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Capital Advisors, LLC vs. Cai, 140 Nev. Adv. Op. 34 (May 23, 2024)

Ashley Burt

Capital Advisors, LLC vs. Cai, 140 Nev. Adv. Op. 34 (May 23, 2024)[1]

OFFICERS AND DIRECTORS OF A PARENT CORPORATION MAY BE LIABLE FOR INTENTIONALLY IMPLEMENTING OR KNOWINGLY PERMITTING ACTIONS BY A WHOLLY OWNED SUBSIDIARY THAT ARE ADVERSE TO THE PARENT CORPORATION AND ITS STOCKHOLDERS

Summary

The Nevada Supreme Court consolidated appeals from district court orders granting a motion for summary judgement on a case involving the liability of officers and directors of a parent company who allegedly had knowledge of actions adverse to the parent company conducted by a wholly owned subsidiary. The court affirmed the decision of the district court in part, reversed in part, vacated in part, and remanded.

Background

Cam Group, Inc. (CAMG) is a Nevada company and the publicly traded U.S holding company of multiple CAMG subsidiary holding companies. The structure for these companies is that CAMG wholly owns CAM Group, CAM group wholly owns CAM HK, CAM HK owns 98% of CAM Heibei. Ricky served as the president and a member of CAMG's board of directors from April 21, 2012 to July 29, 2013. Ricky's spouse at the time, Tracy, served as the CAMG CFO from November 16, 2012 to November 15, 2013. Appellants argued that in 2013, Ricky arranged for and issued a $1.85 million unsecured loan at 0% interest to a company called Parko Ltd. and that failure to stop this loan was her failing her duties. Appellants allege that the loan took around 80% of the cash reserves for the consolidated CAM companies

After making the loan to Parko, Ricky resigned from CAMG to work with National Agricultural Holdings Limited (NAHL), a company that Parko had entered into a Share Purchase Agreement with on July 15, 2013. He also started working for his own company Precursor Management Inc (PMI) whose primary business was managing an equity fund. Through the equity fund, PMI mad loans structures as convertible bonds to Parko that were repayable with shares of NAHL. Parko then transferred shared of NAHL to PMI as part of the transaction. Following this, Ricky's new spouse joined NAHL as a director.

Appellants Capital Advisors, LLC and Danzing Ltd., filed a shareholder derivative action as minority shareholders of Cam Group, Inc. (CAMG) against nine CAMG officers and directors, though seven defaulted. There were five causes of action that were brought to trial: (1) breach of fiduciary duty and self-dealing, (2) breach of fiduciary duty for usurping CAMG's business opportunities, (3) corporate waste, (4) civil conspiracy, and (5) unjust enrichment. After appellants rested, Ricky and Tracy moved for judgement as a matter of law and the district court granted this motion for all five causes of action. The district court then allowed the appellants to submit their remaining claims for damages against the seven defaulted which resulted in a jury reward of $130 million. Tracy and Ricky were then awarded over $2 million in attorney fees.

Discussion

[1] By Ashley Burt.

Officers and directors of a parent corporation may be liable for intentionally implementing or knowingly permitting actions by a wholly owned subsidiary that are adverse to the parent corporation and its stockholders.

The Supreme Court disagrees with the district court's determination that because CAM HK, a subsidiary, made the loan to Parko, that Ricky and Tracy could not be held liable without appellants piercing the corporate veil. The court adopts the logic that officers and directors of a parent corporation can breach their fiduciary duties by not act in the best interest of the parent and its stockholders if they are on the subsidiary board of have knowledge of a proposed action.[2] Further, the court states that a breach can occur even if the actions were implemented through a wholly owned subsidiary that is separated from the parent company by one or more intermediate wholly owned subsidiaries.

Here, the theory of liability is predicated on the officer or director of a parent company breaching their duty to that parent company. This liability is separate from claims seeking to pierce the corporate veil by applying the alter ego doctrine. Because of this, the Supreme Court found that the district court erred by finding appellants couldn't maintain any cause of action against respondents based on the finding that CAM HK made the loan.

Breach of Fiduciary Duty and self-dealing

The Supreme Court finds that appellants successfully showed a breach of fiduciary duty that involved intentional misconduct, fraud, or a knowing violation of the law. Ricky had a personal interest in the loan as his company received 10 million shares through PMI. Additionally, Tracy took no action to fix the internal company controls for monitoring the dispensation of assets and there was evidence that she knew about the loan before it was made. With additional evidence, the court concluded that the appellants presented sufficient evidence for a jury to grant relief and stated that the district court erred by granting judgement as a matter of law.

Usurpation of business opportunity

A claimant must demonstrate that the corporation "had the financial ability to acquire the asset or property" in order to show usurpation.[3]

CAMG's opportunity to invest in NAHL

Appellants assert that there was evidence that CAMG had previously discussed plants to purchase NAHL and that by approving the loan to Parko, Ricky diverted the opportunity. However, because there wasn't enough evidence to prove that CAMG could or would have participated in a partial purchase of NHAL similar in price term as Parko or that CAMG, the Supreme Court concluded that judgement of law was properly granted.

CAMG's business opportunities diverted to NAHL

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[2] Grace Bros, Ltd. v. Uniholding Corp, 2000 WL 982401, at *12 (Del. Ch. July 12, 2000).
[3] Astarte, Inc. v. Pac. Indus. Sys,, Inc, 865 F. Supp. 693, 707 (D. Colo. 1994).

Additionally, appellants argue that there were two business opportunities diverted to NAHL: (1) an opportunity to set up an electronic payment processing system with UnionPay in China and (2) an opportunity to establish an electronic trading platform for the purchase and sale of fertilizer. Here, there was conflicting evidence in regard to expectancy interests and looking at the evidence in the most favorable light to the appellants, the Supreme Court concluded that there was sufficient evidence in which a jury could grant relief ruling that the district court erred by granting judgement as a matter of law.

Corporate Waste

Because appellants were able to provide evidence that the loan was unsecured, offered at a 0% interest, and allegedly drained approximately 80% of all cash revenues, this fulfills the one-sided requirement to prove corporate waste. Therefore, the Supreme Court stated that the district court erred by granting summary judgement as a matter of law.

Civil Conspiracy

"An actionable civil conspiracy is a combination of two or more persons who, by some concerted action, intend to accomplish some unlawful objective for the purpose of harming another which results in damage."[4] Nevada does not require an "individual benefit" to find civil conspiracy but does require a purpose of harm that results in damage.[5] Here, the harm is that 80% of CAM's cash reserves were given in an unsecured, 0% interest loan that may potentially not be repaid. The unlawful objective is found through evidence that Ricky conspired with the other board members to divert money from CAMG and that Tracy was aware of the loan and took no action despite it being one-sided. As a result, the Supreme Court concludes that the district court erred by granting judgement as a matter of law.

Unjust Enrichment

Unjust enrichment is the "unjust retention…of money or property of another against the fundamental principles of justice or equity and good conscience."[6] Benefit in this context is any form of advantage and isn't limited to money or property.[7] Because Parko transferred around 10.7 million shared to PMI, a company solely owned by Ricky there is evidence that he was unjustly enriched at the expense of CAMG and its shareholders. As a result, the Supreme Court concludes that the district court erred by granting judgement as a matter of law.

<u>Conclusion</u>

Officers and directors of a parent company can be individually liable when the they have knowledge of proposed action by a wholly owned subsidiary that is adverse to the parent company and intentionally implement or knowingly permit the adverse action. Said liability isn't dependent upon piercing the corporate veil and isn't limited to wholly owned subsidiaries

[4] Collins v. Union Fed. Sav. & Loan Ass'n, 99 Nev. 284, 303 (1983).
[5] *Supra* note 3.
[6] Topaz Mut. Co. v. Marsh, 108 Nev. 845, 856 (1992).
[7] Certified Fire Prot., Inc. v. Precision Const., Inc., 128 Nev. 371, 382 (2012).

directly beneath the parent company. Here, regardless of which entity made the loan, Ricky and Terry had a fiduciary duty not to intentionally cause or allow a loan by CAMG or its wholly owned subsidiaries. Therefore, the court affirms the district court's grant of summary judgement as a matter of law as to usurpation of business opportunity based on CAMG's potential investment in NHAL. They also affirm these claims as to Tracy because they weren't raised on appeal. The Supreme Court reverses the district court's grant of summary judgement to the remaining causes of action. Therefore, the award of attorney fees and costs is vacated.