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Senate Bill 206 (Substitute S-1 as reported)
Sponsor: Senator Bill Bullard, Jr.
Committee: Financial Services

Date Completed: 4-16-01

RATIONALE

The Business Corporation Act provides for the organization and regulation of corporations, including their filings, the issuance of stock, how meetings of shareholders and directors are conducted, corporate governance, mergers, and dissolution. The Act regulates the majority of business entities in the State, except for limited liability companies, partnerships, and sole proprietorships. Approximately 300,000 corporations, ranging from large public corporations to car dealerships, in the State are regulated under the Act, according to the Bureau of Commercial Services in the Department of Consumer and Industry Services. Originally adopted in 1972, the Act replaced a 1931 statute that had regulated corporations. Since then, the Act has been updated periodically, with significant changes being made in 1989. Amendments enacted in 1997 addressed limits on directors' liability, mergers between corporations and other legal entities, and the modernization of proxy provisions. The Business Law Section of the State Bar of Michigan has recommended that the Act be updated further to reflect the present way in which business is conducted electronically, remove some uncertainty, add flexibility, and conform to legal developments in other states.

CONTENT

The bill would amend the Business Corporation Act to do the following:

- **Permit the electronic transmission of certain documents, including a document relating to a domestic or foreign corporation, a notice or communication under the Act, and notice of a shareholders' meeting.**
- **Permit a corporation's financial report to be distributed electronically.**
- **Permit a shareholders' meeting to be conducted solely by remote communication, and permit a shareholder or board member to participate in a meeting by means of remote communication.**

- **Allow a board to impose certain restrictions on the exercise, transfer, or receipt of rights to purchase shares of the corporation.**
- **Establish time limits for commencing a shareholder action for oppression seeking an award of damages.**
- **Remove mandatory indemnification of an employee or agent of a corporation who was sued.**
- **Prohibit a class or series of shareholders from voting as a class if the class would receive at least the fair value of the shares of the class or series when a plan of merger or share exchange was adopted.**
- **Specify that a corporation would not have disposed of substantially all of its property and assets if it retained a significant business activity, as defined in the bill.**
- **Specify that the Act would apply to professional service corporations formed under the Professional Service Corporation Act.**

Electronic Transmission

Under the Act, a document required or permitted to be filed must be filed by delivery to the administrator together with fees and accompanying documents required by law. (The administrator is the Director of the Department of Consumer and Industry Services.) The administrator may establish a procedure for accepting delivery by facsimile transmission. The bill also would allow delivery by other electronic transmission. ("Electronic transmission" or "electronically transmitted" would mean any form of communication that met all of the following: did not directly involve the physical transmission of paper, created a record that could be retained and retrieved by the recipient, and could be reproduced directly in paper form by the recipient through an automated process.)

Currently, if a document relating to a domestic or

foreign corporation filed with the administrator was at the time of filing an inaccurate record of the corporation action referred to in the document, or was defectively or erroneously executed, the document may be corrected by the filing of a certificate of correction on behalf of the corporation. Under the bill, a certificate of correction also could be filed if the document were electronically transmitted and the electronic transmission were defective.

When, under the Act or the articles of incorporation or bylaws of a corporation or by the terms of an agreement or instrument, a corporation or the board or any board committee may take action after notice to any person or after the lapse of a prescribed period of time, the action may be taken without notice or lapse of time if at any time before or after the action is completed, the person to be notified or to participate in the action to be taken, or in the case of a shareholder, his or her attorney-in-fact, submits a signed waiver of the requirements. The bill would allow a signed waiver or a waiver by electronic transmission.

The bill specifies that when a notice was required or permitted by the Act to be given in writing, electronic transmission would be written notice. When the Act permitted a notice or communication to be transmitted electronically, the notice or communication would be given when electronically transmitted to the person entitled to the notice or communication in a manner authorized by the person.

Currently, if the administrator does not promptly file a document, other than an annual report, submitted for filing, the administrator within 10 days after receiving a written request to file the document from the person submitting it for filing, must give that person written notice of the refusal to file the document, specifying the reasons for the refusal. Under the bill, if the document were not submitted originally by electronic transmission, the administrator could not give the written notice by electronic transmission.

Purchase of Shares

Under the Act, a corporation may issue rights, options, or warrants for the purchase of shares of the corporation. The bill also would permit a corporation to do this for the purchase of other securities of the corporation. The Act requires the board to determine the terms upon which the rights, options, or warrants are issued, their form and content, and the consideration for which the shares are to be issued.

Under the bill, the terms and conditions of any right, option, or warrant issued under these provisions, including those outstanding on the bill's effective

date, could include, without limitation, restrictions or conditions that precluded or limited the exercise, transfer, or receipt of the right, option, or warrant by any person owning or offering to acquire a specified number or percentage of the outstanding common shares or other securities of a corporation, or any transferee or transferees of that person, or that invalidated or voided the right, option, or warrant held by a person or his or her transferee.

Acquisition of Own Shares

Subject to restrictions imposed by the Act or the articles of incorporation, a corporation may acquire its own shares, and those shares constitute authorized but unissued shares. Shares of a corporation acquired by it may be pledged as security for the payment of the purchase price of the shares. Until the corporation pays the purchase price, the shares are not canceled and do not constitute authorized but unissued shares. The bill would delete the provision allowing the pledge of shares as security. Under the bill, a corporation that acquired its own shares could grant a security interest in the shares as payment of their purchase price. Any shares acquired by the corporation in which it had been granted a security interest would not be canceled and would not constitute authorized but unissued shares until the corporation paid the purchase price.

Notice of Shareholders' Meeting

Except as otherwise provided, the Act requires that written notice of the time, place, and purposes of a shareholders' meeting be given at least 10 days but not more than 60 days before the meeting date, either personally or by mail, to each shareholder of record entitled to vote at the meeting. Under the bill, notice could be given personally, by mail, or by electronic transmission. If a shareholder or proxy holder could be present and vote at the meeting by remote communication, the means of remote communication allowed would have to be included in the notice.

Currently, if a meeting is adjourned to another time or place, it is not necessary, unless the bylaws provide otherwise, to give notice of the adjourned meeting if the time and place to which the meeting is adjourned are announced at the meeting at which the adjournment is taken. Under the bill, a shareholder or proxy holder could be present and vote at the adjourned meeting by a means of remote communication if he or she were permitted to be present and vote by that means in the original meeting notice.

Shareholders' Meeting

Unless otherwise restricted by the articles of incorporation or bylaws, a shareholder may participate in a shareholders' meeting by a conference telephone or other similar communication equipment through which all persons participating in the meeting may communicate with the other participants. Under the bill, a shareholder could participate by other means of remote communication, rather than other similar communications equipment.

Under the bill, the board of directors could hold a meeting of shareholders conducted solely by means of remote communication, unless otherwise restricted by the articles of incorporation or bylaws. Subject to any guidelines and procedures adopted by the board of directors, shareholders and proxy holders not physically present at a meeting of shareholders could participate in the meeting by means of remote communication and would be considered present in person and could vote at the meeting if all of the following were met:

- The corporation implemented reasonable measures to verify that each person considered present and permitted to vote at the meeting by means of remote communication was a shareholder or proxy holder.
- The corporation implemented reasonable measures to provide each shareholder and proxy holder a reasonable opportunity to participate in the meeting and to vote on matters submitted to the shareholders, including an opportunity to read or hear the proceedings of the meeting substantially concurrently with the proceedings.
- If any shareholder or proxy holder voted or took other action at the meeting by means of remote communication, the corporation maintained a record of the vote or other action.

The bill also provides that, in addition to any other form of notice to a shareholder permitted by the articles of incorporation, the bylaws, or Chapter 4 (Shareholders) of the Act, any notice given to a shareholder by a form of electronic transmission to which the shareholder had consented would be effective.

Under the Act, the articles of incorporation may provide that any action to be taken at an annual or special meeting of shareholders may be taken without a meeting, without prior notice, and without a vote, if consents in writing are signed by the holders of outstanding shares having at least the minimum number of votes that would be necessary to authorize or take the action at a meeting at which all shares entitled to vote on the action were present and voted. In addition, any action required or permitted by the Act to be taken at an annual or special meeting of shareholders may be taken without a meeting, without prior notice, and without a

vote, if before or after the action all the shareholders entitled to vote consent in writing.

Under the bill, an electronic transmission consenting to an action transmitted by a shareholder or proxy holder, or by a person authorized to act for the shareholder or proxy holder, would be written, signed, and dated for purposes of these provisions if the electronic transmission were delivered with information from which the corporation could determine that the electronic transmission was transmitted by the shareholder or proxy holder, or by the person authorized to act for the shareholder or proxy holder, and the date on which the electronic transmission was transmitted. That date would be the date on which the consent was signed. A consent given by electronic transmission could not be delivered until reproduced in paper form and the paper form was delivered to the corporation by delivery to its registered office in the State, its principal place of business, or an officer or agent of the corporation having custody of the book in which proceedings of shareholders' meeting were recorded. Delivery would have to be made by hand, by certified or registered mail, return receipt requested, or in any other manner provided in the articles of incorporation or bylaws or by resolution of the corporation's board of directors.

Currently, the officer or agent having charge of the stock transfer books for shares of a corporation must make and certify a complete list of the shareholders entitled to vote at a shareholders' meeting or any adjourned shareholders' meeting. The Act specifies certain requirements a list must meet, including being subject to inspection by any shareholder during the meeting. Under the bill, if the meeting were held solely by means of remote communication, the list would have to be open to the examination of any shareholder during the entire meeting by being posted on a reasonably accessible electronic network, and the information required to gain access to the list would have to be provided with the notice of the meeting.

Agreements among Shareholders

Under the Act, an agreement among the shareholders of a corporation that complies with certain requirements in the Act is effective among the shareholders and the corporation even though it is inconsistent with the Act in one or more ways specified in the Act. Under the requirements that an agreement must meet, it must be subject to amendment only by all persons who are shareholders at the time of the amendment, unless the agreement provides otherwise. The bill would delete the current provisions that if amended by an amendment to the articles of incorporation or bylaws, the amendment must be approved by all

shareholders; and, if amended by written agreement, the amendment must be in a writing signed by all shareholders and made known to the corporation.

Shareholders' Actions

Under the Act, a shareholder may bring an action in the circuit court of the county in which the principal place of business or registered office of the corporation is located to establish that the actions of the directors or those in control of the corporation are illegal, fraudulent, or willfully unfair and oppressive to the corporation or the shareholder. If the shareholder establishes grounds for relief, the court may make an order or grant relief as it considers appropriate, including an award of damages to the corporation or a shareholder. The bill specifies that a shareholder could bring a "direct action" under these provisions in addition or instead of any other action that could be available to a shareholder or a corporation. Under the bill, an action seeking an award of damages would have to be commenced within three years after the cause of action had accrued, or within two years after the shareholder discovered or reasonably should have discovered the cause of action, whichever occurred first.

The bill also would define "willfully unfair and oppressive conduct", as used in these provisions, as a continuing course of conduct or a significant action or series of actions that substantially interfered with the interests of a shareholder as a shareholder. The term would not include conduct or actions that were permitted by an agreement, the articles of incorporation, the bylaws, or a consistently applied written corporate policy or procedure.

Board Meetings

Under the Act, regular or special meetings of a board may be held either in or outside the State. Unless otherwise restricted by the articles of incorporation or bylaws, a member of a board or a committee designated by the board may participate in a meeting by means of conference telephone or similar communications equipment through which all persons participating in the meeting can communicate with other participants. Under the bill, a person could participate in a meeting by other means of "remote communication", rather than "similar communications equipment".

Unless prohibited by the articles of incorporation or bylaws, the Act permits action required or permitted to be taken under authorization voted at a meeting of the board or a committee of the board to be taken without a meeting if, before or after the action, all members of the board or of the committee consent to the action in writing. The bill also would permit the members to consent to the action by electronic

transmission.

Indemnification

The Act authorizes a corporation to indemnify a person who is or was a party, or is threatened to be made a party to an action, suit, or proceeding, by reason of the fact that he or she is or was a director, officer, employee, or agent of the corporation. To the extent that the director, officer, employee, or agent has been successful in defense of the action, suit, or proceeding under the Act or in defense of a claim, issue, or matter in the action, suit, or proceeding, the individual must be indemnified against actual and reasonable expenses, including attorneys' fees, incurred by him or her in connection with the action, suit, or proceeding. The bill would delete reference in this requirement to an employee or agent.

A corporation also may pay or reimburse the reasonable expenses incurred by a director, officer, employee, or agent who is a party or threatened to be made a party to an action, suit, or proceeding in advance of final disposition if the individual gives the corporation a written undertaking to repay the advance if it is determined that he or she did not meet the applicable standard of conduct for indemnification, and gives the corporation a written affirmation of his or her good faith belief that he or she has met the applicable standard of conduct. The bill would delete the requirement for an affirmation.

Plan of Merger or Share Exchange

Under the Act, two or more domestic corporations may merge into one pursuant to a plan of merger, and a corporation may acquire all of the outstanding shares of one or more classes or series of another corporation pursuant to a plan of share exchange, approved as provided in the Act. A plan of merger or share exchange adopted by the board of each constituent corporation must, except as otherwise provided in the Act, be submitted for approval at a shareholders' meeting. For a plan of merger or share exchange to be approved certain conditions must be met. Among other things, the board must recommend the plan of merger or share exchange to the shareholders, unless the board determines that because of conflict of interest or other special circumstances it should make no recommendation and communicates the basis for its determination to the shareholders with the plan. Under the bill, the board would have to recommend the plan unless it determined otherwise because of conflict of interest, events occurring after the board adopted the plan, contractual obligations, or other special circumstances.

The Act requires that a vote of the shareholders be taken on the proposed plan of merger or share

exchange. A class or series of shares is entitled to vote as a class in the case of a merger, if the plan of merger contains a provision that, if contained in a proposed amendment to the articles of incorporation, would entitle the class or series of shares to vote as a class, or in the case of a share exchange, if the class or series is included in the exchange. A class or series of shares is not entitled to vote as a class in the case of a merger if the sole purpose of the merger is to change the corporation's jurisdiction of incorporation; the bill would delete this provision. Under the bill, a class or series of shares would not be entitled to vote as a class in the case of a merger or share exchange, if the board of directors determined on a reasonable basis that the class or series was to receive consideration under the plan of merger or share exchange that had a fair value that was not less than the fair value of the shares of the class or series on the date of the adoption of the plan.

The bill also specifies that a plan of merger or share exchange could provide for differing forms of consideration for holders of shares within the same class based on the election of the holders, the amount of shares held, or another reasonable basis.

Disposition of Corporate Property, Assets

Except as otherwise provided in the Act, a corporation may sell, lease, exchange, or otherwise dispose of all, or substantially all, of its property and assets, with or without the goodwill, if not in the regular course of its business, upon terms and conditions and for a consideration consisting of cash or other property, including shares, bonds, or other securities of any other corporation, domestic or foreign, as authorized in the Act. Under the bill, a corporation would not have disposed of all or substantially all of its property and assets if it retained "a significant continuing business activity". The bill specifies that for purposes of these provisions, it would be presumed conclusively that a corporation had retained a significant continuing business activity if the corporation retained a business activity that represented at least 25% of total assets at the end of the most recently completed fiscal year, and 25% of either income from continuing operations before taxes or revenues from continuing operations for that fiscal year, in each case of the corporation and its subsidiaries on a consolidated basis.

Currently, the board must recommend the proposed transaction to the shareholders unless the board determines that because of conflict of interest or other special circumstances it should make no recommendation and communicates the basis for its determination to the shareholders with the submission of the proposed transaction. Under the bill, the board would have to recommend the proposed transaction to shareholders unless it determined otherwise because of conflict of interest, events occurring after the board adopted the plan, contractual obligations, or other special circumstances.

Merger or Acquisition

Under the Act, shareholders of a corporation that proposes to issue, directly or through a subsidiary, its shares, obligations, or securities in the course of a merger, acquisition of some or all of the outstanding shares of another corporation or some or all of the assets of a corporation, proprietorship, partnership, or other type of business organization must have the same rights to receive notice and vote on the proposed acquisition as provided in the Act for approval of a plan of merger or share exchange, and to receive dissenters' rights if certain conditions apply. Under the bill, these rights would apply to shareholders of a corporation that proposed to issue its shares, obligations, or securities in the course of a merger, acquisition of some or all of the outstanding shares of another corporation or interests in another entity, or acquisition of some or all of the assets other than cash of a corporation or

other entity.

Financial Report

The Act requires each domestic corporation at least once a year to cause a financial report of the corporation for the preceding fiscal year to be made and distributed to each shareholder within four months after the end of the fiscal year. Under the bill, the financial report could be distributed electronically, either by electronic transmission of the report or by making the report available for electronic transmission. If the report were distributed electronically under this provision, the corporation would have to provide the report in written form to a shareholder on request.

Applicability to Specific Corporations

Currently, unless otherwise provided in, or inconsistent with, the act under which a corporation is or has been formed, the Act applies to deposit and security companies; summer resort associations; brine pipeline companies; telegraph companies; telephone companies; safety and collateral deposit companies; canal, river, and harbor improvement companies; cemetery, burial, and cremation associations; railroad, bridge, and tunnel companies; and, agricultural and horticultural fair societies. Under the bill, the Act also would apply to professional service corporations formed under the Professional Service Corporation Act.

MCL 450.1106 et al.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The bill would update the Business Corporation Act based on recommendations of the Business Law Section of the State Bar of Michigan. The amendments would modernize the statute and provide needed clarification, as well as add flexibility and certainty in business combination transactions. Among other things, the bill would enhance the opportunities of corporations to communicate electronically. The bill would authorize a corporation to use electronic technology to transmit information to the Department of Consumer and Industry Services as well between the corporation's board of directors and shareholders. Permitting the electronic transmission of documents would accommodate the evolving methods in which information is exchanged in corporate transactions. The bill also would expand the ways in which companies use new technology

when conducting shareholders' meetings, so that these meetings could be held entirely by remote communication, without a board of director's having to designate a physical place for a meeting. In addition, a board directors could permit participation by some or all shareholders in meetings by remote communication, including electronic communication. According to the Business Law Section, these changes would reflect recent amendments in Delaware.

Supporting Argument

When a corporation is threatened by a hostile takeover by another company, the directors of the threatened company might adopt shareholder rights plans to protect the corporation from being rapidly taken over. The Business Law Section reports that more than 2,000 publicly traded corporations nationally have adopted such plans, and that Federal case law has confirmed their legality in Michigan. Nevertheless, because of similar cases in other states, some people might contend that such plans discriminate among shares and, thus, violate statutory provisions for the equal treatment of shares within a class or series. The bill would clarify in statute that shareholder rights plans are permitted in this State.

Supporting Argument

Under Section 489 of the Act, a shareholder may bring suit in circuit court to establish that the action of the directors or those in control of a corporation are illegal, fraudulent, or willfully unfair and oppressive to the corporation or a shareholder. If the shareholder establishes grounds for relief, the court may order various types of remedies, ranging from an award of damages to dissolution of the company. According to the State Bar Business Law Section, the 1998 opinion of the Michigan Court of Appeals in *Baks v Moroun* (227 Mich. App. 472) highlighted problems with the interpretation of this section. The Court did not recognize a separate cause of action under Section 489, and relied on a statute of limitations established in Section 541a, which governs actions against directors and officers for breach of fiduciary duty. This decision may result in situations in which a corporation's directors or officers who engage in unfair and oppressive conduct are subject to the limitations period in Section 541a (which is the same as that proposed by the bill), while others controlling a corporation who commit similar acts are subject to a six-year limitations period under the Revised Judicature Act (RJA). Therefore, the bill would enact a specific period of limitations for claims seeking monetary relief under Section 489. Since the bill would establish a separate cause of action under Section 489, actions under that section for A0102\s206a

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nonmonetary relief would be subject to the RJA's longer period of limitations. Also, by defining "willfully unfair and oppressive conduct", the bill would make it clear that more than an ordinary breach of duty would be required to create a claim under Section 489.

Legislative Analyst: L. Arasim

FISCAL IMPACT

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

Fiscal Analyst: M. Tyszkiewicz