"MINE ALL MINE"

THE CORPORATE OPPORTUNITY DOCTRINE IN ALABAMA

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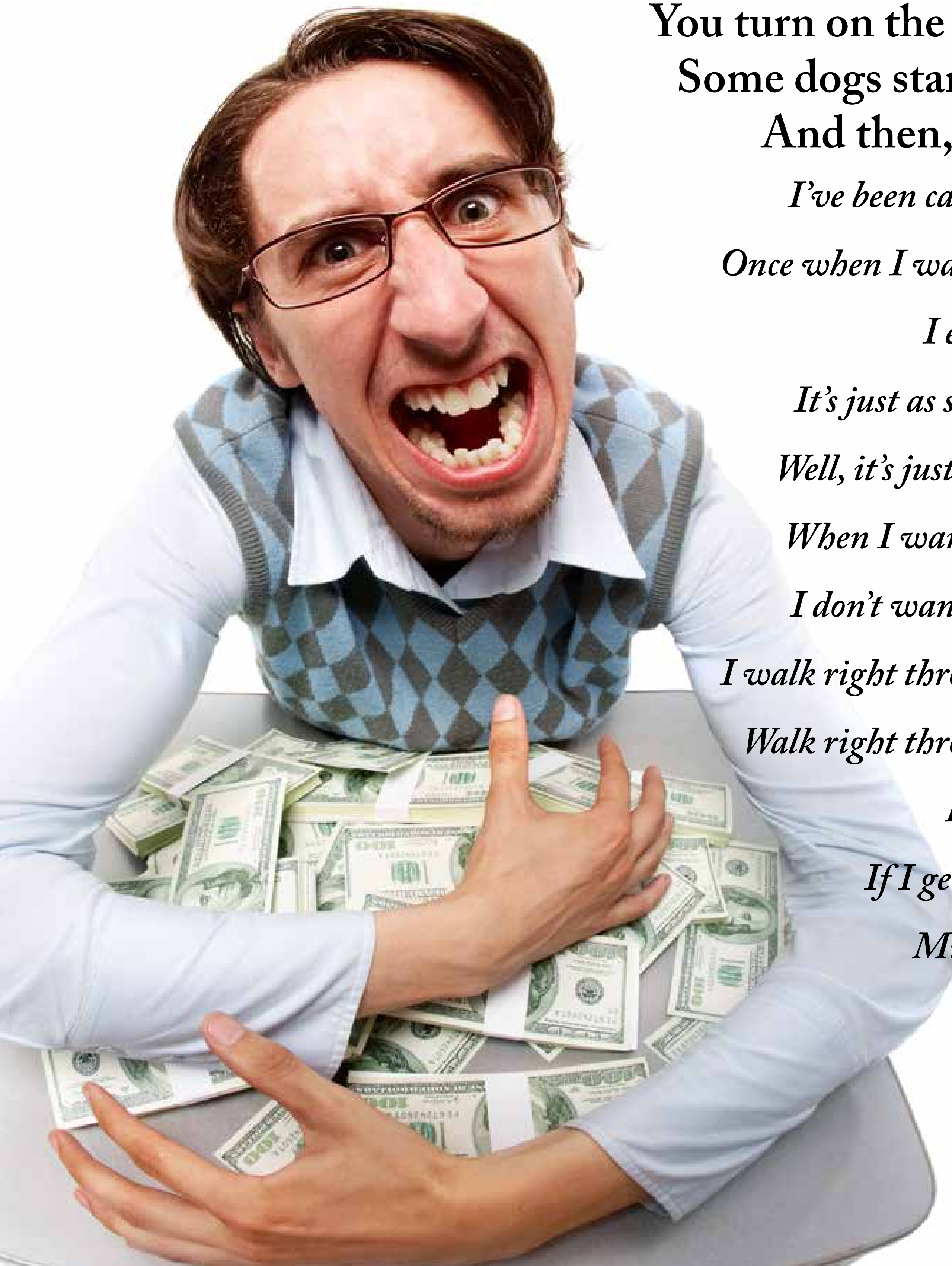


You turn on the car stereo.
Some dogs start barking.
And then, the lyrics:

I've been caught stealing

Once when I was (insert age)

I enjoy stealing

It's just as simple as that

Well, it's just a simple fact

When I want something,

I don't want to pay for it

I walk right through the door

Walk right through the door

Hey all right!

If I get by, it's mine

Mine all mine![1]

As the song says, some folks enjoy stealing. It's just as simple as that. Everything is "mine all mine." Opportunities are taken. Nobody but the taker gets paid. What happens when one of those sorts is a co-owner in a business? Or, heaven forbid, is your business partner? The "corporate opportunity doctrine" may provide some protection.

The corporate opportunity doctrine "precludes corporate fiduciaries from diverting to themselves business opportunities in which the corporation has an expectancy, property interest or right, or which in fairness should otherwise belong to the corporation."[2] In other words, it is a legal principle intended to prevent fiduciaries in a company from taking for themselves any business opportunity that could benefit the company. It arises from the fiduciary duty of loyalty. [3]

A claim of corporate opportunity may arise when a fiduciary individually seizes a promising business opportunity that could be used for the corporation's benefit. The person often organizes a new company (from which the other owners in the existing company are excluded) as part of a plan to take advantage of the opportunity. [4]

Let us consider an example. Dick and Jane open a burger joint, "Dick & Jane Burgers, LLC." They are 50/50 members of the LLC and each have management authority. They decide that a signature of the restaurant will be its amazing house-made buns. Dick & Jane Burgers will make its own buns from scratch, using a recipe from an old magazine. The buns are fantastic. Customers line up to get a burger, just so they can get a bun. Jane normally runs the cash register. Customer after customer tells her, "You guys should start selling just these buns." Jane gets inspired. Jane starts "Jane's Buns, LLC." Jane is the sole member of the new company. Dick does not get a piece. In Jane's off hours from the burger joint, she and her family start making the buns at home and selling them at a local market. Before long, a grocery distributor picks up the buns. Now the buns are available on every grocery-store shelf in town. Jane is so successful with these buns that she starts to lose focus on the burger business. Dick is doing all the work. Dick is not happy. The funny thing is that, now that people can buy the buns at the grocery store, they stop going to Dick & Jane Burgers. The burgers were not that great anyway. Dick & Jane Burgers goes out of business. Dick is unemployed and going broke. The landlord still wants the lease payments. The bank is repossessing the kitchen equipment. Meanwhile, Jane is getting rich from her burgeoning bun empire.

Suppose Dick comes and knocks on the door at your law office? Is there any hope for him? What do you tell him?

As in most areas of the law, every case is different. Maybe the company agreement of Dick & Jane Burgers, LLC, specifically allowed for Jane to do what she did. Or maybe it did not. Either way, the first place the lawyer must start is by reviewing the governing documents of the business. The governing documents will be critical in understanding what sort of conduct is permissible and what is not. At the same time, the lawyer must review the statute governing the particular form of business entity. An owner's duties may depend on the form of entity. A person who is an officer or director or controlling shareholder in a corporation may have different duties than a mere non-controlling shareholder. Similarly, a mere member in an LLC may have different duties than a member with management authority. Next, the lawyer must review the case law that outlines the corporate opportunity doctrine. That is where the rest of this article will now go.

Although there is not a set rule or set test to determine if a fiduciary has breached their duty of loyalty via the corporate opportunity doctrine, the Alabama Supreme Court has described what the doctrine encompasses, holding that it is limited to three possible areas of contention:

1) property wherein the corporation has an interest already existing;
2) in which it has an expectancy growing out of an existing right; or
3) to cases where the officers' interference will in some degree balk the corporation in effecting the purposes of its creation. [5]

The last category of offenses, "balking at the corporate purpose", is likely the most common but it is rather broad and can be generally restrictive on fiduciaries. However, Alabama has adopted the Delaware Supreme Court definition of "balking the corporate purpose" that the Court finds to be more practical:

> "[I]f there is presented to a corporate officer or director a business opportunity which the corporation is financially able to undertake, is, from its nature, in the line of the corporation's business and is of practical advantage to it, is one in which the corporation has an interest or a reasonable expectancy, and, by embracing the opportunity, the self-interest of the officer or director will be brought into conflict with that of his corporation, the law will not permit him to seize the opportunity for himself."[6]

The most succinct definition, however, may be found from the Middle District of Alabama, "The corporate-opportunity doctrine is invoked when a director or officer appropriates for personal benefit a business opportunity that belongs to or <u>should have been offered</u> to the corporation.[7]

Those directors, officers, managers, and/or owners who are tasked with the fiduciary duty of loyalty must act "as guardians of corporate welfare" because of the nature of their control and the power to manage the affairs of the company. Countless sticky situations will continue to arise so long as such guardians take for themselves what should have belonged to or been offered to the company. They would do well to remember that all corporate responsibilities must be discharged in good faith and with "conscientious fairness, morality and honesty in purpose." [8]

Illustrative Cases

The following handful of cases will help illustrate how the corporate opportunity doctrine has been applied by the Alabama courts.

Mitchell v. K&B Fabricators, Inc., 274 So. 3d 251 (Ala. 2018).

In 2018, the Alabama Supreme Court applied the doctrine and found that a CEO had breached his duty of loyalty in multiple instances, all of which were interconnected. The wrongdoer was the CEO of a closely-held corporation with four shareholders (Company A). The business sold storm shelters. The CEO approached a fabricator about starting a separate corporation which would fabricate these same types of storm shelters. This new corporation (Company B) would be closely held by three shareholders. The CEO was the only overlapping shareholder between the two corporations. A shareholder from Company B stated that the CEO wanted to be a shareholder and a director so that the fabricating corporation (Company B) would prioritize Company A's work. However, this relationship changed overtime. The CEO of the selling company (Company A) began to test and investigate whether Company A could fabricate and sell these on their own.

The fabricating company (Company B) sued the selling company (Company A) on several grounds, some of which turned on whether the CEO breached its fiduciary duty of loyalty to Company B. Although the trial court held there was no exclusive agreement between the two companies, the court concluded that the CEO did in fact breach his duty of loyalty to Company B. The CEO appealed. The Alabama Supreme Court affirmed the trial court's decision and found that where the CEO took steps to end Company A's relationship with Company B, started Company A's own fabrication business, sought to hire away a key fabricating employee from Company B, and started competing with Company B, he knowingly destroyed Company B. The Court stated that the CEO consciously caused Company A to no longer deal with Company B and for Company A to complete the fabricating orders itself, which was to the benefit of the CEO and Company A. The duty of loyalty that he owed to Company B did not require him to give all of Company A's orders to Company B. However, "he may not wrongfully use the corporation's resources therein, nor may he enter into an opposition business of such a nature as to cripple or injure the corporation."[9]

Massey v. Disc Mfg., Inc., 601 So. 2d 449 (Ala. 1992).

DMI and Quixote filed a complaint against the Disctronics Group. The complaint alleged, among other claims, that the defendants had diverted business and contracts from DMI to another electronics company (MTI) in violation of fiduciary duties and that they engaged in unfair competition in violation of §§ 8-12-1 et seq., Ala. Code 1975. The bigger allegation, however, was that DMI and Quixote breached a fiduciary duty by failing to present to DMI and Quixote the corporate opportunity represented by the acquisition of MTI.

Initially, the trial court found that DMI had a protectable interest in MTI, calling the acquisition, "a ludicrously good deal." They reasoned that the "fiduciaries" of DMI and Quixote had been "grievously unfair" and had therefore violated their fiduciary duties by taking for themselves a corporate opportunity properly belonging to DMI. In addition, the trial court found that, unless enjoined, the Disctronics Group would cause DMI irreparable harm by taking DMI's major customer to MTI. Considering all these factors, the trial court concluded that DMI and Quixote had presented a fair question as to the existence of a right to be protected and had established a substantial likelihood of success on the merits. The Disctronics Group appealed.[10]

The opportunity presented by MTI was created by the Disctronics Group's prior relationship that was shown to have been established long before. DMI was a wholly owned subsidiary of the Disctronics Group, and no fiduciary duty of loyalty in the context of corporate opportunity is owed by a parent to a wholly owned subsidiary.[11] Also, under the terms of the "Work-Out Agreement," at the end of the option period either the Disctronics Group would control DMI as a wholly owned subsidiary or they would have no interest in the company. Under either scenario, no fiduciary duty of loyalty was owed.[12]

The Court further reasoned Quixote never became a party to be protected from the excesses of the Disctronics Group. The opportunity allegedly usurped from DMI was never DMI's opportunity and could not be, analyzing the creation of the opportunity and the relationship of the parties. [13]

Banks v. Bryant, 497 So. 2d 460 (Ala. 1986).

This case arose from a dispute in which the minority shareholders alleged the majority shareholders, who were also corporate officers and directors, usurped their business interests by obtaining a contract for themselves to manage a new and competing dog-racing track in another county. Originally, "Greenetrack" was one of only two dog racing tracks in Alabama. It was corporate policy that the holding group of Greenetrack was to resist all potential competition, and, if another county did allow for construction of a new dog track, the Greenetrack group would take all of the necessary efforts to build one.

Macon County allowed for the construction of a new dog track. Upon receiving this news, three majority shareholders of Greenetrack acted on their own, not with the corporation, to obtain a contract to operate the new track. The trial court sided with the majority shareholders. The trial court found that, because the majority shareholders formed a new corporation to manage the track and did so to avoid internal conflict within the group, this was a personal opportunity for the shareholders and not a business one.

It was undisputed the majority shareholders used Greenetrack property and resources to acquire the contract in Macon County. This property included architectural plans, confidential marketing studies, physical facilities, an airplane, as well as Greenetrack employees and their skill sets. Interestingly, the majority shareholders also pledged their shares in the Greenetrack holding group as security to cover construction costs.

The majority shareholders argued that these various assets were *not* corporate assets of Greenetrack because they were provided at no cost to Greenetrack. However, on appeal, the Alabama Supreme Court held that this should not be the determinative factor. The Court sided with the plaintiffs in finding that it should not be the cost to Greenetrack that is determinative, but rather the value provided to the new Macon County company.[14] The Alabama Supreme Court held:

> Irrespective of the Macon group's statement that they did not want to do business with Greene Group, it was in fact the facilities, assets, and expertise of Greene Group that they were calling on for aid. It was not the individuals' facilities or expertise or assets that the Macon County group was seeking for the management of its racetrack. This is abundantly clear from what in fact did occur. The Macon County group did not in fact obtain the services of the individuals; rather, it received what these individual defendants had access to through the Greene Group corporation.[15]

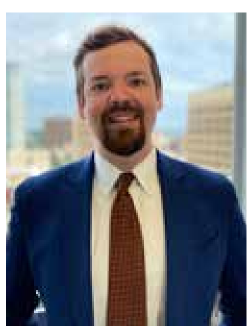
As a result, the Court sided with the minority shareholder plaintiffs and ordered the trial court to impress a constructive trust upon the defendants' newly gained income and assets.

Conclusion

"Thou shalt not steal." It is right there in the Ten Commandments. From the time of Moses through today, and surely far into the future, there are people who steal. People who say, "Mine all mine!" If one of these people is a fiduciary in a business, they may be called to task for breaching the duty of loyalty. Remember Dick & Jane's Burgers? When Dick comes knocking on the law firm door, the lawyer should study the governing documents, study the business entity statutes, review the case law, and see if there is a case. If there is, then Dick may have a remedy in the corporate opportunity doctrine. Dick may become the proud and rightful new owner of half of Jane's Buns, LLC. If there is not a case, then Dick may just be stuck with the lonesome memory of an opportunity lost.

1. "Been Caught Stealing" by Jane's Addiction, Warner Brothers Records 1990.
2. Black's Law Dictionary 340 (6th ed. 1990).
3. Massey v. Disc Mfg., Inc., 601 So. 2d 449, 456 (Ala. 1992).
4. O'Neal and Thompson's Oppression of Minority Shareholders and LLC Members § 3.18 (2d ed., rev., 2009).
5. Lagarde v. Anniston Lime & Stone Co., 126 Ala. 496, 502, 28 So. 199, 201 (1900).
6. Guth v. Loft, Inc., 5 A.2d 503, 511 (Del. 1939).
7. Davis v. Dorsey, 495 F. Supp. 2d 1162, 1170 (M.D. Ala. 2007) (emphasis added).
8. Massey v. Disc Mfg., Inc., 601 So. 2d 449, 455-56 (Ala. 1992)(citing Alpert v. 28 Williams St. Corp., 483 N.Y.S.2d 667, 673-74, 473 N.E.2d 19, 25 (1984)).
9. Citing Banks v. Bryant, 497 So. 2d 460, 462-63 (Ala. 1986).
10. Massey v. Disc Mfg., Inc., 601 So. 2d 449, 453 (Ala. 1992)
11. See Anadarko Petroleum Corp. v. Panhandle E. Corp., 545 A.2d 1171,1174 (Del. 1988)
12. Massey v. Disc Mfg., Inc., 601 So. 2d 449, 457-58 (Ala. 1992)
13. Id. at 459.
14. Banks v. Bryant, 497 So. 2d 460, 461-62 (Ala. 1986)
15. Id. at 462-63.

Gregory A. Brockwell is a business litigation attorney based in Birmingham, Alabama, with the firm of Brockwell Smith LLC. His practice focuses on representing local individuals and businesses in disputes with their business partners, banks, insurance companies, competitors, and the like. Greg has been recognized by Super Lawyers in Business Litigation, by Best Lawyers in America in Construction Litigation, and as a Top Attorney by B-Metro Magazine. He is a Board Member of the Alabama State Bar's "Business Torts and Antitrust Section." He is also the founding chairperson of the "Business Torts" caucus of the Alabama Association for Justice, serving on the ALAJ's Board since 2014.



Allen Sorrell, a native of Pelham, Alabama, joined Brockwell Smith in 2019. Allen was admitted to the Alabama bar in 2015 and has handled litigation all across the state.

In law school, Allen served as an Associate Justice for Cumberland's Moot Court Board and competed in Appellate Moot Court Competitions across the country. Since graduating from the Cumberland School of Law in 2015, he has always represented individuals during their most trying and uncertain times with personal care and attention. As the son of small business owners, he understands the importance and value of client service. Today, Allen advises clients on a variety of matters, providing independent and informed counsel on the legal aspects of their claims and disputes.

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