

**Excerpted pages from**  
**INTRODUCTION TO THE LAW AND LEGAL SYSTEM OF THE UNITED STATES**  
**(Third Edition)**  
**(West Group Publishing Company, 2002)**  
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**CHAPTER XV**

**BUSINESS LAW**

This chapter will outline some of the more important legal aspects of doing business in the United States: the law of business organizations, securities law, antitrust law, bankruptcy, labor and employment law and environmental law. Sources for further study are cited in each section.

**A. Business Organizations**

Most business enterprises are organized in one of three ways: as a sole proprietorship, as a partnership (general or limited), or as a corporation. In addition, a new form of business entity, the limited liability company, has recently emerged. Each business organization shares some common aspects with others, but differs in method of ownership, the degree of personal liability of the investors for the enterprise's debts and in the complexity of the structure. Business organizations are governed primarily by state law, with a few areas governed by federal law.<sup>1</sup>

**1. Sole Proprietorships**

A sole proprietorship is a business enterprise owned solely by one individual. It is the most elementary organizational form of business. Small new businesses often begin as sole proprietorships because they are the simplest and least expensive to form and operate. Local accountants or attorneys in business for themselves or small retail shops are likely to be sole proprietorships.

The formation, operation, and management of sole proprietorships are generally simple. It is not necessary to file any documents with any governmental office other than local requirements (by a city or county) that the owner register the name of the business to prevent fraud. This registration would notify the public, for example, that John Smith is "doing business as Smith's Hardware Store."

The owner has total control, making all decisions concerning the business. Employees may be hired, and some management authority may be delegated to them, but the sole proprietor maintains ultimate control. Businesses that are sole proprietorships are not considered separate legal entities apart from the owner. Thus, the owner of the business is personally liable for all of the business' debts out of the owner's

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<sup>1</sup> Two texts that survey business law for undergraduate students in college are RICHARD A. MANN & BARRY S. ROBERTS, *BUSINESS LAW*, 8TH ED. (West 1991) and KENNETH W. CLARKSTON, ET. AL., *WEST'S BUSINESS LAW* 4TH ED. (West 1989). See also ROBERT W. HAMILTON & RICHARD BOOTH, *BUSINESS BASICS FOR LAW STUDENTS*, 2D ED. (Aspen 1998). Law student guides to the legal aspects of business include WILLIAM A. KLEIN & JOHN C. COFFEE, JR., *BUSINESS ORGANIZATION AND FINANCE: LEGAL AND ECONOMIC PRINCIPLES*, 6TH ED. (Foundation Press 1996). For more detail on corporations, see HARRY G. HENN AND JOHN R. ALEXANDER, *LAW OF CORPORATIONS*, 3D ED. (West 1983, 1986) or ROBERT C. CLARK, *CORPORATE LAW* (Aspen 1986). Succinct guides to many of the issues discussed here are ROBERT W. HAMILTON, *THE LAW OF CORPORATIONS IN A NUTSHELL* (West 1996); ROBERT W. HAMILTON, *BUSINESS ORGANIZATIONS: UNINCORPORATED BUSINESSES AND CLOSELY HELD CORPORATIONS* (Aspen 1997); and LEWIS D. SOLOMON & ALAN R. PALMITEV, *CORPORATIONS: EXAMPLES AND EXPLANATIONS*, 2D ED. (Aspen 1994).

personal assets. However, the owner also reaps all the fruits of the business and need not pay partners or shareholders anything.

The identity of owner and business entails a tax advantage as well. Unlike corporations, sole proprietorships are not considered to be separate taxable entities by the Internal Revenue Service (IRS), the federal income taxing agency. Therefore, unlike the corporation, the sole proprietorship business itself does not have to pay federal income taxes. Instead, the income and deductible expenses of the business are reported on the owner's personal tax return.<sup>2</sup>

## 2. General Partnerships

*Nature of General Partnerships* A partnership is an association of two or more persons to carry on a business for profit as co-owners.<sup>3</sup> There are two kinds of partnerships, general and limited. General partnerships (GP) are discussed here and limited partnerships (LP) are discussed in the next section.

An agreement to operate as a partnership can be written, but unlike a corporation or limited partnership, there is no requirement that any documents be filed with any governmental authority. The agreement may even be oral and a partnership agreement may even be implied from conduct despite a written agreement to the contrary. For example, a business subject to a "partnership agreement" was held not to be a partnership and a business not formally described as a partnership was deemed to be one.<sup>4</sup> Thus, people in business together often may not realize that they are partners subject to all the rights and obligations arising out of a partnership, including the important principle that one partner can bind the entire partnership to debts.<sup>5</sup>

*Reasons for Choice of Form* Like the sole proprietor, partners in a GP are exposed to unlimited liability and the partnership does not have to pay income taxes separate from its owners. Instead, the income or loss of the business is reported on the partners' personal individual tax returns. The choice of the partnership form rather than a sole proprietorship is made because two or more people want to go into business together. A partnership is chosen over a corporation to avoid the complexities involved in forming and running a corporation.

*Formation* The Uniform Partnership Act (UPA) governs the formation, operation, and structure of partnerships in almost all states.<sup>6</sup> Partners may agree to almost any arrangement between them that is not illegal or contrary to public policy. Thus, much of the UPA provides simply a "default provision" — applicable only in the absence of express agreements in the partnership agreement.<sup>7</sup> However, some UPA provisions cannot be changed by agreement of the partners. Among them are provisions declaring that each partner is personally liable for all of the partnership's debts<sup>8</sup> and that each partner owes a "fiduciary duty" to the partnership and the other partners.<sup>9</sup> This fiduciary duty means that each partner must abide by the highest standards of loyalty, good faith, and integrity when engaging in matters pertaining to the

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<sup>2</sup> See HENN & ALEXANDER, *supra* note 1, §18. As explained *infra* p.562, it is possible to reduce the tax disadvantage of the corporate form with closely held corporations by "zeroing out" income through distributions to employees.

<sup>3</sup> Uniform Partnership Act (UPA) §6, 6 UNIF.L.ANN. 1 (1969). All states except Louisiana have adopted the UPA, with some local variations from it. See generally HENN & ALEXANDER, *supra* note 1, §§19-27. Copies of this act, the Uniform Limited Partnership Act and various statutes and rules related to business enterprises are set out in EDWARDS, ADAMS & JOHN H. MATHESON, EDS., SELECTED CORPORATION AND OTHER BUSINESS ASSOCIATIONS: STATUTES, RULES AND FORMS (West 1998).

<sup>4</sup> *Cutler v. Bowen*, 543 P.2d 1349 (Utah 1975) (owner of furnishings, equipment and lease of bar must share compensation for harm to business with bartender-manager because they were partners pursuant to oral agreement to share profits); *Chaiken v. Employment Security Commission*, 274 A.2d 707 (Super. Ct Del. 1971) (nature of agreement showed that barbers working in shop were employees for whom unemployment tax was due, not partners).

<sup>5</sup> UPA §9.

<sup>6</sup> See *supra* note 3.

<sup>7</sup> UPA §4.

<sup>8</sup> *Id.* §15.

<sup>9</sup> *Id.* §21.

partnership.<sup>10</sup> Any partner who fails to act in the best interest of the partnership or who acts in personal self interest is liable to the partnership. Thus a partner who uses partnership assets for personal gain is liable to the partnership for all the resulting profits.<sup>11</sup>

Each partner is required to make an initial contribution to the business in the form of cash, property, services, or some combination of these. The amount of each partner's contribution need not be the same. For example, in forming the ABC partnership, partner A might contribute \$10,000 in cash, partner B might contribute \$5,000 in cash and a \$15,000 building, and partner C might agree to perform \$20,000 worth of management services as an initial capital contribution. If a written partnership agreement exists, it will usually detail each partner's contribution.

*Operation and Management* Pursuant to the UPA, all general partners have an equal voice in the operation and management of the business, unless otherwise agreed, regardless of the amount of capital contributions made by the individual partners. Thus, each partner is entitled to one vote on management matters, and decisions are made on a majority basis.<sup>12</sup> The act of any partner in the name of the partnership binds the partnership.

Partners can agree in the partnership agreement that decision-making authority will be granted to only one or a given group of the partners. Or the partners may agree to afford management powers in proportion to the capital contributions of each partner. For example, in the ABC partnership formed above, the partnership agreement might specify that A gets one vote, while B and C get two votes each. In the absence of such a partnership agreement, A, B, and C would each have one vote.<sup>13</sup>

*Sharing Profits and Losses and Compensation Rights* In the absence of an agreement to the contrary, all partners share in the profits and losses of the partnership equally, regardless of the amount of cash, property, or services contributed by each partner to the partnership. The equal sharing rule is often altered by an appropriate provision in the partnership agreement, which makes the distribution of profits proportional with the amount of capital contribution of each partner. For example, the ABC partnership, in its written partnership agreement, might provide that A is entitled to 20% of the partnership's profits, while B and C are each entitled to 40% of its profits. But partners can elect to allocate profits and losses in any manner they wish, regardless of the partners' initial capital contribution.

The partnership's losses and income can be distributed among the partners in any way they wish. This may be done to provide tax benefits to certain partners, because losses are often deductible on the partners' personal tax returns. If no provision is made for the distribution of losses, the UPA requires that losses be distributed in the same manner as profits are shared.<sup>14</sup>

The partnership agreement can provide that some partners will be compensated for services rendered to the partnership. However, if the partnership agreement does not specifically say so, no partner is entitled to any compensation, regardless of any services provided. Absent express agreement to the contrary, the partners' shares of the profits are considered to be their full compensation.<sup>15</sup>

*Dissolution* Each partner has the inherent power to withdraw from the partnership and cause a dissolution, and the death or bankruptcy of a partner automatically causes dissolution.<sup>16</sup> The UPA states that the withdrawing partner or the partner's estate has the power to cause the partnership to wind up its affairs

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<sup>10</sup> A classic discussion of fiduciary duty is set out in *Meinhard v. Salmon*, 164 N.E.2d 544 (N.Y. 1928) (Cardozo, J.).

<sup>11</sup> *Clement v. Clement*, 260 A.2d 728 (Pa. 1970) (fraud not necessary for recovery by one partner against another; all that need be shown is that second partner freely converted partnership assets to his own personal use).

<sup>12</sup> UPA §18.

<sup>13</sup> *Id.* §18. HENN & ALEXANDER, *supra* note 1, §§20-22.

<sup>14</sup> UPA §18. The partnership's flexibility in allocating income and losses a particular way is a useful way to "shelter" income from taxes, a practice widely used in limited partnerships, as discussed below.

<sup>15</sup> *Id.* See HENN & ALEXANDER, *supra* note 1, §23.

<sup>16</sup> These and other grounds for dissolution are listed in UPA §31.

and liquidate its assets, and pay each partner a sum representing that partner's interest.<sup>17</sup> But the partnership agreement will typically state that the business will continue and that the withdrawing partner or the partner's estate will be entitled to a sum of money representing the partner's interest in the partnership upon death or withdrawal. Even when liquidation is an option with the withdrawing partner or a partner's estate, it is often in everyone's best interest to continue operations and pay off the withdrawing partner or estate.<sup>18</sup>

*Withdrawal of Partners* A partnership agreement may limit a partner's intentional withdrawal from the partnership for a period of time. Thus, if money has been borrowed, partners may not be permitted to withdraw until the loan is paid off. These provisions cannot stop a partner from exercising the right to withdraw and cause dissolution. But the partnership can continue the business by posting a bond to secure payment of the withdrawing partner's share at the end of the time period set in the agreement. Moreover, the withdrawing partner could be liable for damages for wrongful termination of the partnership and will in any event not receive full value upon distribution of assets.<sup>19</sup>

### 3. Limited Partnerships

*Nature and Business Reasons for Choice of Form* A limited partnership (LP) has both general and limited partners. It differs from a general partnership in the fact that the limited partners are not subject to unlimited liability for the debts of the business and risk only the loss of their initial capital contribution to the partnership. Correspondingly, limited partners have little control over the running of the business, which is run by the general partner or partners. Thus, an LP is often the choice of a businessperson who wishes to raise capital, but does not wish to give up control over the business as would happen with a general partnership.

Today, *general* partnerships are often small- to medium-sized businesses operating within the local community and generally have relatively few partners. LPS, on the other hand, are usually much larger because, among other reasons, the LP is popular with investors as a tax shelter device, as discussed below. LPS will often have one general partner and hundreds or thousands of limited partners.<sup>20</sup>

*Formation* LPS can be formed only by compliance with state statutory requirements. Most all states have adopted the Uniform Limited Partnership Act (ULPA)<sup>21</sup> or the Revised Uniform Limited Partnership Act (RULPA)<sup>22</sup> to govern the formation and operation of limited partnerships. To form an LP, a certificate of limited partnership must be filed with a designated state official. This certificate must include specified information concerning the LP, such as the names and addresses of the general and limited partners, the amount of each partner's capital contribution, and the manner in which profits are to be shared.<sup>23</sup> LPS are also required to have a written partnership agreement.<sup>24</sup> In most cases, the certificate of limited partnership and the written partnership agreement are the same thing.

*Operation and Management* Every LP must have at least one general partner and one limited partner. In most circumstances, the general partners in an LP have the same rights and duties as partners in a general partnership and manage the business as provided in the agreement.<sup>25</sup> Limited partners, on the other hand, are treated as investors. They have no rights to participate in the management of the business, to use

<sup>17</sup> *Id.* §37.

<sup>18</sup> *See generally* HENN & ALEXANDER, *supra* note 2, §26.

<sup>19</sup> UPA §38(c). A recent practical article on how to mediate "business divorces" in partnerships and small corporations is James C. Freund, *Anatomy of a Split-Up: Mediating the Business Divorce*, 53 BUSINESS LAWYER 479 (1997).

<sup>20</sup> *See generally* HENN & ALEXANDER, *supra* note 1, §§28-36.

<sup>21</sup> 6 Unif.L. Ann. §§1-31 (1969).

<sup>22</sup> 6 Unif.L. Ann. §§101-1106 (Supp. 1993).

<sup>23</sup> ULPA §2.

<sup>24</sup> *Id.* §2.

<sup>25</sup> *Id.* §9.

partnership property, or to conduct business on behalf of the partnership. However, they are entitled to share in the profits of the business as specified in the partnership agreement.<sup>26</sup>

The exact extent to which limited partners can participate in the business without losing their limited liability status is often undefined. The ULPA states that a limited partner becomes liable as a general partner if the partner “takes part in the control of the business.”<sup>27</sup> The RULPA has a list of “safe harbor” activities in which a limited partner may engage without losing limited liability.<sup>28</sup> As a general rule, any limited partner who engages in management decisions on an ongoing basis will lose limited partner status and will be subject to unlimited liability. Some gross control over management is permitted. Thus, the agreement can give limited partners the right to remove the general partner. In addition, under some circumstances limited partners have been allowed to sue to contest the propriety of the general partner’s management decisions, similar to the right of shareholders in a corporation.<sup>29</sup>

**Dissolution** Unlike the withdrawal or death of any general partner in an LP, a limited partner’s withdrawal or death does not cause dissolution. Upon withdrawal or death, limited partners or their estates are entitled to the value of their interest in the LP.

**Special Tax Aspects of Limited Partnerships** As stated earlier, the partnership form has great flexibility in allocating income and losses among partners. This characteristic has been capitalized upon to provide a “tax shelter” for money. Typically two groups come together for mutual benefit: entrepreneurs with skill, but no money, and taxpayers with high incomes seeking business losses to claim on their tax returns to offset income.<sup>30</sup> For example, assume that a developer believes that there is a need for an office building in a big city, but it has no money. Often the developer will seek out people with high incomes taxed at a high rate to invest their money as limited partners in a partnership formed to build and then rent out and manage the building. The developer uses the investment to build the building, takes the rents from the building as income and allocates the losses (primarily in the form of depreciation of the building) to the limited partner investors. These losses, taken each year for several years, serve to reduce the amount of income from other sources on which the investors must pay taxes. The developer gets the money needed to build the building, and the investors are protected by limited liability from losing more than their investment, and get a substantial tax savings.<sup>31</sup>

## 4. Corporations

### a. General Nature

Corporations are recognized as legal entities distinct from their owners — “shareholders,” so-called because they “hold” a “share” of the overall ownership of the corporation. Corporations can sue and be sued, enter into contractual relations, and own property. Corporations even have constitutional rights separate from their owners or management: since 1868 corporations have been able to sue for violations of their 14th

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<sup>26</sup> *Id.* §§10, 17.

<sup>27</sup> *Id.* §7. See *Alzado v. Blinder, Robinson & Co., Inc.*, 752 P.2d 544 (Colo. 1988) (holding activities of limited partner in promoting boxing match were not sufficient to render him liable).

<sup>28</sup> RULPA §303. These include working as a contractor for the partnership or consulting and advising the general partner with respect to the business.

<sup>29</sup> See RULPA §§1001-1004. In such cases, the managing general partner is judged under the same “business judgment rule” applicable to corporate managers, discussed *infra* p. 566. See *Wylter v. Feuer*, 149 Cal.Rptr. 626 (Cal.App.1978) (finding no basis for suit by limited partners when partnership’s movie did not make money).

<sup>30</sup> The federal income tax system is moderately “progressive,” meaning that as income goes up, the rate of taxation does as well. In general, the tax rate is between 15% and 40%.

<sup>31</sup> The losses taken on the investors tax returns do not relieve the limited partners of tax liability for the benefits of the value of the building. They will pay for the gain their investment has produced when the building is sold years later. But such a “tax deferral,” generally for a number of years, provides the limited partners with real benefit. First, they have the *use* of the money that would have otherwise been paid in taxes over several years. Second, their overall tax liability is less when the building is sold years later, because the investors will often be retired and therefore have less income. Taxpayers with lower incomes pay a smaller percentage of their income in taxes. For more detail, see sources cited in note 44, *infra*, and see generally Chapter XVI, where income and other federal taxes are discussed.

Amendment due process and other rights.<sup>32</sup> One of the principal values of the corporate form of doing business is its limited liability. Absent exceptional circumstances, the shareholders in the corporation cannot be held personally liable for debts incurred or liability imposed on the corporation. However, this is only one feature of the corporation that must be weighed in deciding whether to incorporate, as discussed below.

Corporations law is principally state law. It is largely statutory, but the common law is often relied upon, especially when defining the fiduciary duties of management. Federal law governs trading in publicly-offered corporate securities<sup>33</sup> and federal income taxation law drives some corporate decision-making.<sup>34</sup> There is a Model Business Corporation Act (MBCA) and Revised Model Business Corporation Act (RMBCA) promulgated by a committee of the American Bar Association.<sup>35</sup> However, the MBCA and RMBCA have not gained as wide acceptance by state legislatures as the uniform partnership laws have.

The corporate law of the state of Delaware is very important. Generally, the laws of the state where the company was incorporated control issues of governance of a corporation even when all the corporation's offices and facilities are in other states. Delaware has tried its best to be an attractive state for incorporation by providing perhaps the greatest flexibility for corporate governance. Thus, Delaware has won what some have called "the race to the bottom" that began in the early 20th century — a competition among states to pass corporate laws that least restrict corporate management prerogatives.<sup>36</sup> As a result, over one-third of the corporations listed on the New York Stock Exchange are incorporated in Delaware. The great number of Delaware corporations has in turn produced a great number of cases decided under Delaware law. As a result, Delaware corporate law is by far the most well-developed and therefore the most predictable.<sup>37</sup>

### b. Types of Corporations

There are all sizes of corporations, but it is generally helpful to distinguish between two types: publicly held corporations and closely-held corporations. Both are created by state statute and are subject to the same basic rules. Both can conduct the same types of business. But they inhabit different worlds in terms of ownership and operation. Among the differences is the fact that publicly held corporations are subject to federal regulation to a much greater extent.

*Publicly Held Corporations* Publicly held corporations are those whose shares are traded by the general public in organized markets, such as the New York Stock Exchange, other national exchanges or in the "over-the-counter" markets. These are the largest corporations, such as Exxon, General Motors and IBM. Their stockholders are numerous, widely dispersed and constantly changing. Most shareholders purchase shares as an investment and have no desire to become involved in management decisions or even to attend stockholders' meetings or vote. However, some holders of major blocks of stock serve as directors or managers, are active at shareholder meetings or otherwise seek to affect management decisions.

*Closely-Held Corporations* Closely-held corporations, called close corporations, are corporations that

<sup>32</sup> See *Paul v. Virginia*, 75 U.S. (8 Wall.) 168 (1868) (corporation is a "person" as that term is used in the 14th Amendment). Corporations have been responsible for raising most of the issues of 1st Amendment commercial speech. See Chapter IX, pp. 373-374. Strangely enough, while it is a "person," a corporation is not a "citizen" protected by the privileges and immunities clause of the 14th Amendment or Article IV. See Chapter IX, p. 337. This is so despite the fact that a corporation can be a citizen of a state for purposes of diversity of citizenship. See Chapter V, p. 188.

<sup>33</sup> See *infra* p. 572.

<sup>34</sup> See *infra* p. 561.

<sup>35</sup> See MODEL BUSINESS CORPORATION ACT ANN., 3D ED. (Prentice Hall Law & Bus. 1985-present). The RMBCA and the corporation acts of several states (including Delaware) are set out in SELECTED CORPORATION AND OTHER BUSINESS ASSOCIATIONS: STATUTES, RULES AND FORMS, *supra* note 3. Professor Hamilton, author of the Nutshell on corporations, *supra* note 1, was the reporter for the RMBCA.

<sup>36</sup> See William L. Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663 (1974). But see Daniel R. Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware Corporation Law*, 76 NW. L. REV. 913 (1982).

<sup>37</sup> Delaware's incentive to provide a hospitable environment for corporations is at least in part financial. Currently, 20% of Delaware's state budget comes from fees charged to corporations incorporated there, thereby allowing the state to abolish its sales tax and to lower its residents' income tax.

have relatively few shareholders. Often shareholders will be close business associates or family members. Most often, the shareholders have managed the business from its inception and do not want outside investors involved in the business. There is no market for shares of a close corporation. Moreover, shareholders often agree to restrict transfers of their stock to any outside investors to ensure that the corporation continues to run as the original shareholders want.

The shareholders in close corporations are usually directly involved in the management and daily operations of the business and generally serve as directors and officers. Because of this direct shareholder involvement in the business, close corporations sometimes resemble sole proprietorships or partnerships. In fact, closely-held corporations are often businesses that were once sole proprietorships or partnerships, but have since incorporated to obtain benefits offered by the corporate form, such as limited liability or advantageous treatment of corporate retirement pension plans. Most close corporations are small businesses, but there are some large ones that rival the size of some of the publicly traded corporations. Whatever their size, though, close corporations must still comply with the same state statutory requirements as publicly held corporations. Thus, even though the shareholders and officers may be the same people, the corporation must elect directors, appoint officers, conduct board and stockholders' meetings, and comply with other statutory requirements.<sup>38</sup> Many states have passed special close corporation statutes that attempt to deal with some of the unique features of the close corporation. For example, the shareholders may be able to manage the corporation without having a board of directors. The goal of these statutes is to allow for internal flexibility within the close corporation, much like that in a partnership.<sup>39</sup>

### c. Formation of the Corporation

Despite variations in law from state to state, the basic rules for formation are substantially the same everywhere.<sup>40</sup> The first step is to file "articles of incorporation" with the appropriate state official and to pay a fee. Exactly what these papers must contain varies among the states, but at a minimum they must include the name of the corporation, the number of shares the corporation is authorized to issue, the address of the corporation's registered office in the state, and the incorporators' names and signatures. When these papers are in the proper form, a state official will issue a certificate of incorporation, and the corporation comes into legal existence.<sup>41</sup>

After obtaining a certificate of incorporation, the incorporators must adopt the corporation's bylaws. The bylaws are a set of rules that govern the internal affairs of the corporation. However, rules contained in the articles of incorporation control over contrary bylaws. The articles of incorporation are a matter of public record, whereas the bylaws are not accessible to the general public for inspection.

### d. Business Reasons for Choosing to Incorporate

For many large businesses, the corporate form is the most efficient way to carry on the business. Many small partnerships and sole proprietorships, however, will consider incorporation when they wish to expand their businesses. For these businesses, it is often said that the best advice on whether to incorporate is "when in doubt, don't." It is useful to review some of the advantages and disadvantages of incorporation now before getting into some of the details of corporate operation.

**Limited Liability** The first advantage of incorporation is the limited liability the corporate form provides for all of its shareholders. If a corporation has 1,000 shares of stock and a shareholder owns 250 shares, that shareholder has a 25% ownership interest in the corporation. Shareholders stand to lose no more than the amount represented by the value of their shares, regardless of the corporation's outstanding debts. Such

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<sup>38</sup> See discussion of powers and duties of board of directors *infra* pp. 565-567.

<sup>39</sup> See generally HENN & ALEXANDER, *supra* note 1, §§257-290.

<sup>40</sup> *Id.*, §§116-133.

<sup>41</sup> States enacted general incorporation statutes starting in the early 1800s in response to the growth in business activity at that time. Before then, corporations generally could only be created by action of the legislature and then only for limited public or semi-public purposes (such as to build a toll road or canal). See HENN & ALEXANDER, *supra* note 1, §12.

limited liability allows corporations to raise capital easily since purchasers of shares can own part of a business without incurring its liabilities.<sup>42</sup> While limited partners in an LP also enjoy limited liability, LPs are required to have at least one general partner who remains personally liable for all the partnership debts.

But limited liability is not always as important as it might seem. Liability insurance can often be purchased to cover all but the most unusual losses. Or liability exposure may not be a major worry in a given business. Moreover, banks and other creditors lending money to new and often undercapitalized corporations often insist that shareholders give *personal* guarantees for loans to the corporation. Obtaining loans is often a more efficient method of raising capital than selling shares, since it is often difficult to attract investors in the rather limited market for shares in most small corporations.

*Perpetual Existence* A second reason for choosing to incorporate is the advantage of the perpetual existence of the corporation. A partnership can dissolve at the insistence of any partner and, absent contrary agreement, the withdrawing partner can insist on payment to each partner of the appropriate share of the enterprise.<sup>43</sup> A shareholder in a corporation generally cannot unilaterally dissolve the entity and withdraw his investment. Yet, a partnership may be almost as durable as many corporations. While the partnership's *legal* continuity is disrupted by various occurrences, its *economic* continuity generally is not. In most cases, as noted earlier, the business continues unchanged while the partnership is reformed.

*Ease of Transfer of Shares* A third advantage of incorporation is the fact that the ownership interests represented by shares of stock in a corporation can be easily transferred with no effect on the corporation. If a shareholder dies, the shares pass to the estate and then to heirs. If a shareholder wishes to sell to a new investor, this transaction will not affect the corporation. But, while easy transfer is true of publicly-traded companies, small businesses often restrict transfers of shares to maintain control and commonly have the right to buy back shares of deceased or withdrawing shareholders.

*Centralized Structure* Another reason often given for incorporating is that the corporation is more centrally governed since management power is vested in directors and officers. In a partnership, all general partners usually participate in management decisions. But this is only a default position. Partnership agreements can provide for centralized control in managing partners.

*Tax Treatment* A major consideration in choice of the corporate form is tax treatment of corporate earnings.<sup>44</sup> Consistent with their separate legal existence, corporations must pay their own federal income taxes. Corporate earnings then are effectively subject to a double tax: earnings are taxed once through *corporate* income taxation and then taxed again through *individual* income taxation when the corporation distributes part of those earnings to its shareholders by way of dividends.

But the double taxation problem is not as serious as it might seem for many corporations. In most cases, a closely-held corporation can avoid double taxation. If it is an independent domestic and domestically-owned corporation with no more than 75 shareholders and only one class of stock, it may qualify for special tax treatment as an "S corporation" under the Internal Revenue Code (IRC).<sup>45</sup> Such corporations may opt to have corporate income taxed directly to the shareholders. This "pass-through" or "conduit" form of taxation operates much like taxation of partners in a partnership.

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<sup>42</sup> See discussion of corporate financing and structure *infra* pp. 562-563.

<sup>43</sup> UPA §§31(1)(b), 38(1).

<sup>44</sup> See generally Chapter XVI and DOUGLAS KAHN & JEFFREY LEHMAN, HORNBOOK ON CORPORATE INCOME TAXATION, 4TH ED. (West 1994). Excellent concise guides to federal income tax law are MARVIN CHIRELSTEIN, FEDERAL INCOME TAXATION, 8TH ED. (Foundation 1997), HOWARD E. ABRAMS & RICHARD L. DOERNBERG, FEDERAL CORPORATE TAXATION (Foundation 1998); JOSEPH BANKMAN, THOMAS D. GRIFFITH & KATHERINE PRATT, FEDERAL INCOME TAX: EXAMPLES AND EXPLANATIONS, 2D ED. (Aspen 1999).

<sup>45</sup> 26 U.S.C.A. §§1361 *et seq.* "S Corporation" comes from subchapter S of Chapter 1 of subtitle A of title 26 of the United States Code where these requirements are found. Changes in 1996 raised the number of stockholders from 35 to 75, allowed S corporations to own subsidiary corporations under certain circumstances and have them treated as S corporations, and permitted non-profit S corporations.

Corporations not covered by the exception just explained are called “C corporations.”<sup>46</sup> In many relatively small C corporations, shareholders are also employees or creditors of the corporation. Such C corporations may be able to obtain “pass-through” tax advantages similar to an S corporation. The C corporation could make distributions of corporate income by way of payments of reasonable salaries or interest on loans to shareholder-employees or shareholder-creditors. Such “non-dividend” distributions are deductible from corporate earnings. If the C corporation is able to thus “zero-out” its earnings, corporate income ends up being taxed only once — when it is received by the shareholder-employees and shareholder-creditors — just as in the case of partnership or subchapter S distributions.<sup>47</sup>

Whatever the benefits of incorporation, they come at the price of increased complexity. There is much more paperwork and formal requirements must be observed. Annual reports must be filed and shareholder meetings held and a host of other additional work done (including preparation of separate tax returns) that is not involved when the business is a partnership. And one must add to this the lawyers’ and accountants’ fees in dealing with these complexities. An additional aspect of the various corporate filing formalities is that the filings become public record, thus making the corporate form a less private way of doing business. Not surprisingly, small businesses that have recently incorporated have a natural tendency to continue the business in the same informal way they did when it was a sole proprietorship or partnership. But the consequences of failure to follow essential corporate formalities can be serious because such failures might allow a creditor to disregard the corporate form and reach shareholders’ or officers’ personal assets.<sup>48</sup>

#### e. Corporate Finance and Ownership

Corporations raise capital primarily by issuing “securities.” Securities are evidence of the obligation to pay money or of the right to participate in earnings. Most corporations issue two types of securities to investors: (1) equity securities or shares of stock (already encountered) and (2) debt securities or bonds.<sup>49</sup>

*Stocks* As mentioned earlier, shares of stock represent ownership interests in the corporation. In public corporations, shares are generally freely transferable, meaning that shares can be bought and sold by investors without the consent of the corporation and without affecting corporate operations. Similarly, the death of a shareholder matters little to the corporation, as the shareholder’s heirs become the new owners.<sup>50</sup> The purchasers of stock do not actually “own” the assets of the corporation. All of the business’ assets are owned by the corporation itself. Instead, shareholders are granted certain rights, depending upon the type of stock owned, as outlined below.

Corporate shares are usually divided into two categories, “common stock” and “preferred stock.” Common stock is the most basic type of stock and must be issued by every corporation. It confers upon its holders two fundamental rights: (1) the right to vote for the directors of the corporation and on other matters requiring stockholder approval, such as a merger, and (2) the right to the net assets of the corporation upon dissolution of the corporation. Dividends are discretionary payments made by the corporation to the stockholders out of the earnings of the business. Dividends are declared by the board of directors and are usually paid on a quarterly basis. The receipt of dividends is one way for stockholders to earn a profit on their investment in the corporation. However, the board of directors is not required to declare a dividend, and shareholders have no inherent right to the payment of dividends. The other way they profit is by the increase in the market value of their shares. But there is no guarantee that the stock will increase in value. Its value will depend on the profitability of the business.

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<sup>46</sup> 26 U.S.C.A. §301 *et seq.* Subchapter C of the IRC governs corporate taxation in general.

<sup>47</sup> Yet, this device may be difficult to use where some C corporation shareholders are not employees and the amount that needs to be distributed in this way is so large that payment in salary or bonuses may violate IRC limits on the reasonableness of compensation for employees that can be deducted.

<sup>48</sup> See discussion *infra* p. 567.

<sup>49</sup> See generally HENN & ALEXANDER, *supra* note 2, §§154-161.

<sup>50</sup> As noted earlier in the discussion of closely held corporations, the articles of incorporation may restrict the transferability of shares to assure that control of the business is not lost.

Shares of preferred stock also represent an ownership interest in the corporation. However, the owners of preferred stock are entitled to certain rights and privileges that are superior to those of common stock owners. The most common feature of preferred shares is a dividend preference over common stock. This preference does not guarantee the payment of a dividend, but it does guarantee that any dividends declared by the board will be paid first to the preferred stock owners. Preferred stock holders also are given priority over common stockholders in the event of a liquidation of the corporation, though neither class of shareholders can be paid before the corporation's creditors, including bondholders, discussed next.

**Bonds** In addition to equity securities, most corporations also issue debt securities, or bonds, which represent the borrowing of money. In other words, instead of purchasing an ownership interest in the corporation, the bondholder is making a loan to the corporation. The bond represents an unconditional guarantee by the corporation to pay the bond holder a specific amount on a certain date. In addition, the bondholder is generally entitled to periodic interest payments. For example, the ABC Corporation might issue a \$1,000 ten-year bond, paying 6% interest. To obtain this bond, the purchaser will pay the corporation \$1,000. In return, the corporation agrees to repay the purchaser the \$1,000 in ten years. During the ten-year period, the corporation agrees to pay the bondholder annually 6% of the face value of the note, or \$60 a year. Unlike shareholders, bondholders are not entitled to voting rights, nor do they receive dividends. Instead, a debtor-creditor relationship is established between the corporation and the bondholder.

#### f. Organizational Structure and Powers

Ownership and management of a corporation consists of three tiers: (1) shareholders, (2) directors, and (3) officers. Directors and officers, and occasionally controlling shareholders, comprise the management. Each group has defined powers within the enterprise.

**Shareholders' Rights and Duties** Shareholders' rights are established in the articles, bylaws and the state's general incorporation law. Shareholders have either the absolute or qualified right to inspect the corporate books and records for proper purposes, such as to become informed of corporate affairs.<sup>51</sup> Shareholders do not actually run the business, nor do they have the power to act individually on behalf of the corporation. Instead, their powers must be exercised collectively along with the other shareholders by way of voting, usually at the stockholders' meeting. Most states require a yearly stockholders' meeting with advance written notice.

Each shareholder is entitled to one vote per share of common stock owned. Shareholders do not have to be present at the stockholders' meeting to vote. Through the use of a document called a "proxy," shareholders can appoint someone else to cast their vote on a specific subject. Because of the large number of shareholders in most publicly held corporations and the impracticability of attending shareholders' meetings, voting by proxy is common.

Through their voting powers, shareholders have control over the corporation in three primary ways: (1) they can elect or remove the directors;<sup>52</sup> (2) they can amend the articles of incorporation or bylaws; and (3) they have the right to approve or disapprove extraordinary changes to the corporation, such as a merger with another corporation.<sup>53</sup>

The obligations of shareholders are few. Because of the principle of limited liability, shareholders are not responsible for any of the corporation's debts or other actions, with the extraordinary exception of

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<sup>51</sup> An improper purpose would be to learn business secrets, to aid a competitor of the corporation, or to secure prospects for personal business.

<sup>52</sup> Directors usually serve their full term. If the shareholders are unhappy with a director's performance, the director is simply not reelected. However, the shareholders have the power to remove a director from office *for cause* and some laws expressly provide that shareholders can vote by majority to remove a director at any time *without cause*. See RMBCA, *supra* note 35, §8.08(a).

<sup>53</sup> See *infra* p. 569.

“piercing the corporate veil” discussed below.<sup>54</sup> If the corporation fails, its shareholders lose only their investments.<sup>55</sup>

*Shareholder Rights in Publicly Traded Corporations* In large publicly traded corporations, the governance powers of shareholders is virtually nonexistent. Shareholder proxies are delivered to the corporate managers, who elect directors that often reappoint the incumbent managers. Most shareholders do not choose to exert any control over corporate managers. First, they usually view themselves as passive investors, not owners. Second, they often doubt whether they can improve corporate performance by intervening or controlling the choice of managers. Third, even if they did want to be more active, a great deal of time, money and energy is needed to inform themselves about corporate matters and to persuade and solicit proxies from other shareholders.<sup>56</sup> Consequently, when shareholder meeting announcements are sent out, along with management proxy forms requesting shareholders to vote their shares as it has recommended, most shareholders simply vote with by proxy in favor of the management or throw the entire announcement away.

If shareholders wish to become active in exerting control over corporate actions, however, federal law is of some assistance. Section 14 of the Securities Exchange Act and regulations thereunder regulate the procedures by which proxies are obtained from shareholders of publicly traded corporations.<sup>57</sup> In addition to prohibiting fraud and misrepresentation in management communications to shareholders, the Act and regulations require that an annual report be sent that conforms to particular specifications. The content of proxy statements is regulated. Management is required to include in any proxy statement certain shareholder proposals and supporting statements, and to afford shareholders the opportunity to vote for or against management or shareholder proposals in the management proxy. Section 14 has been viewed as embodying a policy of “corporate democracy” and a desire to prevent management from treating corporations as their own personal property.<sup>58</sup>

*Directors* Directors are responsible for the management of the corporation and for creating corporate policy. The initial directors are usually named in the articles of incorporation or elected by the incorporators, and serve until the first annual shareholder meeting or until their successors are elected and qualified. Thereafter, directors are elected by majority vote of the shareholders and usually serve a term of one year.<sup>59</sup> The number of directors of a corporation varies; some states require at least three, while others require only one.

Directors meet regularly at board meetings to conduct the corporation’s business. Directors do not have the power to act individually for the corporation; they can act only as an entire board. Thus, unlike employees, whose acts in the name of the corporation bind it, directors can bind the corporation only by actions approved by an affirmative vote of the board. They have the responsibility for all major policy-making decisions necessary for the management of all corporate affairs: declaring and paying corporate dividends to shareholders, authorizing major corporate policy and appointing, supervising, and removing officers and employees; and making financial decisions.

Directors, as persons in control of the property of others, are “fiduciaries” who have duties to both shareholders and the corporation. The directors’ fiduciary duties include the duty of care and the duty of loyalty. The duty of care entails being honest and using prudent business judgment when conducting corporate affairs. Directors must exercise the degree of care that a reasonably prudent person would use

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<sup>54</sup> See *infra* pp. 567-568.

<sup>55</sup> See generally HENN & ALEXANDER, *supra* note 2, §§199-203.

<sup>56</sup> A proxy is a document executed by shareholders appointing someone else to vote their shares for them.

<sup>57</sup> 15 U.S.C.A. §78n.

<sup>58</sup> *Medical Committee for Human Rights v. Securities & Exchange Comm.*, 432 F.2d 659 (D.C. Cir. 1970), *vacated as moot*, 404 U.S. 403 (1972).

<sup>59</sup> Directors usually serve from annual meeting to annual meeting, but longer or staggered terms are permissible under most state statutes.

when conducting personal business affairs, including the duty to become informed about corporate affairs.<sup>60</sup> The duty of loyalty prevents directors from, among other things, using corporate funds or confidential corporate information for their personal advantage, competing with the corporation, usurping a corporate opportunity, engaging in insider trading, or selling control over the corporation.<sup>61</sup> A director who breaches either the duty of care or the duty of loyalty may be held answerable to the corporation and to the shareholders.

**Officers** The corporate officers are responsible for the day-to-day operation of the corporation. They are most often selected and removed by the board of directors. Traditional titles include “chief executive officer,” “president,” “vice-president,” “treasurer,” and “secretary.” The officers carry out the board’s decisions and conduct the day-to-day operations of the business. The tenure of the officers is generally pursuant to a contract, though it may also be at the board’s discretion.

Officers are viewed as having the same fiduciary duty of care and loyalty to the corporation and its shareholders as directors do when conducting business affairs, as well as the same obligations concerning corporate opportunities and conflicts of interest.<sup>62</sup> Like directors, officers purporting to contract on behalf of the corporation without the authority to do so may be personally liable on the contract or to the corporation. Even authorized officers may be liable on contracts if they do not advise that they are contracting as an agent of the corporation.

**Shareholder Lawsuits** Many of the above duties of the management of the corporation can form the basis for a shareholder suit for breach of duty. Shareholders may file either a “direct” or a “derivative” shareholder suit. A common example of a direct shareholder suit is a suit to compel the management to declare and pay a dividend.<sup>63</sup> It is “direct” because it enforces a duty owed directly to shareholders.

A shareholder “derivative” suit is one to enforce a duty owed to the *corporation*. Shareholders in such a suit are suing *on behalf of* the injured corporation. In cases where the wrongdoing of officers or directors has injured the corporation itself, the *corporation* has a right to sue its own officers or directors. However, since those very officers or directors control the corporation, they will probably decide that it is “not in the best interests of the corporation” for it to sue them. A derivative shareholder’s suit remedies this problem by allowing the shareholders to “step into the shoes” of the corporation and sue on its behalf. Thus, even one shareholder is able to sue on behalf of the corporation, demanding that the corporation be repaid millions of dollars, even though the individual shareholder’s loss may be nominal or nonexistent. When the derivative suit is successful and benefits the corporation, the plaintiff-shareholder is entitled to be reimbursed by the corporation for reasonable expenses, including attorney fees.<sup>64</sup>

Because shareholders may not have much personally at stake in a derivative suit, legislatures and courts have imposed limitations on such suits to prevent abuse. For instance, the plaintiff in a derivative action must be a shareholder both when suing and at the time of the alleged misconduct. This means that a person cannot buy shares after the alleged misconduct simply for the purpose of bringing a law suit. Also, shareholders wishing to sue must give management the opportunity to take action to remedy the problem by serving them with a formal demand. Finally, if *disinterested* directors have determined that the suit is not

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<sup>60</sup> *Smith v. Van Gorkom*, 488 A.2d 858 (Del. 1985) (rescission of merger allowed in shareholder suit where merger was approved quickly based on a 20-minute presentation by the chairman and without review of merger documents).

<sup>61</sup> See HENN & ALEXANDER, *supra* note 1, §234; see also RMBCA, *supra* note 35, §8.30. See, e.g., *Globe Woolen Co. v. Utica Gas & Electric*, 121 N.E. 378 (N.Y. 1918) (Cardozo, J.) (contract to supply power that grossly favored textile company voided where same person was director and chairman of the executive committee of electric company and chief stockholder and director of textile company).

<sup>62</sup> RMBCA, *supra* note 35, §8.42; HENN & ALEXANDER, *supra* note 1, at §§219-243.

<sup>63</sup> See HENN & ALEXANDER, *supra* note 1, §360. See, e.g., *Godley v. Crandell & Godley Co.*, 105 N.E. 818 (N.Y. 1914) (suit over payment of dividends).

<sup>64</sup> See generally HENN & ALEXANDER, *supra* note 1, §§361-367.

in the best interests of the corporation, the court may dismiss the action.<sup>65</sup>

*Business Judgment Rule* If shareholders sue the directors or officers of a corporation, those directors and officers are entitled to the benefit of the “business judgment rule.”<sup>66</sup> The business judgment rule is a “presumption that in making a business decision the directors of a corporation acted on an informed basis, in good faith and in the honest belief that the action taken was in the best interests of the company.”<sup>67</sup> A hallmark of the business judgment rule is that a court will not substitute its judgment for that of the board if the latter’s decision can be “attributed to any rational business purpose.”<sup>68</sup> This rule allows for honest mistakes and reasonably poor business decisions. However, if the directors permit the corporation to violate the law, the business judgment rule does not apply.<sup>69</sup> On the other hand, directors in a large corporation who are effectively relegated to making broad policy decisions are not required to monitor employees closely to discover illegality absent some cause for suspicion.<sup>70</sup>

#### g. “Piercing the Corporate Veil”

The separate legal existence of the corporation and the limited liability it affords shareholders serve important social and economic purposes. However, there are instances where courts may ignore the corporate structure and its protections for compelling reasons of public policy. This is called “piercing the corporate veil.” The conditions under which the law permits it to be done vary considerably from state to state.<sup>71</sup> Whatever test is used, it is easy to exaggerate the importance of veil-piercing. Only when stockholders of officers are using the corporate structure to perpetuate a fraud, to evade the law or to escape obligations will “piercing” generally be successful. And when piercing is used, the corporation involved is almost always a closely-held one.

*Formalistic Approach* Under one approach, identified with New York, courts will disregard the corporate structure only when there has been noncompliance with the corporate formalities, such as failing to complete the incorporation process or to hold directors’ meetings, or where shareholders treat corporate property as their own.<sup>72</sup> This is a rather permissive test. But even so, the conservative “formalistic” approach can trap shareholders and officers of close corporations run by friends or family members, who run the business on an informal basis, ignoring corporate formalities and routinely mixing corporate and personal assets.

*Undercapitalization Approach* Other states have given less weight to legal formalities and emphasize “undercapitalization” — where the assets of the company are “trifling compared with the business to be done and the risks of loss.”<sup>73</sup> But even under this test, Courts are often unwilling to disregard the protections of the corporate shell when the creditor is a *business creditor* (such as a bank). The reason is that the business creditor voluntarily enters into the relationship with the company, can investigate the company’s ability to

<sup>65</sup> See HENN & ALEXANDER, *supra* note 1, §362. See also Federal Rule of Civil Procedure 23.1 (requiring a verified complaint and specific pleading).

<sup>66</sup> See generally, CLARK, *supra* note 1, §3.4.

<sup>67</sup> *Aronson v. Lewis*, 473 A.2d 805, 812 (Del. 1984).

<sup>68</sup> *Sinclair Oil Corp. v. Levien*, 280 A.2d 717, 720 (Del. 1971). See *Schlensky v. Wrigley*, 237 N.E.2d 776 (Ill.App. 1968) (rejecting challenge to management decision not to install lights at baseball field to permit games to be played at night); *Herald Co. v. Seawell*, 472 F.2d 1081 (10th Cir. 1972) (rejecting challenge to purchase by corporation of its own shares for use in employee trust plan).

<sup>69</sup> *Miller v. American Telephone & Telegraph Co.*, 507 F.2d 759 (3d Cir. 1974) (shareholder suit allowed to contest corporation’s failure to collect \$1.5 million debt owed by political party, a violation of federal election laws).

<sup>70</sup> *Graham v. Allis-Chalmers Manufacturing Co.*, 188 A.2d 125 (Del. 1963) (directors not liable for damage to corporation caused by criminal price-fixing activities of middle-level executive employees).

<sup>71</sup> See HENN & ALEXANDER, *supra* note 1, §146.

<sup>72</sup> See *Walkovsky v. Carlton*, 223 N.E.2d 6 (N.Y. 1966) (refusing to disregard corporate form where separate corporations were set up for one or two taxis in a fleet, thus protecting shareholders-owners of fleet from tort liability).

<sup>73</sup> See *Minton v. Cavaney*, 364 P.2d 473, 15 Cal. Rptr. 641 (Cal. 1961) (dictum). In this case, there was also evidence that many of the basic corporate formalities had not been followed, including the serious omission of failing to complete the formation of the corporation.

pay beforehand and require additional security as needed. Most situations where the veil is pierced are where the creditors are injured tort victims.<sup>74</sup>

*“Dummy” Corporations* Often the shareholder of a company whose corporate form is sought to be disregarded is another corporation and the creditor seeks to reach the assets of the “parent” or owner corporation. If the subsidiary is treated as a “dummy” and controlled in every way by the parent corporation, the subsidiary’s corporate form can be disregarded to reach the assets of the parent. This will be particularly so if the subsidiary is used to carry on particularly risky functions of a business.<sup>75</sup>

In theory, the piercing doctrine applies to publicly held as well as closely held corporations. However, research reveals no case in which the *shareholders* of a corporation whose stock was publicly traded or widely held were found personally liable for the obligations of the corporation. Instead, when courts pierce the corporate veil of a publicly traded corporation, liability is usually imposed on the individuals who *managed* the enterprise, on a parent corporation that gave orders, or on a group of corporations that were operating as an economic unit.<sup>76</sup>

*Choice of Law in Veil-Piercing* “Internal affairs” of the corporation are usually governed by the law of the state of *incorporation*. However, some courts resolve issues of veil-piercing according to the law of the state where the corporation *operates*.<sup>77</sup> This is especially so if the state of incorporation is one of convenience. Also, there is a growing *federal* common law of veil-piercing. For example, federal environmental laws impose environmental cleanup obligations on “owners” and “operators.” The Supreme Court has rejected the view that this includes shareholders and any parent corporation that were heavily involved in the operations of the company that caused the contamination. However, it instructed lower courts to determine “whether, in degree and detail, actions directed to the facility by an agent of the parent alone are eccentric under accepted norms of parental oversight of a subsidiary’s facility.”<sup>78</sup>

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<sup>74</sup> See *Consumer’s Coop v. Olsen*, 419 N.W.2d 211 (Wis. 1988) (declining to disregard limited liability for business creditor). But see *Victoria Elevator Co. v. Meriden Grain Co.*, 283 N.W.2d 509 (Minn. 1979) (holding major shareholder liable where wide variety of wrongful acts occurred).

<sup>75</sup> But see *Craig v. Lake Asbestos of Quebec*, 843 F.2d 145 (3d Cir. 1988) (applying New Jersey law, declining to hold parent liable in tort case where asbestos production had been transferred to wholly-owned overseas corporation for lack of complete “alter ego” control). *Craig* contains a good discussion of controlling authorities.

<sup>76</sup> David Barber, *Piercing the Corporate Veil*, 17 WILLAMETTE L. REV. 371, 372 (1981).

<sup>77</sup> This is consistent with the general notion that the state of operation has the greater contacts and interest in the issue. See Chapter VII, pp. 260-263.

<sup>78</sup> *United States v. Bestfoods*, 524 U.S. 51 (1998). See generally KATHRYN R. HEIDT, ENVIRONMENTAL OBLIGATIONS IN BANKRUPTCY ¶10.04 (West Group 1993-1998). See also *Anderson v. Abbott*, 321 U.S. 349 (1944) (bank holding company).