affairs required for proper exercise of partner’s rights and duties or, on demand, for any other information concerning the partnership business.

**Partnership property** – It is presumed to be partnership property if partnership funds are used. Presumed to be partner’s property if acquired in her name and without partnership funds and no sign she is acting for partnership. Partner is not a co-owner of partnership property and has no interest which can be transferred.

**Partnership ownership interest** – A partner cannot unilaterally transfer his management rights but may unilaterally transfer his financial rights. This does not make the transferee a partner.

**Dissociation** – When a partner withdraws from the partnership by giving notice to the partnership, partner’s expulsion, death or bankruptcy, or an agreed-upon event. Wrongful dissociation if in breach of express term of the partnership agreement, which requires looking at whether the partnership is at-will or a term partnership. A partner who wrongfully dissociates is liable for any damages. Partnership assets will be liquidated, or the partnership can continue and the other partners can buyout the dissociating partner’s interst.

**Dissolution** – Dissolution and winding up occur only in limited circumstances. In an at-will partnership, any partner who dissociates by express will may compel dissolution. In a term partnership, if one partner dissociates wrongfully or because of death or bankruptcy, dissolution only if one-half of the remaining partners agree to wind up the partnership. The priority of distribution is first to all creditors, including outside and inside creditors. Second, the partnership must repay all capital contributions paid into the partnership by the partners. Third, profits or losses, if any.

**Corporations**

**Formation** – To form a de jure corporation, there must be (1) an incorporator to execute the articles and deliver them, (2) the filing of the Articles of Incorporation with the secretary of state containing the corporate name, addresses, initial director, registered agent, statement of purpose, and capital structure, and (3) the delivery and notarization of the Articles along with some fees. The statement of purpose can be general (any lawful business) or specific.

**Ultra vires** – As a general rule, a corporation has the power to engage in any lawful business. However, a corporation may limit the business in which it may engage by having a narrow purpose provision in its articles of incorporation. A corporation may not carry on business outside the scope of its stated purpose. Business outside the scope of the stated purpose is said to be ultra vires. At common law, an ultra vires contract was illegal and unenforceable. However, it is more limited today. It may be raised only by (1) a shareholder seeking to enjoin a proposed ultra vires action, (2) the corporation seeking damages against the officers or directors who authorized the ultra vires act, or (3) the state, seeking to dissolve the corporation for engaging in an ultra vires act.

**De facto corporation** – If the corporation was not fully formed properly but the incorporators are unaware of the deficiencies, a de facto corporation can be found under the relevant statute if there has been a good faith attempt to comply with the formalities and some exercise of corporate privileges.

**Corporation by estoppel** – Similarly, if a third party is unaware of the failure to form properly, a corporation by estoppel arises where a third party deals with them as a corporation and assumes the risk of limited liability.

**Pre-incorporation contracts** – As a general rule, corporations are legal entities separate and apart from their shareholders. One consequence of this is that corporations are not liable for contracts made prior to incorporation. Generally only the promoters are liable on pre-incorporation contracts, even if the third party with whom the promoter dealt knew that the corporation had not yet been formed. The corporation may become liable only if it adopts the contract. Adoption may be explicit or implicit.

**Pre-emptive Rights** – Rights of existing shareholders to maintain their percentage ownership by buying stock whenever the corporation has a new issuance for money. Rights must be in the articles.

**Duty of care** – Directors and officers are fiduciaries and owe the corporation the duty to act in good faith and with the care that an ordinarily prudent person in a like position would exercise for their own business. Specific problems arise where there is nonfeasance or misfeasance.

**Nonfeasance** – Directors and officers breach the duty of care due to nonfeasance only if the breach caused the loss to the corporation.

**Misfeasance** – Directors and officers can breach the duty of care due to misfeasance, but a court will apply the business judgment rule. Under the BJR, a court will not second-guess a business decision if it was informed, made in good faith, without conflicts of interest, and had a rational basis. Directors who meet the duty of care standard of conduct will not be liable for corporate designs that, in hindsight, turned out to be poor or erroneous.

**Duty of loyalty** – Directors and officers are fiduciaries and owe the corporation the duty of loyalty to act in good faith and with reasonable belief that they are acting in the corporation’s best interest. This duty prohibits a director competing with his corporation. It also bars a director from usurping corporate opportunities – a director cannot take for himself a business opportunity in which his corporation might have an interest unless he first offers the opportunity to the corporation and the corporation rejects the opportunity. The burden of rebutting a breach of the duty of loyalty is on the defendant.

**Interested director transaction** – A director owes a duty of loyalty to the corporation and will not be permitted to profit at the expense of the corporation. If a director has a personal interest in a transaction in which his corporation is a party, a conflict of interest arises. A conflicting interest arises if the director knows that a related person is a party to the transaction. An interested director transaction can be upheld ONLY IF (1) it was fair to the corporation when entered into, (2) the majority of disinterested directors approve, and (3) the majority of disinterested shares approve. Some courts also require an independent showing of fairness.

**Competing ventures** – A director or officer cannot compete with the corporation, or else a court may impose a constructive trust on whatever profits the director or officer gains from the competing venture.

**Usurpation of corporate opportunity** – Director cannot usurp a corporate opportunity until he tells the board about it and waits for board to reject the opportunity. The closer the opportunity is to the corporation’s line of business, the more likely a court will find it to be a corporate opportunity. The corporation’s lack of financial ability to take advantage of the opportunity typically is not a defense. If a director does not give the corporation an opportunity to act but rather usurps the opportunity, the corporation can recover the profits that the director made from the transaction or may force the director to convey the opportunity to the corporation, under a constructive trust theory, for whatever consideration the director purchased the opportunity.

**Shareholder voting agreements** – Shareholders may enter into written/signed agreement providing for the manner in which they will vote their shares. Need not be filed with the corporation and not subject to any time limit.

**Shareholder proxy agreements** – Shareholder may vote his shares in person/by proxy executed in writing. A proxy will only be valid for 11 months unless otherwise provided. Appointment of proxy is generally revocable by shareholder. Proxy is irrevocable only if appointment form conspicuously states so and the appointment is coupled with an interest, which may be in shares of the corporation.

**Shareholder liability and PCV** – As a general rule, shareholders in a properly formed corporation are not personally liable for the obligations of their corporation. However, to prevent fraud or unfairness, a court will pierce the corporate veil and hold shareholders personally liable for the corporation’s obligations where (1) corporate formalities have been ignored and injustice has resulted; (2) the corporation was inadequately capitalized at the time of formation, or (3) the corporate form is being used to perpetrate a fraud. Courts are more likely to PCV for a tort victim than a contract victim because the tort victim did not voluntarily choose to transact wit a corporation and assume the risk of limited liability.

**Derivative Suits** – Shareholders may file a derivative suit to enforce the corporation’s claim, not a personal claim, where (1) stock ownership when the claim arose and throughout the suit, (2) adequate representation of the corporation’s interest, (3) written demand on the corporation that they bring the suit, and (4) corporation joined the suit initially as defendant.

**Shareholder as creditor** - Shareholders may become creditors of the corporation by lending the corporation money and receiving a promissory note from the corporation as evidence of the debt owed. Also, shareholders who are unsecured creditors are not subordinate to other, outside unsecured creditors.

**Controlling shareholder duty not to unfairly prejudice minority shareholders** – Generally, shareholders act in their own personal interests and owe no fiduciary duty to the corporation or their fellow shareholders. However, modern law imposes a duty on a controlling shareholder to refrain from using his control to obtain a special advantage or to cause the corporation to take action that unfairly prejudices the minority shareholders.

**Fundamental corporate change** – Generally, only the directors, officers and board manage the business, set policies or declare distributions. However, certain changes cannot be done by the board alone. To make a fundamental corporate change, there must be (1) a majority of the board of directors adopts a resolution recommending the change, (2) notice of the proposed change to all shareholders (whether or not entitled to vote) at least 10 days in advance of the meeting, (3) approval by a majority of all votes entitled to be cast and by a majority of any voting group entitled to vote as a group, and (4) the change must be formalized in the articles which are filed with the state. Fundamental corporate changes include (1) amendment of the articles, (2) mergers or consolidations, (3) transfers of assets not in the ordinary course of business, and (4) dissolution.

**Dissenting shareholder right of appraisal** – In a close corporation, a dissenting shareholder may force the corporation to buy its stock for fair value before a fundamental corporate change. The shareholder must first file a written notice of objection and intent to demand payment, abstain or vote against the proposed change, and after the vote make a written demand to be bought out.

**10b-5 violations under federal securities act** – Section 10b prohibits fraud or misrepresentation in connection with the purchase or sale of any security. To establish a 10b5 violation, there must be (1) fraudulent conduct such as misrepresentation of material information, insider trading, or tipping, (2) in connection with the purchase or sale of any security, (3) use of a means of interstate commerce, (4) an intent to deceive, manipulate or defraud, and in some cases (5) reliance and (6) damages in private causes of action. Information is material if a reasonable investor would consider it important when making an investment decision. Scienter requires intent to deceive. Forms of fraudulent conduct include (1) insider trading, (2) tipping, (3) misappropriation, or (4) tippee liability.

**Insider trading** - One of the most common forms of fraudulent conduct under rule 10b5 is insider trading. Insider trading occurs where there is a duty to abstain or disclose certain information. A corporate insider who breaches a duty not to use inside information for personal benefit can be held liable under 10b5. Typical insiders such as directors, officers, and employees are deemed to owe a duty of trust and confidence to their corporation that is breached by trading on inside information.

**Tipping** – Tipping occurs where the insider passes material information for a wrongful purpose.

**Misappropriation** - Misappropriation occurs where there is a duty to the source of the information.

**Tippee** – One who does not owe any duties to the corporation since they are not a corporate insider may still be liable as a tippee under 10-b if the tipper breached a duty by disclosing the information and the tippee knew that the tipper was breaching the duty.

**Section 16b short-swing trading** – Section 16b of the Securities Exchange Act provides that any profit realized by a director, officer or shareholder owning more than 10% of the outstanding shares of the corporation from any purchase and sale of any equity security of his corporation within a period of less than six months must be returned to the corporation. The section applies to publicly held corporations whose shares are traded on a national exchange or that have (1) at least 2,000 shareholders and (2) more than $10 million in assets. The purpose of 16b is to prevent unfair use of inside information and internal manipulation of price. This is accomplished by imposing strict liability for covered transactions whether or not there is any material fact that should or could have been disclosed – no proof of use of inside information is required.