



“The Business Judgment Rule”

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The business judgment rule is a legal concept that gives the directors and officers of a corporation some level of protection against liability during good times and bad. In essence, if a director or officer functions with good faith and in a reasonable manner that is believed to be in the best interests of the corporation, he or she is protected from liability. There are definitely many shades and nuances when it comes to the question of liability, so I recommend that you get professional guidance in all cases where there may be any uncertainty at all.

In the real world of business, what tends to happen very often is an entrepreneur starts a business using his personal signature to guarantee all the credit accounts. The business grows and before anything gets structured correctly—before any corporations or other entities are created—the business grows to a medium-sized or large company, possibly with hundreds of employees. At this point, a sole proprietorship is clearly not the ideal business structure.

At some point, and usually the earlier the better, it makes sense to structure the business as a corporation and separate the personal credit history of the business owner from the business. Ideally, it would be best to start out as a corporation and build the creditworthiness of the corporation.

If you start, or restructure, your business as a corporation, then you have no personal liability, and creditors can only take the assets of the corporation and not yours personally.

Remember, however, that if you do structure your company as a corporation, since you are a leader of that corporation, you still enter the zone of



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insolvency and at that point you have a fiduciary duty to the interests of both your shareholders and the creditors and you must act accordingly or risk liability.