

From the desk of:
Irving A. Sonkin

MEMO RE CORPORATE STATUS

1. **INTRODUCTION.** This Memo should be read in conjunction with our Memo Regarding Choice Of Business Entity. This Memo is an introduction of various issues. In this memo we:

- Summarize what it means to be a **Corporation**.
- Discuss guidelines for maintaining the **Corporation's** separate status.
- Describe various **Corporate Documents**.

2. **DEFINED TERMS.**

2.1. **Act.** The Washington Business Corporation's Act, as codified in Title 23B of the Revised Code Of Washington.

2.2. **C Corporation.** A **Corporation** that is taxed as a separate taxable entity.

2.3. **Company.** Acacia Property Management, Inc., a Washington corporation.

2.4. **Company's Professionals.** The **Company's** accountant, attorney and other consultants.

2.5. **Company Documents.** Written evidence of the **Company's** creation, existence and decisions.

This term does not include contracts with third parties, nor financial records.

2.6. **Corporation.** Washington corporations in general.

2.7. **Director.** A person in whom management of the **Company** is vested.

2.8. **Interested Persons. Shareholders, Directors and/or Officers.**

2.9. **Minutes.** Memorialization of the **Company's** deliberations and decisions.

2.10. **Officers.** The persons in whom the day to day operations of the **Company** are vested.

2.11. **S Corporation.** A **Corporation** that is taxed as a flow through entity (**Shareholders** taxed directly).

2.12. **Shares. Stock** is divided into **Shares**.

2.13. **Shareholder.** One of the owners of the **Company**.

2.14. **Stock.** Units of ownership in the **Company**.

3. **FORM OF ORGANIZATION.**

3.1. **Entity.** The characteristics of a **Corporation** include:

- **Administration.** It has centralized management.
- **Existence.** It can be perpetual.
- **Shield.** It provides a shield/limitation against personal liability.
- **Status.** It is a separate legal entity.
- **Stock.** It's ownership is evidenced by **Stock**, which is easily transferable (subject to legal and contractual limitations).

3.2. **Tax Impacts.** The tax impacts depend on whether, under the Internal Revenue Code, you are a **C Corporation** or as an **S Corporation**.

3.2.1. If no election is made, a **Corporation** will be a **C Corporation**. A **C Corporation** can deduct medical expenses and certain other items that are considered fringe benefits for employees. These items are probably not deductible by an **S. Corporation**. Any profit in a **C Corporation** is taxed as a separate taxable entity. The marginal tax rate starts at the lowest corporate tax rate rather than at the existing (higher) marginal personal tax rate. Any salary or dividends are taxable to the **Shareholder** at ordinary rates.

3.2.2. You can elect to be an **S Corporation**. If you qualify to be an **S Corporation**, you are a “pass through” tax entity, which means that you will essentially be taxed as an individual. However, you may have an advantage when paying Social Security tax. You may be able to classify some earnings “dividends,” rather than as earned income. The trend has been to treat **S Corporations** as partnerships or sole proprietorships for tax purposes.

3.3. **Technical Requirements.** You must comply with the technical requirements of maintaining a separate entity to benefit from having a **Corporation**. The following are guidelines in order to maintain your **Company** as an independent entity.

4. **DOCUMENTS.** The **Company’s** existence and activities are evidenced by numerous **Company Documents**. **Company Documents** should be kept where they are readily accessible, such as in a “Corporate Minute Book.” Copies of all **Company Documents** should be kept off-site. The **Company Documents** include the following (the ones with “*” are optional):

4.1. **Articles Of Incorporation.** These are required by the **Act** to establish a **Corporation**. They contain minimum information. The “Articles Of Incorporation” must be filed with the Secretary Of State.

4.2. **Annual Report.** An “Annual Report” will have to be completed and filed with the Secretary of State, subject to an annual fee.

4.3. **Corporate License.** This is evidence from the State that the **Company** is a validly existing entity. The license is valid for one year and is renewed through the filing of the “Annual Report.”

4.4. **Bylaws.** The “Bylaws” are the nuts and bolts of the **Company**, establishing internal procedure.

4.5. **Indemnity Agreement.** An agreement between the **Shareholders** sharing the risk of personal liability by requiring allocation of all personal liability between the **Shareholders** in proportion to their respective **Share** ownership.

4.6. **Minutes.** The **Company** should create and maintain **Minutes** of its annual meeting and in order to memorialize material decisions.

4.7. **Stock Certificates.** The physical evidence of ownership of the **Company**.

4.8. **Receipt For Common Stock.** An acknowledgment from each **Shareholder** that their **Stock** has not been registered with the Securities Exchange Commission and is not readily transferable.

4.9. **Stock Issuance Agreement*.** An agreement for the initial sale of **Stock** to **Shareholders**.

4.10. **Shareholders Agreement*.** An agreement amongst the **Shareholders** and the **Company** that regulates:

- Issuance of **Units**.
- Rights and obligations of each **Unitholders** with regard to the **Company**.
- Rights and obligations of each **Unitholders** with regard to each other **Unitholder**.
- Transfer of **Units**.
- **Management**.

5. **ENTITY MATTERS.**

5.1. **Separate Entity.** You must deal with the **Company** as a separate legal entity. Transactions between the **Company** and **Interested Persons** should have the same formalities that would be observed when transacting business with a stranger. Transactions between the **Company** and **Interested Persons** should be approved by non-interested **Members**.

5.2. **Registered Agent And Office.** The **Act** requires that the **Company** maintain a “Registered Office” with a “Registered Agent.” The Registered Agent is the legal recipient of formal correspondence from the State and of legal process (such as law suits). The “Registered Agent” must maintain a “Registered Office.” The initial “Registered Agent” and initial “Registered Office” are set in the “Articles Of Incorporation.” Either may be changed by formal notice to the Secretary of State.

5.3. **Company Name.** You must use your **Company** name exactly as it appears in your “Articles Of Incorporation,” letter for letter and symbol for symbol. Any deviation must be registered as a “Trade Name” with the State. The “Trade Name” registration is part of the “Master Business Application.” In this connection,

use the **Company's** name on ALL:

- Accounts, including those with financial institutions, vendors, governmental entities, utility providers, etc.
- All contracts to which the **Company** is a party.
- Directories, such as building, telephone, internet and professional.
- Government forms, including licenses and tax returns.
- Printed materials, including stationary, business cards, checks, statements, purchase orders, invoices, etc.
- Other situations that require the use of a firm name

If you were doing business prior to incorporating, you should send a written notice to all persons and entities with whom you do business, informing them of the **Company's** existence.

5.4. **Signing Documents.** Any and all documents signed on behalf of the **Company** must be signed in your representative capacity. Every signature must be in your capacity as an officer, director or other authorized agent of the **Company**. The following is an example of a proper **Company** signature:

“NEW CORPORATION INC.” (official **Company** name)

By: _____
“Selma Smith,” its President (name **and** title of person signing)

5.5. **Licenses And Permits.** All necessary governmental business licenses and permits (Federal, State, County and/or City) should be obtained prior to engaging in business activities. Each registration must be in the name of the **Company**. Confirm with the **Company's Professionals**.

5.6. **Termination And Dissolution.** A **Corporation** is dissolved by the **Shareholders**, Court order or State action, e.g. failure to timely file or pay the annual report and renewal fee. Neither the **Company**, its employee benefit plans, nor any contractual obligation should be entered into, terminated or amended before consulting with the **Company's Professionals**.

5.7. **Transfer Of Stock.** Transfer of **Stock** is controlled by a “Shareholders Agreement (if any),” the Bylaws, State and federal law.

6. **FINANCES.**

6.1. **Capitalization.** The **Company** must be capitalized (funded) as follows:

- The initial capitalization is through the contribution of cash or other assets in exchange for the issuance of **Shares** to the contributor.
- Additional capital may be through the contribution of cash or other assets in exchange for the issuance of **Shares** to the contributor (either increasing the investment of an existing **Shareholder** or to a new **Shareholder**).
- Issuing **Company** debt in exchange for money. The **Company** cannot borrow funds until after the initial **Shares** have been issued.

Shareholders must transfer the appropriate assets/amount of cash to the **Company** prior to the **Shares** being issued. These transactions are limited by State statute, taxing statutes, securities laws and **Company Documents**. These transactions must be reviewed in advance by **Company's Professionals** and properly memorialized.

6.2. **Tax Status.** The **Company** must have an Employer's Tax Identification Number ('EIN') issued by the Internal Revenue Service. If the **Company** elects to be treated as an **S Corporation** and/or elects to use a fiscal year that is not a calendar year, forms must be timely filed with the Internal Revenue Service. The **Company** must register with state taxing authorities (through the “Master Business License Application”) and with local authorities. The **Company's** accountant can assist you in preparing the necessary forms. We do not provide any tax services, unless set forth specifically in writing by us.

6.3. **Segregation Of Assets.** The **Company's** assets and affairs must be kept separate from the personal assets and affairs of **Interested Persons**. **Company** bank accounts must be established and used for all **Company** receipts and disbursements. All assets owned by the **Company** should be entered upon the books of the **Company**. All personal disbursements should be paid through personal accounts. All **Company** disbursements should be paid through **Company** accounts. If you are short of funds, transfer to where needed and have the proper party make the disbursements. Prepare and maintain written evidence of all transfers between **Interested Persons** and the **Company**. Do not commingle personal and **Company** assets.

6.4. **Accounting.** Proper accounting is mandatory. **Directors** and **Officers** are responsible for timely complying with appropriate accounting practices.

7. **MEETINGS/MINUTES.**

7.1. **Overview.** Material **Company** decisions should be memorialized through "Resolutions" contained in **Minutes**. **Minutes** can be of a meeting, or of an agreed decision without a meeting. The **Minutes**:

- **Liability.** Provide a basis for avoiding personal liability.
- **Record.** Provide a reference regarding past decisions.
- **Taxes.** Assist in supporting tax deductions and obligations.

7.2. **Mechanics.** The **Minutes** should be transcribed by the Secretary, or transcribed by the **Company's** attorney under the direction of the Secretary. **Shareholder's** Meetings and **Director's** Meetings should be held as set forth in the Bylaws, but at least once each year.

7.3. **Shareholder's. Shareholders' Minutes** should address such matters as:

- **Bylaws.** Adopting, repealing or modifying Bylaws.
- **Directors.** Electing or removing of **Directors**.
- **Dispositions.** Disposing of assets other than in regular course of business.
- **Distributions.** Approving the distribution of assets (such as dividends).
- **Ratifying.** Ratifying prior years' activities.
- **Stock.** Creating and issuing **Shares**.
- **Status.** Approving changes in status, including mergers and liquidations/or consolidations.

7.4. **Director's. Director's Minutes** generally should address such matters as:

- **Banking.** Approving banking relationships and requirements and the borrowing of funds.
- **Bylaws.** Adopting, repealing, or modifying bylaws, subject to **Shareholder** preemption.
- **Committees.** Designating and appointing committees.
- **Contracts.** Negotiating and approving contracts that bind the **Company**.
- **Dividends.** Declaring dividends and other distribution of the **Company's** assets (subject to preemption by the **Shareholders**).
- **Employment.** Hiring or firing of key employees and appointing or revoking agents.
- **Every Day.** Conducting the everyday business and affairs of the **Company**.
- **Licensing.** Complying with licensing requirements.
- **Officers.** Electing or removing **Officers**.
- **Ratifying.** Ratifying the prior years' activities.
- **Shareholder.** Recommending actions that need **Shareholder** approval.
- **Taxes.** Authorizing the preparation of all necessary tax and other governmental returns and timely paying all taxes due.

7.5. **Organizational Minutes.** The initial **Directors** should have a meeting prior to the **Company** acquiring assets, issuing **Stock** or doing business. At the organizational meeting the **Directors** should adopt Bylaws and the other nuts and bolts of operating a **Company**, such as its various financial and contractual relationships. Discuss this with the **Company's Professionals**.

8. **INDIVIDUAL DUTIES.**

8.1. **Interested Persons.** The **Interested Persons** are key to the **Company's** success, and have the most to gain by its success.

8.1.1. **Shareholder(s).** The **Company** is wholly owned by its **Shareholders**.

8.1.2. **Directors.** Management of the **Company** is vested in the **Directors**. The **Directors** are referred to as being members of the "Board Of Directors." **Directors** are elected by, and serve at the discretion of the **Shareholders**. **Directors** can resign at any time.

8.1.3. **Officers.** Day to day operations are carried out by the **Officers**. The **Officers** serve under the direction, supervision and discretion of the **Directors**. **Officers** can resign at any time, subject to the terms of any written employment agreement.

8.1.4. **Distinctions.** **Directors** control the policy of the **Company** and **Officers** implement that policy. A **Director** may not delegate his/her authority. An **Officer** may delegate his/her responsibility and authority, but may remain liable for the results of such delegation.

8.2. **Responsibilities.** The responsibilities of **Interested Persons** include:

8.2.1. **Administrative.** Each **Director** has potential personally liability for:

- **Company Transactions.** Improperly declaring dividends or repurchasing **Stock**.
- **Employee.** Failing to pay any employment salary, benefits or taxes when due.
- **Fraud.** Fraudulent entries in the **Company Documents**.
- **Insurance.** Failing to maintain adequate insurance coverage.
- **Legal.** Failing to comply with applicable statutes, ordinances, rules and regulations.
- **Licenses.** Failing to properly maintain the **Company** and all other required licenses.
- **Supervision.** Failing to properly supervise the **Officers** and/or operations.

8.2.2. **Compensation.** Elaborate compensation plans, such as profit sharing plans, pension plans, and the like should be submitted to the **Shareholders** for their approval.

8.2.3. **Conflicts-Potential.** An **Interested Person** may not compete with the **Company** nor personally profit from business opportunities available to the **Company**, unless first approved in writing by the **Company** and the other **Shareholders** and **Directors**.

8.2.4. **Dividends, Salaries And Shares.** **Directors** or **Shareholders** may declare dividends, establish salaries and issue **Shares**. There are complex statutory and tax implications upon the issuance of **Shares** and the declaration of dividends.

8.2.5. **Duty To Inspect.** A **Director** has the right to inspect all of the **Company's** books, records, documents, and property at any reasonable time. A **Director** can be personally liable if the **Company** or its creditors suffer loss due to a **Director's** failure to exercise diligence.

8.2.6. **Loans To Directors Or Officers.** If the **Company** loans money to any **Director** or **Officers**, the loan first must be approved by a super majority (over 50%) of the voting **Shares** and recorded in the **Minutes**.

8.3. **Company's Accountant.** The **Company** should maintain a professional relationship with an accountant. The **Company's** accountant should be kept and consistently informed of the **Company's** business activities. The accountant will assist the **Company** in meeting all record keeping requirements.

8.4. **Company's Attorney.** An attorney is an integral part of the **Company's** planning process. An attorney can only represent one related party, e.g., if the attorney represents the **Company**, he/she cannot represent any **Interested Person**. There is always a potential conflict of interest if more than one person or entity is involved. Often a **Corporation** is formed by an individual **Shareholder's** attorney. If so, all of the **Shareholders** should acknowledge in writing that they have been informed of potential conflicts of interest. Each **Shareholder** should consult with their own personal attorney. Our representation of the **Company** is limited to those matters that we are specifically requested to undertake, and that we agree to undertake.

9. **LIABILITY/INSURANCE/INDEMNITY.**

9.1. **General Rule.** One of the main advantages of incorporating is that it limits the individual liability of **Shareholders** for obligations of the **Company**.

9.2. **Ignoring Company Form.** Sometimes the **Company** entity is disregarded by the Courts, and **Interested Persons** are individually liable for the **Company's** obligations. Some of the factors that can create personal liability include where:

- **Co-Mingling.** A **Shareholder** treats the assets of the **Company** as his/her own and/or treats personal assets as belonging to the **Company**.
- **Capitalization.** The **Company** does not have sufficient capitalization for normal operations.
- **Formalities.** Failure to follow **Company** formalities, such as not naming **Company**.
- **Statutes.** Statutes that create personal liability under a variety of circumstances, such as willful failure to pay salaries to employees, failure to pay certain taxes and environmental.
- **Torts.** A **Shareholder** acts or does not act.
- **Voluntary.** A **Shareholder** agrees to be personally liable for **Company** obligations.

9.3. **Insurance Coverage.** The **Company** should carry sufficient insurance for all property and operations. You should consult with a qualified insurance professional and review all risks and coverages to protect the **Company** and its **Interested Persons**, employees and agents.

9.4. **Indemnification.** The **Company**, in the Articles Of Incorporation and subject to the Act has indemnified its **Directors** and **Officers** where they act in good faith and there is no violation of a duty owed to the **Company**.

10. **CONCLUSION.** We hope these comments have been of some help to you. If you need further elaboration, have questions, or need our assistance, please feel free to contact me.

IAS