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SFA BILL ANALYSIS

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Senate Bill 414 (as enrolled) **PUBLIC ACT 118 of 1997**
Sponsor: Senator Michael J. Bouchard
Senate Committee: Financial Services
House Committee: Commerce

Date Completed: 5-29-98

CONTENT

The bill amended the Business Corporation Act to make a number of revisions. Among other issues addressed, the bill does all of the following:

- **-- Allows shareholders of certain corporations to contract among themselves without restrictions under the Act.**
- **-- Revises the Act's provisions limiting directors' liability.**
- **-- Specifies procedures for other types of business organizations, such as a limited liability company (LLC) or limited partnership, to combine with a corporation.**
- **-- Repeals a section of the Act commonly referred to as the "greenmail" provision.**

A more detailed description of these issues follows.

Shareholder Contracts

An agreement among a corporation's shareholders that complies with the bill is effective among the shareholders and the corporation, even if it is inconsistent with the Act in any of the following ways:

-- It eliminates the board of directors or restricts the discretion or powers of the board.
-- Subject to the Act's limitations pertaining to the protection of creditors, it governs the authorization or making of distributions, regardless of whether the distributions are in proportion to ownership of shares.
-- It establishes who are directors or officers of the corporation, or the terms of office or manner of selection or removal of corporate directors or officers.
-- It governs, in general or in regard to specific matters, the exercise or division of voting power by or between the shareholders and directors or by or among any of the shareholders or directors, including the use of weighted voting rights or director proxies.
-- It establishes the terms and conditions of any agreement for the transfer or use of property or the provision of services between the corporation any shareholder, director, officer, or employee of the corporation, or among any shareholder, director, officer, or employee of the corporation.
-- It transfers to one or more shareholders or other persons all or part of the authority to exercise the corporate powers or to manage the business and affairs of the corporation, including the resolution of any issue about which there exists a deadlock among directors or shareholders.
-- It requires dissolution of the corporation at the request of one or more of the shareholders or upon the occurrence of a specified event or contingency.
-- It otherwise governs the exercise of the corporate powers or the management of the business and affairs of the corporation or the relationship among the shareholders, the directors, and the corporation, or among any of the shareholders or directors and is not contrary to public policy.

An agreement authorized by this provision must be set forth in a provision of the articles of incorporation or bylaws approved by all persons who are shareholders at the time of the agreement, or in a written agreement that is signed by all persons who are shareholders at the time of the agreement and are made known to the corporation. The agreement also is subject to amendment by all persons who are shareholders at the time of the amendment, unless the agreement provides otherwise. In addition, if amended by an amendment to the articles of

incorporation or bylaws, the amendment must be approved by all shareholders. If amended by written agreement, the amendment must be in a writing signed by all shareholders and made known to the corporation.

The existence of an agreement under this provision must be noted conspicuously on the face or back of a certificate for shares issued by the corporation or on an information statement required under the bill. If, at the time of the agreement, the corporation has shares outstanding represented by certificates, the corporation must recall the outstanding certificates and issue substitute certificates that comply with the bill's shareholder agreement provisions. Failure to note the existence of an agreement on the certificate or information statement does not affect the validity of the agreement or any action taken pursuant to it. Any purchaser of shares who, at the time ownership is transferred, does not have knowledge of the existence of an agreement is entitled to recision of the purchase.

A purchaser is considered to have knowledge of the agreement at the time of transfer of ownership, if the agreement's existence is noted on the certificate or information statement in compliance with the bill and, if the shares are not represented by a certificate, the information statement was delivered to the purchaser at or prior to the time of transfer of ownership. An action to enforce the right of recision authorized by this subsection must be commenced within 90 days after the existence of the agreement is discovered or two years after the shares are transferred, whichever is earlier.

An agreement authorized under the bill ceases to be effective if shares of the corporation are listed on a national securities exchange or are regularly traded in a market maintained by one or more members of a national or affiliated securities association. If an agreement ceases to be effective for any reason and is contained or referred to in the corporation's articles of incorporation or bylaws, the board of directors may adopt an amendment to the articles or bylaws, without shareholder action, to delete the agreement and any references to it.

A shareholders' agreement under the bill that limits the discretion or powers of the board of directors must relieve the directors of, and impose upon the person or persons in whom the agreement vests discretion or powers, liability for acts or omissions imposed by law on directors, to the extent that the discretion or powers of the directors is limited by the agreement. The person or persons in whom the discretion or powers are vested must be treated as a director or directors for purposes of any indemnification and any limitation on liability under the Act.

The existence or performance of an agreement authorized by the bill is not grounds for imposing personal liability on any shareholder for the acts or debts of the corporation or for treating the corporation as if it is a partnership or unincorporated entity, even if the agreement or its performance results in failure to observe the corporate formalities otherwise applicable to the matters governed by the agreement.

Dissolution of the corporation pursuant to an agreement authorized by the bill must be implemented by the filing of a certificate of dissolution.

Incorporators or subscribers for shares may act as shareholders with respect to an agreement authorized under the bill if no shares were issued when the agreement was made.

Failure to satisfy the bill's unanimity requirement with respect to an agreement authorized by the bill does not invalidate any agreement that would otherwise be considered valid.

Directors' Liability

The Act previously allowed a corporation's articles of incorporation to include a provision that a director was not personally liable to the corporation or its shareholders for monetary damages for a breach of the director's fiduciary duty. That provision specified, however, that it may not have eliminated or limited the liability of a director for any of the following:

-- A breach of the director's duty of loyalty to the corporation or its shareholders.
-- Acts or omissions not in good faith or that involved intentional misconduct or knowing violation of law.
-- A violation of the Act's provisions regulating distribution of dividends (MCL 450.1551).
-- A transaction from which the director derived an improper personal benefit.
-- An act or omission occurring prior to the date on which the provision of the articles of incorporation took effect.

The bill provides, instead, that the articles may contain a provision eliminating or limiting a director's liability to the corporation or its

shareholders for money damages for any action taken or any failure to take any action as director, except liability for any of the following:

-- The amount of a financial benefit received by a director to which he or she is not entitled.
-- An intentional infliction of harm on the corporation or the shareholders.
-- A violation of the Act's provision regulating distribution of dividends (MCL 450.1551).
-- An intentional criminal act.

The bill also specifies that, if the articles of incorporation contained a provision eliminating the liability of a director under the Act prior to the bill's effective date, that provision is considered to eliminate or limit the liability of a director as provided in the bill.

Mergers Between Corporations and Other Entities

The bill provides for mergers between a "domestic corporation" and a "business organization". Under the Act, "domestic corporation" means a corporation formed under the Act, or existing on January 1, 1973, and formed under any other Michigan statute for a purpose for which a corporation may be formed under the Act. Under the bill, "business organization" means a domestic or foreign limited liability company, limited partnership, general partnership, or any other type of domestic or foreign business enterprise, incorporated or unincorporated, except a domestic corporation.

All of the following apply to a merger between a domestic corporation and a business organization:

-- One or more domestic corporations may merge with one or more business organizations if the bill's requirements are satisfied. (If all of the business organizations are foreign corporations, the merger must proceed under the Act's provisions governing those types of mergers.)
-- The merger is permitted by the law of the jurisdiction in which each constituent business organization is organized and each constituent business organization complies with that law in effecting the merger, and each foreign constituent business organization transacting business in Michigan complies with the applicable Michigan laws.

The board of each domestic corporation proposing to participate in a merger must adopt a plan of merger, setting forth all of the following:

-- The name of each constituent entity, the name of the surviving constituent entity, the street address of the surviving entity's principal place of business, and the type of organization of the surviving entity.
-- For the domestic corporation, the designation and number of outstanding shares of each class and series, specifying the classes and series entitled to vote, each class and series entitled to vote as a class, and, if the number of shares is subject to change before the merger's effective date, the manner in which the change may occur.
-- The terms and conditions of the proposed merger, including the manner and basis of converting shares, partnership interests, membership interests, or other ownership interests of each constituent entity into ownership interests or obligations of the surviving entity, or into cash or other consideration (which may include ownership interests or obligations of an entity not a party to the merger), or into a combination of those interests and obligations and cash or other considerations.
-- If the surviving entity is to be a domestic corporation, a statement of any amendment to the articles of incorporation of the surviving corporation to be effected by the merger or any restatement of the articles, which must be in a form restated as provided in the Act.
-- Other provisions with respect to the

proposed merger as the board considers necessary or desirable.

A plan of merger adopted by the board of each constituent domestic corporation must be submitted for approval at a meeting of the shareholders.

A domestic corporation that has not yet commenced business, has not issued any shares, and has not elected a board may merge with any domestic or foreign entity by unanimous consent of its incorporators. To effect such a merger, the majority of the incorporators must execute a certificate of merger.

After a plan of merger is approved, a certificate of merger must be executed and filed on behalf of each domestic corporation. The certificate must set forth all of the following:

-- A statement of the requirements for a plan of merger (described above) and the manner and basis of converting the ownership interests of each constituent entity.
-- A statement that the plan of merger has been adopted by the board.
-- A statement that the plan of merger will be furnished by the surviving entity, on request and without cost, to any shareholder of the domestic corporation.
-- If approval of the shareholders of the domestic corporation is required, a statement that the plan is approved by the shareholders.
-- In the case of a merger by a domestic corporation that has not yet commenced business, a statement that the corporation has not commenced business, has not issued any shares, and has not elected a board, and that the plan of merger has been approved by the unanimous consent of the incorporators.
-- A statement of any assumed names of merging entities transferred to the surviving entity, specifying each transferred assumed name and the name of the entity from which it was transferred. If the surviving entity is a domestic corporation or a foreign corporation authorized to transact business in Michigan, the certificate may include a statement of the names or assumed names of merging entities that are to be treated as newly filed assumed names of the surviving corporation.

A certificate of merger becomes effective in accordance with the Act. When a merger takes effect, all of the following apply:

-- Every other entity party to the merger merges into the surviving entity and the separate existence of every other entity that is party to the merger ceases.
-- The title to all real estate and other property and rights owned by each entity party to the merger is vested in the surviving entity without reversion or impairment.
-- The surviving entity may use the name and the assumed names of any merging entity, if filings required under the Act or other applicable statute are made.
-- The surviving entity has all liabilities of each constituent entity. This does not affect the liability, if any, of an "obligated person" with respect to a merging entity for acts or omissions that occurred before the merger. ("Obligated person" means a general partner of a limited partnership, a partner of a general partnership, or a participant in or an owner of an interest in any other type of business enterprise who, under applicable law, is generally liable for the obligations of the business enterprise.)
-- A proceeding pending against any entity party to the merger may be continued as if the merger has not occurred, or the surviving entity may be substituted in the proceeding for the entity whose existence ceased.
-- The articles of incorporation of a surviving domestic corporation are amended to the extent provided in the plan of merger.
-- The ownership interests of each entity party to the merger that are to be converted into ownership interests or obligations of the surviving entity or into cash or other property are considered converted.

If the surviving entity is a foreign business organization, it is subject to Michigan laws pertaining to the transaction of business in Michigan if it transacts business in this State. The surviving entity is liable, and is subject to service of process in a proceeding in Michigan, for the enforcement of an obligation of a domestic corporation that is party to the merger, and in a proceeding for the enforcement of a right of a dissenting shareholder of a domestic corporation against the surviving entity.

Greenmail

The bill repealed a section of the Act (MCL 450.1368) that prohibited a corporation from purchasing, directly or indirectly, any of its shares that were listed on a national securities exchange from any person who held 3% or more of its shares, unless one of the following applied:

-- The corporation made an offer, of at least equal value, to all other holders of the same shares.
-- The purchase was authorized in advance by the holders of the shares entitled to vote on the purchase by a vote that could have been required by the articles of incorporation or the Act.
-- The purchase met the requirement of the articles of incorporation for the purchase of shares from any person having 3% or more of the shares.
-- The shares had been beneficially owned by the person for at least two years before the date of purchase.
-- The purchase was made on the open market and not as a result of a privately negotiated transaction.
-- The purchase price per share was not greater than the average market price per share during the 30 business days before the date of purchase.
-- The purchase was authorized by the Act.

MCL 450.1132 et al.

Legislative Analyst: P. Affholter

FISCAL IMPACT

The bill will have no fiscal impact on State or local government.

Fiscal Analyst: M. Tyszkiewicz

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