

Empire College School of Law
Professor Viveka A. Rydell
Business Organizations - Spring 2016
April 11, 2016

Student ID# _____

This examination covers Introduction to Forms of Business Entities through Insider Trading and Other Securities Fraud (Chapters 1-19).

This examination will test your knowledge of the materials that we covered in class. Please answer each question concisely. Please use headings, underline issues and rules, as this will help you organize your thoughts, spot and frame the legal issues, and present the rules and doctrines clearly. Try to answer all questions with complete sentences. Do not use abbreviations, other than those commonly used for each business organization (like LLP). Answer all questions presented. If you cannot answer a question completely, answer as best you can. If not all fact are present, by all means, address scenarios. Partial answers will be given partial credit. Please write clearly. **You have 3 hours for this examination. Good luck!**

PART I (50 POINTS)

- A. In June 2014, photographer Anna Smith (A) and her college friend, another SSU fine arts major, sculptor Bob Williams (B), approached you about an idea to open a new art studio in Healdsburg, which they would like to call AB+Arts. They also have an idea for an interactive App called Sono-Arts that lets people post invitations to experiential events at different gorgeous Sonoma County venues, post photos from the art created or seen there, sell tickets, and any art objects left over from those events. Anna's aunt Cheryl (C), who is an art gallery owner in San Francisco, with a second home in Healdsburg, will invest \$200,000. Cheryl also has Cloverdale office space that the former art students are allowed to use for free (following the dot-com bust, local commercial leasing space was at 20% vacancy rates). Cheryl is also a lawyer and has offered to be their lawyer. Anna and Bob come to you (a friend from a local yoga class) for advice.
- Draft a memo on which business forms to consider, the pros and cons of each
 - In the case they choose a Corporation, what must Articles of Incorporation include?
 - Address whether it is advisable for Cheryl to be their lawyer, and if not, why not
- B. By May 2016, benefiting from the artistic founders' hard and creative work, AB+Arts (by then a Healdsburg-based corporation) has become a well-known art gallery in Healdsburg. This notoriety, coupled some remarkably well-timed growth in the economy (and with it, and interest and expendable income to buy art) and a spike in art appreciation due to the announcement of an internationally renowned photographer moving to Sonoma County, AB+Arts has stock is valued at \$50/share. Things have changed a bit since 2014. Cheryl would like to get paid for the office space (even the Healdsburg market for delapidated buildings is hot), Anna has become a certified Yoga teacher. Anna still creates art, but she is working less on the client/sales side; leaving Bob with most of the day-to-day work to both be an artist and an art gallery owner/seller. Bob is tired of working long hours (evening shows for tourists on weekends). During a hike at Lake Sonoma, Bob decides he wants to get out of their company, to help children in Kenya, with his sculptures.

ARTBOX, a publicly-traded Lifestyle Brand corporation headquartered in New York, enters into an agreement with Cheryl (now both a majority shareholder and a director) of Sono-Arts. The agreement states that, as long as no AB+Arts directors lost their seats on the board of directors, Cheryl would sell her 60% interest to ARTBOX for \$100 per share, giving ARTBOX control of

AB+Arts. The sale is likely to make the other 40% of AB+Arts stock less valuable because Sono-Arts has over the years borrowed heavily (on art supplies and "inspirational trips," and paid its shareholders large travel reimbursements as well as dividends to create "content" for the Sono-Arts App.

Without telling Anna and Bob, Cheryl entered the agreement with ARTBOX, as she felt strongly that transforming AB+Arts, and the Sono-Arts App into a "Sonoma life style brand" would be the only way to save the company from impending bankruptcy. She has also signed contracts on behalf of AB+Arts for water bottles, coffee mugs, picnic blankets, wine label art, and wine event sponsorships, without consulting her fellow board members.

Shortly thereafter, ARTBOX put on an experiential Art Installation in Geyserville. Sadly, the pyrotechnic component of the mobile art object back-fired. Tourist/Plaintiff David Brown (D), had severe burn injury on 50% of his body and had to be treated at Memorial Hospital for 2 months. The bills were in the amount of \$200,000, and as he was the sole provider of his family of three, the economic loss to them was 2 months of salary at his San Francisco tech company.

PART II (50 POINTS)

Answer the following questions.

1. When seeking minority shareholder approval for a proposed cash-out merger, which test must the corporation involved comply with. After naming the test, please also name and explain the two interrelated aspects of that test.
2. What are the three venues under which Securities Fraud actions may be brought?
3. Describe the different tools used to shield directors and officers from personal liability for actions (or inactions).
4. When might Board of Directors be found to have violated his or her Oversight responsibilities?
5. Describe the Williams Act and the policy reasons behind its enactment.
6. In what three instances may a fiduciary's failure to act in GOOD FAITH be shown?

7. Describe the Business Judgment Rule, as well as factors to be considered in "piercing the corporate veil."
8. To recover for corporate "waste," what must a plaintiff typically show?
9. What is the "Misappropriations Theory"?
10. Who is a Promoter, what does he/she do, and what is the extent of a promoter's liability?

END OF EXAMINATION