

ESSAY QUESTION NO. 9

Answer this question in booklet No. 9

Resources Inc. is an Alaska corporation with 150 shares of stock issued at formation that were registered under the Alaska Securities Act. The corporation owns 15 square miles of land, including all mineral rights, and operates a coal mine on the land. Cutting through the property is a highly prized recreational river used by fishermen and boaters. The Corporation recently received an offer from a nature conservancy group to purchase all of the corporation's property within 2 miles of both sides of the river for \$3 million. The directors of the corporation favor the sale, as it will not interfere with their mining operation and the property represents a small fraction of the corporation's assets. However, under the articles of incorporation, they must obtain approval from the shareholders for the sale of real property. There are 150 shareholders of record. George, a shareholder, wants the proceeds from the sale distributed to all shareholders as a one-time dividend.

Both the sale of the property and the dividend proposal are properly noticed for a vote at a special shareholders meeting to be held in October. The directors state in a letter to shareholders that the proceeds from the sale are needed to upgrade the environmental systems of the coal mining operation, made necessary by a recent EPA order. Prior to the October meeting, George sends letters to all of the corporations' shareholders soliciting their proxies to vote on the sale and dividend proposals. George states in his letter that he intends to vote in favor of the sale and the dividend declaration. George goes on to state that there is no EPA order requiring any upgrades of the coal plant and that the directors instead plan to keep the money to purchase a corporate jet.

1. Assume that George's statements are false. Has George violated an Alaska statute? Discuss.
2. Assume that only 100 of the 150 shareholders of record participate in the shareholder meeting, and they show up in person and vote their own shares. Analyze whether there is a quorum and explain how many shareholders must vote in favor of the real estate sale in order for the sale to be authorized. Would your analysis change if only 10 shareholders attend the shareholder meeting in person, and one of the shareholders holds the proxies for 90 other shareholders who are not physically present?
3. For the purpose of this question only, assume that the 150 shares are owned by 3 shareholders, each holding 50 shares, and that four people are running for election to 3 director positions. If Mary, one of the three shareholders, wanted to make sure that a specific candidate were elected

to one of the three director positions, describe how Mary should vote her shares. Assume that there are no provisions in the articles of incorporation that would restrict Mary's options.

GRADERS' GUIDE

*** QUESTION NO. 9 ***

SUBJECT: BUSINESS LAW

Question (1): Assume that George's statements are false. Has George violated an Alaska statute? Discuss. (35 points)

Yes, George has violated an Alaska statute relating to corporate securities. Pursuant to AS 45.55.160, it is unlawful to make an untrue statement of a material fact in connection with soliciting a shareholder's proxy. Meidinger v. Koniag, Inc. 31 P.3d 77, 82 (Alaska 2001). In Brown v. Ward, 593 P.2d 247, 250 (Alaska 1979), the Alaska Supreme Court stated that a misrepresentation contained in a proxy statement was material if there was a substantial likelihood that a reasonable shareholder would consider it important in deciding how to vote. The test is an objective one and not dependent upon proof that specific shareholders were in fact induced to give their proxy because of the misrepresentation. Id. The directors should be able to establish that George's statements were untrue and that they were material, because a reasonable shareholder would have been influenced to provide George with his or her proxy instead of the directors as a result of the misrepresentation. Statements suggesting that directors are lying to the shareholders and seeking to use resources in a wasteful fashion would be considered highly relevant to voting shareholders. Meidinger at 83 (Supreme Court held that "the misrepresentations were so obviously important to an investor, that reasonable minds cannot differ on the question of materiality", and affirmed superior court's grant of summary judgment.)

Question (2): Assume that only 100 of the 150 shareholders of record participate in the shareholder meeting, and they show up in person and vote their own shares. Analyze whether there is a quorum and explain how many shareholders must vote in favor of the real estate sale in order for the sale to be authorized. Would your analysis change if only 10 shareholders attend the shareholder meeting in person, and one of the shareholders holds the proxies for 90 other shareholders who are not physically present? (35 points)

The facts state that "under the articles of incorporation, they must obtain approval from the shareholders for sale of real property." The facts do not suggest that the quorum level was set at any specific level by the articles of incorporation. AS 10.06.415 states that unless the articles of incorporation provide otherwise, "a majority of the shares entitled to vote, represented in person or by proxy, constitutes a quorum at a meeting of shareholders."

Thus, 100 shareholders present at the meeting constitute a majority of 150, and there is a quorum of shareholders at the meeting for purposes of voting on the issue of the real estate sale.

AS 10.06.415 provides that if a quorum is present, “the affirmative vote of the majority of shares represented at the meeting and entitled to vote on the subject matter is the act of the shareholders, unless the vote of a greater number ...is required by this chapter, the articles of incorporation or the bylaws.” Absent any statement in the facts that the voting level has been altered from the statutory presumption of majority vote, the real estate sale would need to be approved by 51 of the 100 shareholders present in order to be valid.

Under the scenario where one shareholder holds 90 valid proxies, the analysis of the quorum and the voting level required would be the same. For shareholders to count toward a quorum, they can either be physically present or present by proxy. AS 10.06.415(a). Thus, there are still a majority of the shareholders present (100 shareholders out of 150) and therefore, a quorum. The number of votes approving the sale of the real estate would still be 51, regardless of whether the votes were in person or by proxy.

The facts indicate that “the property represents a small fraction of the corporation’s assets.” This was put into the question to avoid any discussion of the special rule contained in AS 10.06.568 which provides for special shareholder voting procedures when there is a proposed sale of “all or substantially all of the property and assets” of the corporation. The facts of the question should also obviate the need for any discussion under AS 10.06.358 which prohibits a distribution that exceeds the corporation’s retained earnings.

Question 3: For purposes of this question only, assume that the 150 shares are owned by 3 shareholders, each holding 50 shares, and that four people are running for election to 3 director positions. If Mary, one of the three shareholders, wanted to make sure that a specific candidate were elected to one of the three director positions, describe how Mary should vote her shares. Assume that there are no provisions in the articles of incorporation that would restrict Mary’s options. (30 points)

Mary would use the cumulative voting process. Pursuant to AS 10.06.420(d), unless the articles of incorporation provide otherwise, a shareholder may cumulate his or her votes and give a candidate all or a portion of the votes equal to the number of shares owned, multiplied by the number of directors seats that are being filled. Thus, Mary could insure the election of her specific candidate by casting all of her 150 votes (50 shares times 3 director seats) for her candidate. If Mary were good at math she might consider influencing the outcome of the other two director positions by casting at least 113 votes for her candidate and spreading her remaining 37 votes among the other candidates.

No points to be given, but for your information, the formula for ensuring that cumulative voting will control the election of a particular seat is: # of total votes (shares x seats) divided by the number of director seats plus 1, and then add 1. So in this case, the math is 150 shares x 3 seats which equals 450, divided by 4 (3 director seats plus 1) which equals 112.5, and then adding 1, which equals 113.5 or 113, since there are no fractional votes.

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1. George does have obligation to the company since he is a shareholder if he is not an officer or on board of directors he is entitled to his own opinion. George has a duty to bring forth a legitimate issue but he doesn't have the right to start and spread lies. But his duty is less as a shareholder. The officers and board members must act in accordance with telling the truth and working for the best interests of the company. No statute violation

2. At 100 there is 2/3 of the stockholders voting but it depends of if this is also 2/3 of the stock. Look at the articles filed with the state and bylaws of the corp. If articles are silent then default is that every share hold counts the same. So two thirds are there and vote can be taken. Because this is for sale of corporation land that shareholders must be given opportunity to be involved. There is quorum present but you have to have 60% majority vote to let land be sold. So 60 out of 100 must vote to sell the land.

Assuming that only 10 show up but one has proxy for another 90 shareholders the vote can't be held. Statute says that majority of shareholders must be there and while proxies give person signed to the right to vote their shares as he sees fit there are certain things that can't be done by proxy and selling land is part of it. Must have majority. Otherwise it would not matter what the others and the meeting wanted. If one had 90 other proxies they could do anything and no one else could have a say.

3. Mary can vote her shares as one block for a single candidate. There are only 100 other shares so to defeat any of Mary choices 51 would have to voted on a specific candidate to defeat Mary choice. So of the 100 the other started with and subtract 51 to secure the first

seat. Now there is only 49 votes left and you have 3 seats and only 4 running. If Mary votes as a block she will seat one of her choices. Other shareholder override on 1 pick for 51 votes. then no matter how they vote Mary will get to pick the next one and if block vote then other will get to pick the third seat.

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1. George's Statement

Majority shareholders of a corporation owe a fiduciary duty to minority shareholders. One could argue that George, in effect, becomes a majority shareholder by procuring proxies and therefore owes a fiduciary duty to the other shareholders. His material and intentional misstatement breaches this fiduciary duty because he is not acting in the best interest of the minority shareholders by trying to force an improper distribution. George was in possession of a letter that said the proceeds of the sale are needed to upgrade the environmental systems of the coalmining operation pursuant to an EPA order.

Furthermore, this misstatement could render his procurement of the proxies as void because he did not provide sufficient information for the other shareholders to consent to his proxy request. However, the problem with this argument is that the directors sent the letter to shareholders, which means that the shareholders could have had adequate knowledge of the EPA order and therefore gave knowing consent to George to vote anyway.

2. Quorum/ Voting

At a properly noticed meeting, quorum is met when the majority of outstanding shareholders are present. In this case, there are 150 shareholders of record and 100 are present, thereby representing a quorum.

In order to determine how many shareholders must vote for the real estate transaction, the

transaction must be properly characterized. A transaction in the ordinary course of business in a SH meeting can be passed by a vote of the majority of the shareholders present. Therefore, a vote approving the real estate transaction of 51 members would be sufficient. However, if this transaction is considered to be a fundamental corporate change, in that , many of the assets are being sold or the purpose of the corporation is changing, 2/3 of all outstanding shares must vote to approve it. A fundamental corporate change is one that completely changes the purpose of the business, merges a business with another, or sells substantially all of it's assets. Here, Resources Inc noted that the sale will not interfere with their mining operation and only represents a small fraction of the corporation's assets. Therefore, since Resources is able to continue with it's purpose without major interference or a merger, this is likely not a fundamental corporate change requiring 2/3 of the outstanding *shares* to approve the project.

Proxies

The use of proxies does not affect the quorum analysis as long as the proxies were properly procured. Here, there is a problem with the material misstatement, as noted above. Yet, the issue is whether the shareholders had notice of this misstatement.

HOwever, there may be a problem because the quorum analysis requires that a majority of shareholders be present, here, while a majority of the *shares* are presenet, the majority of shareholders are not.

3. Mary's Vote

A default requirement in Alaska Corporations is that shareholders are entitled to cumulative voting. Cumulative voting is where one shareholder can apply all of their votes (according to the number of shares they own) to one director position. There has been no change to this statutory default rule to cumulative voting rights for Mary. Therefore, Mary would apply all 50 of her shares to one position rather than among all three positions. This would ensure that person to be seated as a director because the remaining 100 shares would have to be split among 3 candidates. Therefore, the three other candidates would not all be able to receive more votes than Mary's candidate.

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Statements of Shareholders

In a non-closed corporation, a shareholder who is not also an officer or director, owes no fiduciary duties to other shareholders.

His statements, although false, do not violate a statute. There is no evidence of intentional misrepresentation here, and he does not fall within the ~~fiduciary~~ ~~requirements~~ requirements attributed to officers, directors and managing ~~shareholders~~ shareholders under statute. He can raise his concerns with other shareholders.

However, he may not take their proxies and then vote as he likes.

Quorum

A quorum is established when there is a majority of shares present at the meeting. Without a quorum, the meeting cannot happen. Of the quorum, $\frac{2}{3}$ of shareholders votes must be cast in favor of the real estate transfer for it to be valid, as it is a special meeting and a transfer of property.

It is the number of shares and not the number of shareholders who are necessary to establish a quorum.

However, a shareholder's proxy

$\frac{3}{4}$

must be ^(signed and) sent, directly to the Board, and not solicited and carried by one shareholder physically present.

Nevertheless, ten people present can be enough to establish a majority of shares for a quorum, ~~if the shares~~

Cumulative Voting

~~As a shareholder is a~~
As a way to protect the interests of minority shareholders, cumulative voting is preferable when electing members of the Board.

$\frac{4}{4}$

A shareholder may have as many votes as the number of shares she owns, multiplied by the number of directors up for election, ^{or re-election} divided any way she chooses.

Mary, thus, has fifty shares. Since there are three positions to fill, Mary has 150 votes to cast. She should cast all of these votes for one candidate. This would be the best strategy for Mary.

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1.) George has made false statements in connection with proxy solicitation. If George has made these statements knowing that they were false and for the purpose of obtain the proxies of others, he has violated an ~~abold~~ statute. George has a duty to act in good faith and fairly towards his fellow shareholders. The directors are under a duty to exercise their business judgment in the management of the corporation. In their judgment, the money from the sale should be used to benefit the corporation by upgrading the facilities. George's conduct is urging an illegal dividend and the directors and other shareholders may take action to stop George's proxy solicitation based on false representations of fact.

2.) a quorum requires a majority of shareholders. If there are 150 shareholders, 100 would satisfy the quorum requirement. In order to authorize the sale of corporate assets, a $\frac{2}{3}$ majority vote will be required. 100 of the 150 shareholders would have to ^{of all shareholders} vote in favor of the sale.

Accordingly, if 100 shareholders attend the meeting they would all have to vote in favor of the sale.

The analysis would change if only 10 shareholders (one with proxy for 90 others) attended the meeting. There would be ~~no~~ a quorum ~~(99 shareholders represented)~~ but there would

$\frac{2}{2}$

not be a sufficient number of votes to authorize the sale
($\frac{2}{3}$ of all outstanding shares).

3. Cumulative voting will be presumed and is favored.
Here Mary has 50 shares and there are 3 open director positions. Mary will have a total of (50×3) 150 votes to use. She may allocate all 150 votes towards a single director position.

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1. George's Violations

George is only a shareholder to the corp., and not an officer or director. Also, because there are 150 shareholders, it does not appear this would be considered a "closely held" corporation. Absent it being a closely held corp., George does not owe a duty of care or loyalty, or other fiduciary duties to other shareholders.

However, George may not give intentional false statements to other shareholders in order to induce them into giving him their votes by proxy. This is a violation of Alaska law. If the corp. is considered

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to be closely held, George probably breached a fiduciary duty as well.

2. Quorum

In Alaska, a quorum is defined as a majority of the number of shares unless the Articles define it differently. Here, there is no indication that Resources' Articles of Incorporation provide differently. Thus, a quorum would be 76 shareholders.

In voting, a majority of the present shareholders voting must vote in favor of the proposal to sell the real estate. If the sale of real estate was not in the "ordinary course of business," a $\frac{2}{3}$ supermajority

$\frac{3}{5}$

is required, but that does not seem to be the case. Thus, half of the ~~100~~¹⁰⁰ ~~people~~ shareholders present must vote in favor of the proposal, or 51 shareholders.

The next issue is whether a quorum is lost where only 10 shareholders are present, but 100 shares are represented. In Alaska, proxy voting is allowed, and thus, the analysis does not change. As long as at least 76 shares are represented, the vote may go through. Because there are ~~100~~ 100 shares present, the vote may proceed.

$\frac{4}{5}$

3. Mary

Because there are only 3 shareholders, this ~~is~~ is a closely held corporation. In Alaska, cumulative voting is allowed and that is how ~~is~~ Mary should vote her shares. In cumulative voting, ~~the~~ a shareholder can multiply the number of ~~the~~ open seats by her number of shares, and submit that many votes. Because Mary has 50 shares, and there are 3 director positions open, Mary could cast 150 votes for one of the candidates.

The only problem is that cumulative voting is generally designed to protect

5/5

Minority shareholders in ~~closed~~ corporations.

Here, Mary is not a minority shareholder and it is a closely held corporation. Thus, I am not sure if Mary could do cumulative voting in this situation. Assuming she could, that is the method by which she could ensure her candidate is chosen. Because cumulative voting is a default right to shareholders absent any contrary provision in the Articles, it is likely Mary could do this because the facts say the Articles do not preclude her from doing so.