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## FARALLON LAW GROUP NEWSLETTER (MARCH, 2012)

### Maintaining Corporate Formalities

Forming a corporation generally protects the shareholders from personal liability for claims against the company. However, in order to retain that protection, it is critical that certain corporate formalities be maintained.

➤ **Properly Form the Corporation.** The corporation should be properly formed and all necessary internal documentation completed. For example, organizational resolutions of the Board of Directors should adopt Bylaws and approve the issuance of shares, the opening of accounts, corporate signatories, any S-corporation tax election, etc. The corporation should also be properly capitalized with adequate funds and other assets. There are no specific rules as to the minimum amount of contributions but should be sufficient to carry the corporation through the initial phase of operations.

➤ **Keep Corporate Assets Separate.** Corporate funds should be maintained in separate accounts in the name of the corporation and never commingled with non-corporate funds. To the extent necessary, any loans to or from the corporation should be evidenced by signed promissory notes including the accrual of interest. Payments from the corporation to officers, directors and shareholders should be documented and appropriately characterized, e.g., distribution, dividend, reimbursement of expenses, payment of wages, etc. Corporate assets (funds, property or other assets) should never be used for personal purposes. All corporate purchases of goods or services should be done in the name of the corporation.

➤ **Hold Meetings.** The shareholders and Board of Directors should hold meetings periodically, at least every 12 months. The specific requirements, often contained in the Bylaws, should be followed (such as proper notice, having a quorum, following voting rules, etc.). Minutes of every formal meeting should be prepared and approved. In lieu of meetings, formal resolutions (often called an "Action By Written Consent") can be prepared (some must be unanimously approved). The Board and shareholders should consider and approve various corporate matters, including significant corporate decisions such as:

- Election of Directors and officers (and changing the terms of employment);
- Any transactions with insiders;
- Entering into a lease;
- Entering into any other significant contractual agreement;

- Issuing shares or other equity or taking on significant debt;
- Issuing dividends/distributions;
- Entering into a significant new venture or line of business; and,
- Considering the sale, in whole or in part, of the assets or the dissolution of the business.

➤ **Maintain Proper Records.** The corporate books should contain all corporate documents (Articles/Certificate of Incorporation, meeting minutes, Actions By Written Consent, stock ledger, etc.) in an organized manner. Complete and accurate financial records should be maintained and proper financial statements should be prepared.

➤ **Properly Sign Legal Documents.** All contracts signed on behalf of the corporation should be signed using a proper "signature block", in the following form which specifies that the person signing is signing in a particular capacity:

*[Insert name of corporation]*

By: \_\_\_\_\_

*[signature above]*

Printed Name: \_\_\_\_\_

Title: \_\_\_\_\_

➤ **Comply with Organizational Documents.** Officers, directors and shareholders should comply with the requirements and restrictions in the Articles/Certificate of Incorporation, Bylaws and other corporate documents such as shareholder and buy-sell agreements.

These rules apply equally to other types of entities (such as limited liability companies) although some types require fewer formalities, e.g., LLCs do not require periodic formal meetings of the managers/members although properly documenting decisions is recommended.

Regardless of adhering to corporate formalities, it is also always recommended for corporations to maintain adequate amounts of business liability and other insurance to provide additional protection.

***Please feel free to contact Boris Lieberman or Mario Kashou at 415-255-2450 if you have questions about maintaining proper corporate formalities.***

*This Newsletter is intended as a general guide to law issues and developments. It does not contain a general legal analysis or constitute a legal opinion of Farallon Law Group LLP or any member of the firm on the legal issues described. It is recommended that readers not rely on this general guide in structuring individual transactions but that professional advice be sought in connection with individual transactions.*