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RECHT BERATUNG WEITERBILDUNG

Introduction to US Business Law 9. Company Law

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Prof. Dr. Andreas Kellerhals

Recent developments

- > Tarifs: Negotiations for a customs agreement underway, Trump communicated that Switzerland will have to pay much more
- > 2nd assassination attempt on Trump
- > Strait of Hormus – open/closed?
- > Trump is obliged under the 1973 War Powers Act to limit the war after 60 days if not congressional approval to continue?
- > Trump asked for removal of Jimmy Kimmel after joke on Melania
- > King Charles in USA

Repetition last time

Tort law

- > State law
- > Harmonization
- > abuse?
- > Great importance of tort law in the US
- > 3 elements: legal duty to care, breach, damage – causation
- > 3 categories: intentional, negligence, strict liability
- > Exemples:
 - > Chocolate bar
 - > Carbolic smoke ball
 - > Donough v. Stevenson
 - > Etc.

Company law

Overview

- > Corporate law (or company law) is basically state law
 - > Interstate commerce clause (Art. 1 sec. 8 USC) – only few federal legislation
 - > Therefore: US corporate law does barely exist
 - > Significant differences between states (competition)
 - > Companies are free to choose domicile
 - > Doing business in that specific state not necessary
 - > Regulatory competition
 - > Dominant state jurisdiction: Delaware
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- **50% of all US companies**

Delaware (1)

- > Why Delaware?
 - > No tax on activities outside the state
 - > Special, experienced courts (Court of Chancery)
 - > no juries
 - > More case law than anywhere else
 - > Long tradition (since 19th century)
 - > Computerized registration system
 - > Confidentiality?
 - > Lax corporation laws
 - > Manager friendly approach
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Delaware (2)

> Delaware

> Internal affairs doctrine

- > For internal matters jurisdiction with state of incorporation

> All offices may be held by a single person who also can be sole shareholder

- > US citizenship/residence not necessary

- > May also operate anonymously

> Other states have followed up

- > Race to the bottom? (Delaware effect)

Easy to create company in Delaware

> <http://www.youtube.com/watch?v=4DVkdt5yVhM&feature=relmfu>

Florida articles of incorporation

> <http://form.sunbiz.org/pdf/cr2e047.pdf>

Delaware code of ethics and company law

> [Court of Chancery](#)

> <http://www.youtube.com/watch?v=6SllwWYi7u4>

Certain harmonisation do exist - model laws

- > Regulatory competition lead to efforts to establish common standards
 - > National Conference of Commissioners on Uniform State Laws – NCCUSL created several model acts which are adopted by most states
 - > Uniform Partnership Act (UPA) 1916
 - > Revised Uniform Partnership Act (RUPA) 1994
 - > Kind of legal harmonisation
 - > But still considerable differences remain
 - > Louisiana declined to adopt the model acts at all
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Relevant legal basis

- > State laws
 - > Model laws
- > Federal law
 - > Limited power
 - > interstate trade
 - > Only a few but important legislations
 - > always after crisis, (f.e. stock exchange, Governance, etc)

Enron case

- > The **Enron scandal** was an accounting scandal sparked by American energy company Enron Corporation filing for bankruptcy after news of widespread internal fraud became public in October 2001, which led to the dissolution of its accounting firm **Arthur Anderson**, previously one of the five largest in the world.
- > The largest bankruptcy reorganization in US history at that time, Enron was cited as the biggest audit failure
- > Shareholders filed a \$40 billion lawsuit
- > SEC began investigations
- > As a consequence of the scandal, new regulations and legislation were enacted to expand the accuracy of financial reporting for public companies.
- > One piece of legislation, the **Sarbanes-Oxley Act**, increased penalties for destroying, altering, or fabricating records in federal investigations or for attempting to defraud shareholders.

Relevant Federal Laws

- > Securities Act of 1933
 - > After stock market crash 1929
 - > Regulates Securities (information, fraud)
 - > Securities Exchange Act of 1934
 - > Governs secondary trading of securities
 - > Stocks, bonds, etc.
 - > Antifraud provisions
 - > Sarbanes-Oxley Act of 2002
 - > After Enron
 - > The legislation set new or enhanced standards for all U.S. public company boards, management and public accounting firms.
 - > It does not apply to privately held companies
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Legal entity – common characteristics

- > Shareholder's liability limited to investment
- > Formation: filed with secretary of state
- > Taxes as separate entity
- > Statutory requirements (persons, no residence, name, officers, shares, address, purpose)
- > Financing (stocks, bonds)
- > Piercing corporate veil (torts, fraud, inadequate capitalization, parent liability)
- > Duties of directors and officers (duty of care, duty of loyalty, business judgement rule)
- > Private / public (listed) corporations (Securities and Exchange Act, Sarbanes – Oxley Act)

Influence of USSC

Limitation of financial contributions to politicians?

In 2010 in a five to four decision, *Citizens United v Federal Election Commission* the USSC held that corporations were persons that should be protected in the same way as natural persons under the First Amendment, and so they were entitled to spend unlimited amounts of money in donations to political campaigns.



Different forms of doing business

1. Sole Proprietorship
2. General Partnership (GP)
3. Limited Partnership (LP)
4. Corporation (Company)
5. Closed Corporation
6. Limited Liability Company (LLC)
7. Limited Liability Partnership (LLP)

1. Sole Proprietorship

- > Most simple way of running a business
 - > Only one owner
 - > Large part of US economy
 - > No separate legal existence from owner
 - > No formalities
 - > «John Miller – hairdresser»
 - > All debts of business are also personal debts
 - > No business taxes – personal taxes
 - > ~ «Einzelunternehmung»
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2. General Partnership (GP)

- > Almost every business activity as goal
 - > At least 2 partners
 - > People or business entities
 - > No legal personality
 - > Each partner is personally, jointly and severally liable for all partnership debts (torts)
 - > duty of care and loyalty (no competition)
 - > General rule: profit share equally
 - > Agreement possible by contribution
 - > Dissolved when one partner leaves
 - > Partnership agreement not subject to any form requirements
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- > No registration necessary

3. Limited Partnership (LP)

- > Variation of general partnership
 - > RUPLA (Rev. Uniform Limited Partnership Act)
 - > One or more general partners and one or more limited partners
 - > Comparable to „Kommanditgesellschaft“
 - > Liability limited to their investment
 - > Investment in money, kind or services
 - > No management function for limited partner
 - > „sworn certificate“ with Secretary of State
 - > Firm: „limited partnership“
 - > Tax considerations have made LP very popular as investment vehicle, particular in real estate or „venture capital“ companies
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4. Corporation (1)

- > Legal entity comparable to «AG»
 - > Easily formed by filing the articles of incorporatons with State Secretary
 - > Articles of incorporations (Statuten) and public notary
 - > Not very demanding
 - > Bylaws (Reglemente)
 - > Business name includes „Corp.“, „Inc.“ or „Ltd.“
 - > Issuing shares
 - > Types: Public corporation/closed corporation
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4. Corporation (2)

- > Board of Directors = VR / officers (Angestellte)
 - > Z.B. CEO, CFO, etc, chairman of the board
- > Board of Directors appoints the officers and monitors them
- > Both have duty of care and loyalty
 - > Also majority stock owner
- > Decisions protected from court review by „business judgement rules“
 - > Judges are no better business man, to protect board if acting in good faith
 - > Exception: conflict of interest
- > Internal affairs-rule (law of the where company was created)
 - > For internal affairs (first Delaware, today all states)
- > Stockholder not liable

 - > Exception: Piercing corporate veil (Expl.)

Piercing corporate veil (1)

- > The rule
 - > Laya v. Erin Homes Inc. (1986)
 - > Mr. and Mrs. Laya purchased a mobile home from Erin Homes, Inc.
 - > When the corporation failed to deliver their mobile home as promised, they sued both the corporate entity (which had almost no assets) and its only shareholders, Mr. Ferns and Mr. Finnerman
 - > Court dismissed lawsuit, citing the familiar basic American rule that corporate liability extends only to the assets of the corporation, thus precluding a „piercing of the corporate veil“ to reach the assets of the corporate shareholders
 - > But there are exceptions
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Piercing corporate veil (2)

> Walkovszky v. Carlton (1966)

- > New York taxis business
 - > Set up a corporation for each taxi but was in fact run by one company
 - > Taxi hit person on the street
 - > That taxi corporation had no money
 - > Insurance only up to \$10'000
 - > Question: piercing the veil?
 - > Undercapitalised subsidiary?
 - > In such cases piercing seems possible (misuse)
 - > But in this case Court held by majority no piercing
-

Piercing corporate veil (3)

- > In Kinney Shoe Corp vs. Polan, the Fourth Circuit Federal Court of Appeals held that it would pierce the veil if
 - > (1) the corporation had been inadequately capitalized to meet its obligations
 - > (2) if no corporate formalities (e.g. meetings and minutes) had been observed,
 - > (3) if the corporation was deliberately used to benefit an associated corporation
- > However, a subsequent opinion of the same court emphasized that piercing could not take place merely to prevent "unfairness" or "injustice".
- > In a case concerning one of the worst oil spills in history, caused by the Amoco Cadiz which was owned through subsidiaries of the Amoco Corporation, the Illinois court stated that the parent corporation was liable by the fact of its group structure. ^[59] The courts therefore "usually apply more stringent standards to piercing the corporate veil in a contract case than they do in tort cases" because tort claimants do not voluntarily accept limited liability.†

Piercing corporate veil (4)

> Amoco Cadiz

- > In a case concerning one of the worst oil spills in history, caused by the Amoco Cadiz which was owned through subsidiaries of the Amoco Corporation, the Illinois court stated that the parent corporation was liable by the fact of its group structure.
- > The courts therefore "usually apply more stringent standards to piercing the corporate veil in a contract case than they do in tort cases" because tort claimants do not voluntarily accept limited liability.¹

4. Corporation (3)

- > Limited liability (corporation only)
 - > Yearly: income statement, balance sheet, evtl. auditing
 - > Stocks and stockholders
 - > Stock exchange – public corporation (AG)
 - > Stocks can be transferred with agreement
 - > Consent not required (otherwise in articles of incorp.)
 - > „one man corporations“ possible
 - > Director's duties
 - > Business judgement rule
-

4. Corporations (4)

> Closed corporation

- > „Closed corporation“ (GmbH)
 - > Fixed shareholders (family business)
 - > Not more than 500
 - > < US \$ 5 million
 - > Not so many
 - > Same name
 - > Tax advantages
 - > Often specific duty of care
 - > Voting rights – agreements
 - > **Stock transfer restrictions**
-

4. Corporations (5)

> public corporations

- > Listed on a stock exchange
- > Special federal legislation

> Stock transfer restrictions

4. Corporations (6)

> Advantages:

- > Perpetual lifetime (not dependend of lifetime owner)
- > No liability for stockholders
- > Board and officers are obliged to do business in best interest of stockholders

> Disadvantages:

- > Double taxation
 - > Result: limited liability company
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5. Limited Liability Company (LLC) (1)

- > Relatively new type – more flexible
 - > Recently established by statutory law
 - > 1992 Uniform Limited Liability Company Act (NCCUSL)
 - > Between limited partnership and closed corporation
 - > Combines advantage of limited liability of corporation and tax status of partnership (no double taxation)
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5. Limited Liability Company (LLC) (2)

- > Similar formation like corporation
 - > Article of incorporation and certificate of formation from State Secretary
 - > Name: LLC oder Limited Liability Company
 - > Often only limited duration (f.e. 30 years)
 - > Transfer to third party without consent only interest, not voting rights
 - > Members do also manage LLC
-
- > For small companies, not investors

Corporation or LLC?

> http://www.youtube.com/watch?v=i_Je_66jwtY

6. Limited Liability Partnership (LLP)

- > More recent model
 - > General partnership in which the partners enjoy certain types of liability protection
 - > Protection varies from state to state
 - > Insurance instead of personal liability
 - > Registered with Secretary of State
 - > Popular legal form for professional like lawyers
 - > Many big law firms are LLP
 - > Can have unlimited term
 - > Change in partnership only with consent
-

Capital Market Regulation

- > Securities and Exchange Commission (SEC)
 - > Sole power concerning federalwide business and supervision of financial services operators and mutual funds
 - > National Securities Market Improvement Act (1996)
 - > Securities Litigation Uniform Act (1998)
 - > Very powerful
 - > State authorities nowadays very limited powers
 - > < 25 million
- > Sarbanes-Oxley Act (2002)
 - > Additional obligation on executives, audit committees, information)

Stock exchange

- > NYSE (Wall Street)
- > Largest stock exchange in the world
 - > Dow Jones Index
- > 1790
- > 24. October 1929 («black Thursday»)
- > NY Stock Exchange Regulation

Conclusions 1

- > Like Swiss law US law distinguishes between two fundamental types of legal organizations:
 - > partnership and corporations
 - > But also „hybrid“ legal forms
 - > Choosing right form mostly depends on
 - > Liability risks
 - > tax
-

Conclusions 2

- > Legal basis of corporations: state law mostly in accordance with model laws
- > Creation of company very easy
- > No minimum required capital
- > One man corporation legal
- > Liability/management

Next time (in two weeks!)

antitrust