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THE REVISED MODEL BUSINESS CORPORATION ACT AND CORPORATE LAW REFORM IN MISSISSIPPI: PART TWO

Wendell H. Holmes*

In the 1987 Regular Session of the Mississippi Legislature, a new business corporation act for Mississippi (hereinafter New MBCA) became a reality.¹ The new law became effective January 1, 1988.² It is based almost entirely upon the Revised Model Business Corporation Act (hereinafter RMA) and profoundly changes much of the state's pre-existing corporate law. Part One of this article,³ completed prior to the passage of the New MBCA, discussed in detail the relationship of the provisions of the RMA to the prior Mississippi Business Corporation Act (hereinafter Old MBCA) and proposed changes in Mississippi

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¹ Mississippi Business Corporation Act, 1987 Miss. Laws Ch. 486 [hereinafter New MBCA], *codified at* Miss. CODE ANN. §§ 79-4-1.01 to-17.04 (Supp. 1987). The New MBCA repeals the former statute, Miss. CODE ANN. §§ 79-3-1 to-293 (1972 and Supp. 1986) [hereinafter Old MBCA] in its entirety.

² The New MBCA is to a large degree an outgrowth of the work of the Business Law Reform Task Force convened by Secretary of State Dick Molpus in July, 1986. The Task Force undertook to draft proposed legislation to replace the existing business corporation, nonprofit corporation, professional corporation, limited partnership, and securities acts. The author was a member of the Task Force and of the subcommittee responsible for drafting the proposed business corporation act. The views expressed in this article are solely those of the author and do not represent in any way those of any other person affiliated with the Task Force.

Among the other legislation that was generated by the Task Force is a new nonprofit corporation act which closely parallels the New MBCA. This act is labeled the Mississippi Nonprofit Corporation Act, 1987 Miss. Laws Ch. 485, *codified at* Miss. CODE ANN. §§ 79-11-101 to-399 (Supp. 1987).

³ Holmes, *The Revised Model Business Corporation Act and Corporate Law Reform in Mississippi: Part One*, 56 Miss. L.J. 165 (1986) [hereinafter *Part One*].

law (including substantial revisions to much of the RMA)⁴ in the areas of corporate formation and organization, and corporate management and governance. That work now serves as the author's critique of the New MBCA regarding those topics.⁵ The methodology of Part Two of this article will, logically, be somewhat different from that of Part One. Whereas the earlier installment was primarily an analysis of existing Mississippi law with proposals for revision (using the RMA as the point of departure for the revision process), this Part will undertake a critical analysis of the New MBCA in those areas not covered in Part One: capitalization, shareholder litigation, organic changes, and the problems of the closely-held business.

I. CAPITALIZATION

A. *Par Value, Stated Capital, and Distributions*

By far the most revolutionary aspect of the New MBCA (at least in contrast to traditional Mississippi practice) is section 6.40.⁶ In one swift motion, the concepts of par value, stated capital, earned surplus, capital surplus, and treasury stock were swept from the corporate statutes. The approach of the New MBCA to these areas is particularly striking in light of some highly idiosyncratic provisions of prior Mississippi law.

Specifically, under the Old MBCA, the minimum permissible par value of stock was \$1.00.⁷ Moreover, while no-par stock was ostensibly permitted, any practical advantage of the concept was undercut by the statute's insistence that the *issue* price of no-par stock not be less than \$1.00.⁸ Thus the *raison d'être* of no-par stock, *i.e.*, the elimination of "watered stock" liability,

⁴ It might be noted that *Part One* was completed prior to the finalization of the work of the Task Force.

⁵ The New MBCA uses the same numerical system as the RMA, resulting in easy cross-reference. In addition, while the New MBCA (as is typical of Mississippi legislation) includes no published commentary and little legislative history, the Official Comments to the RMA should constitute persuasive authority regarding the interpretation of the new act.

⁶ See New MBCA, *supra* note 1, § 6.40. The new act adopts without change the corresponding provision of the RMA. REVISED MODEL BUSINESS CORP. ACT § 6.40 (1984).

⁷ Old MBCA, *supra* note 1, § 33.

⁸ *Id.*

was completely defeated.⁹ These aspects of the Old MBCA deprived corporate planners, arguably without justification,¹⁰ of a substantial degree of flexibility in matters involving a corporation's stock structure.¹¹

Criticism of the par value concept has long been widespread, and the breach in the dam occurred in 1975 when California eliminated the requirement of a statement of par value of authorized shares.¹² The ABA Committee on Corporate Laws took up the torch in 1979,¹³ and its approach was reflected in the RMA and, correspondingly, by the New MBCA.

The mere elimination of par value, however, might not appear at first blush to be that significant of a change. It is only in its relation to the question of dividends and distributions that its true importance is manifested.

The Old MBCA was a traditional "earned surplus" statute.¹⁴ Under its provisions, the par value of shares issued with a par value, or (absent any contrary allocation by the board of directors) the full consideration for no-par shares was committed

⁹ For discussion of this issue under the Old MBCA, see Hodge & Perry, *The Model Business Corporation Act: Does The Mississippi Version Lime The Bushes?*, 46 Miss. L.J. 371, 380-81 (1975) [hereinafter Hodge & Perry] (liability of shareholder for watered stock).

¹⁰ The historical rationale for the concept of par value has generally been twofold: to assure equitable contributions among shareholders by requiring that they pay a standard price ("par") for their shares; and to provide a "cushion" of capital to which creditors of the corporation would have recourse. See B. MANNING, *A CONCISE TEXTBOOK ON LEGAL CAPITAL* 19, 22 (2d ed. 1981) [hereinafter MANNING, *LEGAL CAPITAL*] (general background of development of legal capital concept). That neither premise applies today is clear. Under current practice par value establishes only the *minimum*, not the actual, issue price of shares. In addition, even under statutes such as the Old MBCA which prescribed a minimum capital contribution as a condition of doing business, the amount mandated (generally \$1000) was insufficient to provide any meaningful protection to creditors. See Old MBCA, *supra* note 1, § 111; Hodge & Perry, *supra* note 9, at 379.

¹¹ See Hodge & Perry, *supra* note 9, at 381-82.

¹² 1975 Cal. Stat. 682, § 7, codified at CAL. CORP. CODE § 202(d)(e).

¹³ Committee on Corporate Laws, *Changes in the Model Business Corporation Act - Amendments to Financial Provisions*, 34 BUS. LAW. 1867 (1979) [hereinafter *Financial Provisions*] (amendments and comments of committee). The proposed changes were finally approved for inclusion in the Model Act in 1980. Committee on Corporate Laws, *Changes in the Model Business Corporation Act - Amendments to Financial Provisions*, 35 BUS. LAW. 1365 (1980).

¹⁴ For a general discussion of such statutes, see MANNING, *LEGAL CAPITAL*, *supra* note 10, at 72-75.

to stated capital.¹⁶ The excess, if any, became capital surplus. Under ordinary circumstances, capital surplus could not be distributed to shareholders. Rather *dividends* (cash or property) could be paid only out of the "unreserved and unrestricted earned surplus"¹⁶ of a corporation, defined basically as the "balance of its net profits, income, gains and losses."¹⁷ In contrast, *distributions* (cash or property) from capital surplus¹⁸ were prohibited absent authorization in the articles of incorporation or by two-thirds of the shareholders, and were subject to other conditions involving the protection of senior security holders.¹⁹

This much of the Old MBCA was representative of most earned surplus statutes; the exact parameters of a corporation's discretion in these matters was, however, clouded by an additional, non-uniform provision of the Old MBCA specifically prohibiting *cash* dividends unless paid out of unreserved and unrestricted earned surplus.²⁰ As previously discussed in some

¹⁶ See Old MBCA, *supra* note 1, § 39. If no-par shares were issued, at least \$1.00 per share was required to be allocated to stated capital. *Id.*

¹⁶ *Id.* § 83(a).

¹⁷ *Id.* § 3(m). Stock dividends, however, could be issued out of any treasury shares reacquired out of surplus (presumably earned or capital), and out of authorized but unissued shares so long as appropriate amounts of "any unreserved and unrestricted surplus" were transferred to stated capital. *Id.* § 83(c), (d).

¹⁸ *Id.* § 3(1), (n). "Surplus" was defined as "the excess of the net assets of a corporation over its stated capital." "Capital surplus" was "the entire surplus of a corporation other than its earned surplus." *Id.* Functionally, capital surplus generally represented the excess (if any) of the issue price of shares over their par value.

¹⁹ *Id.* § 85. Neither dividends nor distributions from capital surplus could be made if the corporation was insolvent or would thereby be rendered insolvent.

The use of the label "distributions" was, of course, a distinction without a difference, since the economic effects on shareholders and the corporation were identical in either event; only the nature of the accounting transaction involved was in any way affected.

²⁰ *Id.* § 87. The full text of the statute was as follows:

Anything to the contrary in this chapter notwithstanding, the board of directors of a corporation shall never declare, nor shall a corporation pay, a cash dividend unless such dividend is out of the unreserved and unrestricted earned surplus only of such corporation and has been legally appropriated for the specific purpose of paying dividends; provided further, that no such dividend shall be declared or paid when the corporation is insolvent or when the payment thereof would render the corporation insolvent or when such payment would

detail in Part One, the full import of this additional restriction, particularly on the ability of a corporation to make *cash* distributions from capital surplus, has never been clear.²¹ Unless one were willing to rely upon the frankly artificial bifurcation of "dividends" and "distributions,"²² the Old MBCA made any such cash distributions of dubious legality.²³

The drafters of the RMA recognized the irrationality of the earned surplus test as a device for protecting creditors and senior security holders from payments to junior security holders. Thus, in addition to eliminating the concepts of stated capital and par value, they subjected distributions to shareholders to the sole restriction of insolvency,²⁴ at the same time consolidating under the classification "distributions" transactions previously denominated as dividends, distributions, share repurchases, redemptions, and distributions in liquidation.

Thus, under section 1.40 of the New MBCA, a "distribution" is defined as "a direct or indirect transfer of money or other property (except its own shares) or incurrence of indebtedness by a corporation to or for the benefit of its shareholders," and may take the form of "a declaration or payment of a divi-

be contrary to any provisions in the articles of incorporation. Nothing in this chapter shall impair or prevent a legal distribution to shareholders upon liquidation or dissolution as provided in this chapter.

Id.

²¹ See Hodge & Perry, *supra* note 9, at 377-79.

²² See note 19 *supra*.

²³ The statute could be circumvented, however, either by a redemption of stock out of capital surplus, or possibly by a property (in kind) distribution. See Hodge & Perry, *supra* note 9, at 378-79.

²⁴ See 1 MODEL BUSINESS CORP. ACT ANN. 484 (3d ed. 1985) (annotation notes that insolvency restriction was significant limitation on distributions); *Financial Provisions*, *supra* note 13, at 1867-68 (supporting adoption of more rigid stated capital requirements).

It should be noted that this response to the inadequacy of stated capital provisions is not an inevitable one; arguments have been advanced that the proper approach would be the adoption of a more realistic minimum amount of stated capital which could not be reduced. See, e.g., Note, *The Inadequacy of Stated Capital Requirements*, 40 U. CIN. L. REV. 823, 841 (1971) (article uses trust fund theory approach to justify increased stated capital requirements). In effect this adopts the "trust fund" concept of *Wood v. Dummer*, 30 F. Cas. 435 (No. 17,944)(C.C.D. Me. 1824). The logistical difficulties in both formulating that "realistic" amount and in policing its maintenance make this a somewhat utopian proposal.

dend; a purchase, redemption or other acquisition of shares; a distribution of indebtedness; or otherwise."²⁵

The heart of the financial provisions, however, is section 6.40. Under subsection (a), the board may authorize and the corporation may make distributions to shareholders subject only to the restrictions of the articles (if any) and of subsection (c). The statutory restriction adopts the twofold standard of equity and balance sheet solvency.²⁶ Thus, a distribution cannot be made if, after giving effect to it, the corporation cannot pay its debts as and when they became due (insolvency in the equity sense) or the corporation's total assets will be less than its total liabilities, together with the amount required to satisfy the liquidation rights of senior security holders (insolvency in the balance sheet sense).²⁷

The obvious merit of the new scheme is the flexibility it provides to corporate managers. Ironically, this flexibility may engender the criticism that the new system gives inadequate guidance to directors, many of whom (particularly in the closely-held corporation which is the norm in Mississippi) may lack the requisite financial sophistication to make the judgments that the statute demands.

Such criticisms are addressed only in part by the statute. Section 6.40(d) allows directors to rely upon financial statements prepared on the basis of accounting practices which are reasonable under the circumstances, on a fair valuation, or any other method reasonable under the circumstances.²⁸ The matter of

²⁵ New MBCA, *supra* note 1, § 1.40(6).

²⁶ See *Financial Provisions*, *supra* note 13, at 1868.

²⁷ See New MBCA, *supra* note 1, § 6.40(a),(c). Under the Old MBCA, "insolvency" meant only equity insolvency. See, e.g., Old MBCA, *supra* note 1, § 3(o).

It should be noted that § 6.40 of the RMA has already been subject to an official amendment regarding the determination of insolvency. Under that amendment, codified as § 6.40(g), any indebtedness which by its terms can only be repaid to the extent that a distribution could be made is not treated as a liability under § 6.40(c). See Committee on Corporate Laws, *Changes in the Model Business Corporation Act - Amendments Pertaining to Distributions*, 42 BUS. LAW. 259 (1986), 42 BUS. LAW. 1207 (1987) (amendments and comments). This amendment was adopted in Mississippi in 1988. MISS. CODE ANN. § 79-4-6.40(g)(Supp. 1988).

²⁸ This terminology deliberately omits reference to technical accounting jargon and specific concepts such as "generally accepted accounting principles." REVISED MODEL BUSINESS CORP. ACT § 6.40 Official Comment 4 (1984).

timing is governed by subsection (e), under which the effect of a distribution is determined in most cases as of the date of authorization, or the date of payment if more than 120 days after authorization.²⁹ In all other respects the statute is silent as to factors that should guide the board's determination of whether solvency (particularly in the equity sense) will be impaired; due to the absence of any substantial case authority, the Official Comments to the RMA provide the only persuasive guidance on this issue.³⁰ In any event, while under new section 8.33, adopted in 1988, consenting directors are expressly subjected to personal liability for illegal distributions, that liability is enforced only to the extent that the director's conduct violates the duty of care embodied in section 8.30 of the New MBCA and is not shielded by the business judgment rule.³¹ Thus, most misjudgments will

²⁹ See New MBCA, *supra*, 1, § 6.40(e)(3). Special rules are stated for distributions by purchase, redemption or other acquisition of shares, in which case the operative date is the earlier of the date money or property is transferred or debt is incurred, or the date the shareholder ceases to be a shareholder with respect to the acquired shares; and for other distributions of indebtedness, in which case the operative date is the date of distribution. *Id.* § 6.40(e)(1)-(2). This provision resolves the conflict posed in cases such as *Williams v. Nevelow*, 513 S.W. 2d 535 (Tex. 1974), in which the court held that for a corporation repurchasing shares in exchange for an installment promissory note, solvency was to be determined as of the time of the issuance of the debt instrument, not as of the time of each subsequent installment payment on the debt. The New MBCA embraces the rule of *Williams*.

³⁰ REVISED MODEL BUSINESS CORP. ACT § 6.40 Official Comment 2 (1984). The comments state that decisions involving equity insolvency should be "based on a cash flow analysis that is itself based on a business forecast and budget for a sufficient period of time to permit a conclusion that known obligations of a corporation can reasonably be expected to be satisfied over the period of time that they will mature." *Id.* Reliance solely upon a comparison of current assets to current liabilities, or of the present liquidation value of assets to existing liabilities, is eschewed. *Id.* In any event, the same decisions were required under the Old MBCA, which adopted the equity insolvency test. Old MBCA, *supra* note 1, § 3(o).

³¹ MISS. CODE ANN. § 79-4-8.33 (Supp. 1988). The same result would have obtained under the New MBCA as originally enacted. See *Financial Provisions*, *supra* note 13, at 1882. The new statute adds express rights of contribution against other culpable directors and shareholders who accepted the distribution knowing of the violation (which includes violations of the articles). *Id.* § 79-4-8.33(b). Any action must be commenced within two years of the date determined by § 6.40(c) or (g). *Id.* § 79-4-8.33(c).

Section 8.30 of the New MBCA is identical to its counterpart in the RMA; for an extensive discussion of those provisions and the related business judgment rule, see *Part One*, *supra* note 3, at 188-202. Of course, any decision tainted by self-dealing would be outside of the protection afforded by § 8.30.

not be actionable.

B. Shares

Corresponding to the changes involving par value and related concepts, the New MBCA differs substantially from its predecessor in its treatment of authorized shares. The New MBCA contains no reference to the traditional classification of "common" and "preferred" shares. Rather, the statute mandates only that there be at least one class of stock with unlimited voting rights, and at least one class of stock which is entitled to receive the net assets of the corporation in dissolution.³² If more than one class of stock is authorized then the articles must prescribe a distinguishing designation for shares (which, presumably, could include the terms common or preferred) but no legal significance is attached to the nomenclature used.³³ Rather, of paramount importance under the New MBCA is the *statement* of preferences, limitations and relative rights contained in the articles — in the words of the Official Comments to the RMA, the "contract" between the owners of these shares and the corporation with respect to their interests.³⁴ Except as permitted for series of shares all shares of a class must have identical rights.³⁵ As under the Old MBCA provisions on preferred stock, the variable rights and preferences permitted by the statute (which declares itself nonexclusive) include voting rights,³⁶ re-

³² New MBCA, *supra* note 1, § 6.01(b). Of course these rights may be consolidated in one class.

³³ *Id.* § 6.01(a). A possible exception to this is suggested by the RMA Comments, which state that if the fundamental rights of voting and residual equity interest are reposed in a single class of stock, that class may be described as simply "common shares." REVISED MODEL BUSINESS CORP. ACT § 6.01 Official Comment 1 (1984).

³⁴ REVISED MODEL BUSINESS CORP. ACT §6.01 Official Comment 1 (1984).

³⁵ *See* New MBCA, *supra* note 1, § 6.01(a).

³⁶ *Id.* § 6.01(c)(1). It should be noted that, as originally adopted, the New MBCA would not have permitted nonvoting common stock, pursuant to the mandate of Miss. CONST. art. 7, § 194. On November 10, 1987, the electorate approved Senate Concurrent Resolution No. 550 of the 1987 Regular Session of the Mississippi Legislature which repealed § 194. The original language of the New MBCA made nonvoting common stock permissible unless prohibited by § 194. New MBCA, *supra*, note 1, § 6.01(c)(1). The 1988 amendments to the New MBCA now simply sanction nonvoting shares generally. Miss. CODE ANN. § 79-4-6.01(c)(1) (Supp. 1988).

demption or conversion features,³⁷ and dividend and liquidation preferences.³⁸ As was true under the Old MBCA,³⁹ the new statute provides for the issuance of classes of shares in series (so-called "blank stock") under which the board of directors, if so authorized by the articles of incorporation, can define the precise terms of each series by appropriate amendment to the articles at the time of issuance.⁴⁰

As under the former statute,⁴¹ the New MBCA permits the issuance of fractional shares or scrip.⁴² Holders of fractional shares have voting and proprietary rights; holders of scrip do not in the absence of contrary provision. The major innovation in the new law is that the board is now given the option of paying a shareholder the monetary value of fractional shares, or to "arrange for disposition of fractional shares," in addition to the issuance of fractional shares or scrip.⁴³

As previously noted,⁴⁴ among the traditional corporate law notions abandoned by the New MBCA is that of treasury shares.⁴⁵ The drafters of the RMA concluded that the distinction between treasury shares and authorized but unissued shares was both unnecessary and, from many perspectives, undesir-

³⁷ *Id.* § 6.01(c)(2). The New MBCA changes existing law in this regard in one significant respect. Under the Old MBCA the right to redeem shares was limited to the option of the corporation. Old MBCA, *supra* note 1, § 27(a). Under the New MBCA redemption may be authorized at the option of the shareholder, another person, or upon the occurrence of a designated condition. New MBCA *supra* note 1, § 6.01(c)(2). Moreover, the Price at which conversion or redemption is to occur may either be fixed by the articles, or may be determined by the use of a designated formula or by reference to extrinsic data or sources. *Id.* at § 6.01(c)(1-2).

³⁸ See New MBCA, *supra* note 1, § 6.01(c)(3), (4).

³⁹ See Old MBCA, *supra* note 1, § 29.

⁴⁰ See New MBCA, *supra* note 1, § 6.02. In this fashion, the board "fills in the blanks" in previously authorized shares. Such amendments require no shareholder action. *Id.* at § 6.02(d)(4).

⁴¹ See Old MBCA, *supra* note 1, § 45.

⁴² See New MBCA, *supra* note 1, § 6.04.

⁴³ *Id.* § 6.04(a)(1),(2). The "cash out" option is frequently employed in "going private" transactions. REVISED MODEL BUSINESS CORP. ACT § 6.04 Official Comment (1984).

⁴⁴ See *supra* text accompanying notes 6 and 7.

⁴⁵ See Old MBCA *supra* note 1, § 3(i). Those shares that were issued but reacquired by the corporation, and were held by the corporation rather than being cancelled or restored to the status of authorized but unissued shares were considered issued but not outstanding. *Id.* See also New MBCA, *supra* note 1, § 6.01(2).

able.⁴⁶ Thus, under the New MBCA, shares acquired by the corporation are deemed to be authorized but unissued shares unless the articles prohibit their reissuance; in that event they are cancelled, and the statute permits the directors to file without shareholder action an amendment to the articles reflecting the decrease in the number of authorized shares.⁴⁷ Since the economic effect of the transaction is essentially that of a distribution of corporate assets, any reacquisition is within the definition of distribution and subject to the restrictions of section 6.40.⁴⁸

Together with the elimination of par value, stated capital and surplus, the New MBCA substantially modifies the rules involving the consideration for issuance of shares and its allocation. The Old MBCA, like most traditional statutes, limited the permissible consideration for shares to money, tangible or intangible property, or services actually performed; promissory notes were specifically prohibited. The judgment of the board as to the value of consideration received was conclusive absent fraud.⁴⁹

Substantially greater flexibility is provided under the new act, which adds promissory notes, contracts for future services, and other securities of the corporation to the roster of eligible forms of consideration.⁵⁰ The board is required to determine the

⁴⁶ REVISED MODEL BUSINESS CORP. ACT § 6.31 Official Comment (1984).

⁴⁷ See New MBCA, *supra* note 1, § 6.31.

⁴⁸ See New MBCA, *supra* note 1, §§ 1.40(6), 6.40; REVISED MODEL BUSINESS CORP. ACT § 6.31 Official Comment (1984). See also *supra* notes 6, 28 and accompanying text. Under the Old MBCA shares could be repurchased only out of earned surplus, by article authorization or two-thirds approval of shareholders, or capital surplus. Old MBCA, *supra* note 1, § 9. Exceptions existed for purchases made to eliminate fractional shares, collecting or compromising debts, payments under dissenters' rights, and redemption or purchase to return redeemable shares. *Id.* § 9 (a-d). Under the New MBCA the twofold insolvency test would be the sole limitation on any reacquisition. See, e.g., New MBCA, *supra* note 1, § 6.40(c).

⁴⁹ See Old MBCA, *supra* note 1, § 35.

⁵⁰ See New MBCA, *supra* note 1, § 6.21(b). An exception was made in the 1987 act for transportation corporations, due to a constitutional limitation applicable to such entities for money, property actually received, or labor done (or in good faith agreed to be done). Miss. CONST. art. 7, § 195; New MBCA, *supra* note 1, § 6.21(F). Senate Concurrent Resolution No. 548 of the 1987 Regular Session of the Mississippi Legislature, repealing § 195, was approved by the electorate on November 10, 1987. An amendment was adopted in 1988 to the statute to remove the special rule stated in § 6.21. Miss. CODE ANN. § 79-4-6.21 (Supp. 1988). The statute provides for protective mechanisms, such as

value of consideration received or to be received but only for the purpose of determining that the shares are validly issued, fully paid and nonassessable; its determination is declared conclusive for these purposes.⁵¹ The "fraud" standard placed on the discretion of the board is eliminated; liability for improper issuance of shares is thus governed by the ordinary duty of care of section 8.30 and the conflict of interest provisions of section 8.31.⁵²

Due to the elimination of the par value and stated capital concepts, the board is no longer required to allocate consideration received for shares to "stated capital" and "surplus" accounts,⁵³ as was mandated by prior law.⁵⁴

As under prior law,⁵⁵ a shareholder's liability is limited to the agreed consideration under section 6.20 or as provided in a subscription agreement;⁵⁶ the new statute also expressly insulates shareholders from personal liability for corporate obligations except those for which his own conduct creates liability.⁵⁷

The New MBCA also makes an important change in prior law dealing with stock options. Under the Old MBCA any option issued as a means of compensation to directors, officers, employees or subsidiaries, not part of a general issuance to other share-

deposit of shares in escrow, when shares are issued for notes or future services. *Id.* § 6.21(e).

⁵¹ *Id.* § 6.21(c),(d).

⁵² REVISED MODEL BUSINESS CORP. ACT § 6.21 Official Comment (1984).

⁵³ *Id.* Of course the statute does not prohibit the use of such categories as an accounting matter, if the board desires. *Id.*

⁵⁴ See Old MBCA, *supra* note 1, § 39.

⁵⁵ *Id.* § 47.

⁵⁶ New MBCA, *supra* note 1, § 6.20. These provisions do not substantially deviate from the prior statute. See Old MBCA, *supra* note 1, § 31.

⁵⁷ See New MBCA, *supra* note 1, § 6.22. The statute does permit, however, the imposition of such liability by a provision in the articles. *Id.* §§ 2.02(b)(2)(v), 6.22(b).

The New MBCA, then, eliminates any potential for "watered stock" liability based solely upon the issuance of shares below an artificially determined price. Rather, problems of overreaching, unfairness or unequal treatment are now placed under the broader penumbra of the board's fiduciary obligations. See REVISED MODEL BUSINESS CORP. ACT. § 6.21 Official Comment (1984); *Financial Provisions*, *supra* note 13, at 1879.

A special rule permits the issuance of shares to existing shareholders without consideration (*i.e.*, as a stock dividend or stock split) so long as this is done on a pro rata basis, and such issuance does not dilute the interests of a class of stockholders without their approval. See, *e.g.*, New MBCA, *supra* note 1, § 6.23(a)(b).

It should be noted that, in all events, the sole power to issue stock can be reserved to the shareholders in the articles. *Id.* § 6.21(a).

holders, required the approval of a majority of shareholders.⁵⁸ This provision was an indefensible restriction on the board's discretion, given the widespread acceptance of incentive compensation plans, and extrinsic rules requiring their disclosure in most public companies.⁵⁹ Thus the New MBCA deletes the requirement of shareholder approval altogether, rendering the matter one of business judgment and fiduciary duty of the board.⁶⁰

C. Preemptive Rights

As under prior law,⁶¹ the New MBCA makes preemptive rights⁶² elective; that is, they do not exist unless so provided in the articles.⁶³ The Old MBCA did not, however, address the content of preemptive rights if only the mere election to provide them was made; with little Mississippi case law to consult for guidance one would have to divine the effect of the grant of "preemptive rights" from other common law authority.⁶⁴ Section 6.30 of New MBCA, which statutorily defines the presumptive effect of preemptive rights, is arguably an improvement over the silence of its predecessor. However, it erects traps for the unwary that should be carefully scrutinized by planners.

Specifically, under the New MBCA, a statement that the corporation elects preemptive rights, without any express provision to the contrary, will not entitle shareholders to exercise pre-

⁵⁸ See Old MBCA, *supra* note 1, § 37.

⁵⁹ See 17 C.F.R. § 240.14a-101 (1987)(disclosure of compensation plans in proxy statements of corporations registered under § 12(g) of Securities Exchange Act of 1934).

Moreover, as the comments to the RMA point out, approval may be required by stock exchange rules. REVISED MODEL BUSINESS CORP. ACT § 6.24 Official Comment (1984).

⁶⁰ See New MBCA, *supra* note 1, § 6.24.

⁶¹ See Old MBCA, *supra* note 1, § 49.

⁶² *I.e.*, the right of existing shareholders to acquire their proportionate share of any new issuance of stock before sales to others. H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS § 174 (2d ed. 1983) [hereinafter HENN & ALEXANDER]. See New MBCA, *supra* note 1, § 6.30.

⁶³ See New MBCA, *supra* note 1, § 6.30.

⁶⁴ The generally accepted view was that preemptive rights did not attach to treasury shares, shares issued for non-cash consideration, or shares issued in connection with a merger or consolidation; a split of authority existed as to whether they applied to originally authorized but unissued shares. See HENN & ALEXANDER, *supra* note 62, § 174, at 439-40.

emptive rights with respect to (a) shares issued as compensation to directors, officers, agents, employees, subsidiaries or affiliates, or to satisfy conversion or option rights created as compensation to any of those persons; (b) originally authorized shares issued within six months of incorporation; and (c) shares issued for consideration other than money (*e.g.*, property or services).⁶⁵ Moreover, preemptive rights are denied to shares with limited voting rights but preferential distribution rights; shares with general voting rights but no preferences have no rights to shares with preferences unless those shares are convertible into shares without preferences.⁶⁶ Finally, if shares subject to preemptive rights are not acquired by shareholders, they can be offered to third parties for a period of one year at a price not less than that at which they were offered to the shareholder; an offer at a lower price or after one year again invokes the preemptive right.⁶⁷

Preemptive rights generally are not utilized in the public corporation arena but are frequently encountered as a protective device for minority shareholders in closely-held corporations.⁶⁸ This being the case, it must be noted that the New MBCA creates various avenues whereby a majority interest can effectively avoid the right—for example, by issuing shares as compensation to a majority director or officer or by issuing shares for property or services. While any such action taken as an oppressive measure could trigger liability for breach of fiduciary duty,⁶⁹ lengthy and expensive litigation may be necessary on the shareholder's part to assert the right to maintain his proportionate position. Thus, planners representing minority shareholders should con-

⁶⁵ See New MBCA, *supra* note 1, § 6.30 (b)(3).

⁶⁶ *Id.* § 6.30(b)(4)-(5).

⁶⁷ *Id.* § 6.30(b)(6). It should also be noted that preemptive rights can be waived without consideration. *Id.* § 6.30(b)(2).

⁶⁸ R. CLARK, CORPORATE LAW § 17.1.4 (1986) [hereinafter CLARK].

⁶⁹ See *Katzowitz v. Sidler*, 24 N.Y.2d 512, 515, 249 N.E.2d 359, 364, 301 N.Y.S.2d 470, 477 (1969) (offer of shares at 1/18 of book value without valid business purpose and with intent to dilute interest of dissenting shareholder held breach of fiduciary duty). *But cf. Masure v. Osborne*, 388 Pa. 121, 130 A.2d 157, 159 (1957) (book value not conclusive of market value; offer to plaintiff was prima facie evidence of good faith). Of course, preemptive rights often give a minority shareholder nothing more than the option of throwing his money down a bottomless well; thus other structural protections should be considered by representatives of such interests.

sider the inclusion of appropriate provisions in the articles to broaden the scope of preemptive rights and narrow the statutory loopholes.

II. SHAREHOLDER LITIGATION

Prior Mississippi law contained only one brief statutory reference and virtually no case authority⁷⁰ on the subject of shareholders' derivative actions.⁷¹ The only reference in the Old MBCA was section 93, which incorporated the contemporaneous ownership requirement, *i.e.*, that only one who was a shareholder at the time the challenged transaction took place could file a derivative suit.⁷² The statute's silence was particularly maddening since the Mississippi Rules of Civil Procedure failed to adopt Rule 23.1 of the Federal Rules of Civil Procedure dealing with derivative actions.⁷³ Thus the New MBCA provisions on derivative suits bring welcome clarification to this area of Mississippi law; nonetheless it is only fair to say that the new statute leaves unanswered a number of significant questions.

Section 7.40 of the New MBCA was adopted without change from the RMA. Two prerequisites exist to maintaining a derivative action: first, as under the prior statute, the plaintiff must have been a shareholder (either of record or beneficial owner) as

⁷⁰ The sole annotated case is *Liberty Sav. & Loan Ass'n v. Mitchell*, 398 So. 2d 208 (Miss. 1981), which while derivative in nature involved no typical derivative action issues. Of course such a dearth of case authority on corporate issues in Mississippi is hardly unique. See *Part One, supra* 3, at 168.

⁷¹ For useful general background, see CLARK, *supra* note 68, §§ 15.1 - 15.10. See also HENN & ALEXANDER, *supra* note 62 § 358-81.

⁷² The text of the statute read as follows:

No action shall be brought in this state by a shareholder in the right of a domestic or foreign corporation unless the plaintiff was a holder of shares or of voting trust certificates therefor at the time of the transaction of which he complains, or his shares or voting trust certificates thereafter devolved upon him by operation of law from a person who was a holder at such time.

Old MBCA, *supra* note 1, § 93. In contrast, the 1969 Model Act also provided for (1) payment to the defendant by plaintiff of reasonable expenses upon final judgment and a finding that the action was brought without reasonable cause, and (2) security for expenses. MODEL BUSINESS CORP. ACT § 49 (1969). For a detailed discussion of the contemporaneous ownership requirement, see Harbrecht, *The Contemporaneous Ownership Rule in Shareholders' Derivative Suits*, 25 UCLA L. REV. 1041 (1978).

⁷³ FED. R. CIV. P. 23.1. Since the federal rule would apply in the federal courts of Mississippi, it was, however, the most likely authority to be applied by analogy.

of the time of the challenged transaction or have received his shares by operation of law from such an owner⁷⁴; and second, the complaint, which must be verified,⁷⁵ must allege with particularity those efforts made to obtain action by the board and their refusal to act, or why the failure to take such action should be excused.⁷⁶ Like most statutes, however, the New MBCA is unfortunately silent on the issue of what *constitutes* "demand futility," a matter on which a substantial body of often contradictory case law exists.⁷⁷ The new statute empowers the court to stay any action pending an investigation by the corporation.⁷⁸

A matter of great practical significance to shareholders' attorneys is that the New MBCA, unlike the statutes of several major states,⁷⁹ makes no provision for security for expenses as a prerequisite to suit.⁸⁰ Rather, abusive or vexatious litigation is deterred by the potential for an award of the defendant's reasonable expenses, including attorneys' fees, if the court on termination (not "final judgment") finds that the suit was brought

⁷⁴ See New MBCA, *supra* note 1, § 7.40 (a), (e).

⁷⁵ *Id.* § 7.40(b). This requirement, imported from Fed. R. Civ. P. 23.1, has been held to require only that the plaintiff have a good faith belief in the accuracy of the allegations made, notwithstanding his failure to understand the complaint. *Surowitz v. Hilton Hotels Corp.*, 383 U.S. 363, 373 (1966), *reh. denied*, 384 U.S. 915 (1966).

⁷⁶ See New MBCA, *supra* note 1, § 7.40(b). Unlike the Federal Rules, no reference is made to necessity for demand on *shareholders*, a prerequisite applied in a few jurisdictions. See, e.g., *Solomon & Sons Trust, Inc. v. New England Theatres Operating Corp.*, 93 N.E.2d 241, 248 (Mass. 1950) (if demand on officer fails, then other shareholders must be served demand). The Federal Rules require such demand only "if necessary," presumably under the substantive law of the state, and like the RMA most modern statutes adopt no such requirement. A collection of cases on the issue may be found at 2 REVISED MODEL BUSINESS CORP. ACT ANN. 741-43 (3rd ed. 1985).

⁷⁷ For a useful summary of recent cases on point, see 2 REVISED MODEL BUSINESS CORP. ACT ANN. 737-41 (3d ed. 1985).

⁷⁸ See New MBCA, *supra* note 1, § 7.40 (b).

⁷⁹ See, e.g., CAL. CORP. CODE § 800(c)-(f) (West 1977 & Supp. 1987) (motion for security allowed if no benefit to corporation or shareholders, or if moving party was not participant in transaction); N.Y. BUS. CORP. LAW § 627 (McKinney 1986) (corporation entitled to security from plaintiffs). Currently eighteen states have such statutes. 2 REVISED MODEL BUSINESS CORP. ACT ANN. 728 (3d. 1985). On the other hand, the Illinois Business Corporation Act of 1983 makes no such provision. ILL. REV. STAT. Ch. 32, § 7.80 (1985).

⁸⁰ The drafters of the RMA took the position that such requirements discriminate unfairly against the small shareholder and are inconsistent with other types of corporate actions (e.g., antitrust and class actions) that involve substantial litigation expense but impose no similar impediment. REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 1(h) (1984).

without reasonable cause.⁸¹

As is true of most derivative action statutes,⁸² the New MBCA provides that such suits cannot be discontinued or settled without court approval. Notice of any settlement or discontinuance, if approved, must be given to the shareholders if the court determines that their interests will be substantially affected.⁸³

Perhaps the most troublesome omission in the New MBCA (as in its source, the RMA) is the failure to deal with the effect of a determination by the board of directors, or a special litigation committee appointed by the board, that the pursuit of a derivative claim is against the best interest of the corporation. Substantial variance in approach to this issue exists among recent cases. The New York rule, established by *Auerbach v. Bennett*,⁸⁴ is that the trier of fact may examine the independence, good faith, and diligence of the body recommending dismissal; beyond this, the court will not second guess the merits of the recommendation but will apply the business judgment rule. A more complex approach is taken in Delaware where, under *Zapata Corporation v. Maldonado*,⁸⁵ the court is to apply a two-

⁸¹ See New MBCA *supra* note 1, § 7.40 (d). The comments to the RMA state that it was deemed unnecessary to make reference to an award of attorney's fees to a successful plaintiff, in light of the universal recognition of this right both legislatively and judicially. REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 1(i) (1984).

⁸² See FED. R. CIV. P. 23.1 (court approval necessary for settlement); 2 REVISED MODEL BUSINESS CORP. ACT ANN. 727 (3d ed. 1985) (no compromise allowed without court approval).

⁸³ See New MBCA, *supra* note 1, § 7.40 (c). The statute does not prescribe who is to bear the expense of such notice (which, obviously, could be considerable); the comments to the RMA state that this is discretionary with the court. REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 1(i) (1984).

⁸⁴ 47 N.Y. 2d 619, 633, 419 N.Y.S.2d 920, 928, 393 N.E.2d 994, 1002 (1979).

⁸⁵ 430 A.2d 779 (Del. 1981). The significance of *Zapata* has, however, been undercut by two subsequent decisions. In *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984), the court held in effect that demand on directors should be excused only where, under the particular facts alleged by the plaintiff, a reasonable doubt exists as to the independence of the directors and the fact that the decision would be upheld by the business judgment rule. *Id.* at 814. See Recent Decisions, *Corporations — Derivative Action — Demand Futility is Achieved by the Creation of a Reasonable Doubt of Directorial Disinterest Through Allegations of Factual Particularity*, 55 Miss. L.J. 181, 194 (1985) (discussing *Aronson* decision). Moreover, in *Kaplan v. Wyatt*, 499 A.2d 1184 (Del. 1985), the court upheld a decision by the trial judge to forego application of the second tier "independent business judgment" review of *Zapata*, emphasizing that this step was purely discretionary. 499

step process. First, the court must review the good faith and independence of the decisionmaker and the factual bases underlying its recommendation, as to which the corporation has the burden of proof. Secondly, assuming that the corporation meets this burden, the court is to determine by applying its own business judgment whether a motion to dismiss should be granted.⁶⁶

The drafters of the RMA simply sidestepped the issue, noting only that the law was "in state of flux" and should be allowed to develop judicially, with the possibility of an appropriate amendment to the RMA at a later date.⁶⁷ Since the resolution of this question may as a practical matter be the most significant issue in many derivative actions, I would urge the Mississippi Legislature to monitor closely the progress of the RMA in this regard and to consider the early adoption of an amendment to section 7.40 of the New MBCA to provide a clear standard for our courts to apply.

III. ORGANIC CHANGES

The New MBCA substantially alters existing laws in the area of fundamental corporate changes. Those matters will be

A.2d at 1192.

⁶⁶ *Accord*, *Joy v. North*, 692 F.2d 880, 888-89 (2d Cir. 1982), *cert. denied*, 460 U.S. 1051 (1983) (business judgment rule does not apply when special litigation committee recommends dismissal of shareholder's derivative suit). For additional background see, e.g., Block & Prussin, *Termination of Derivative Suits Against Directors on Business Judgment Grounds: From Zapata to Aronson*, 39 BUS. LAW. 1503, 1505-07 (1984) (only excused when board is extremely self-interested); Block & Prussin, *The Business Judgment Rule and Shareholder Derivative Actions: Viva Zapata?*, 37 BUS. LAW. 27, 35 (general discussion of demand requirement); Brown, *Shareholder Derivative Litigation and the Special Litigation Committee*, 43 U. PITT. L. REV. 601, 610-19 (1982) (examination of shareholder demand rule before Aronson); Chittur, *Ventriloquism For Corporate Directors to Terminate Shareholder Litigation: The Death of the Derivative Suit*, 75 NW. U.L. REV. 96, 98-124 (1980) (emphasis on Auerbach and relative positions of directors, shareholders and litigation committees); Note, *Special Litigation Committees: An Unwelcome Solution to Shareholders Demands*, 1981 U. ILL. L. REV. 485, 493-97 (examination of business judgment rule and demand requirements with thorough analysis of relevant case law).

Yet another position was taken in *Miller v. Register & Tribune Syndicate, Inc.*, 336 N.W. 2d 709 (Iowa 1983), which refused to recognize a board-appointed committee but suggested that the court itself might appoint a committee of disinterested and experienced persons to make a recommendation on the issue. *Id.*

⁶⁷ REVISED MODEL BUSINESS CORP. ACT § 7.40 Official Comment 2(a) (1984).

discussed here under the classifications of amendments to the articles, sales of assets, corporate combinations, dissolution, and dissenters' rights.

A. *Amendments to the Articles and Bylaws*

In most respects, the New MBCA does not differ markedly from the provisions of the Old MBCA.⁸⁸ As under the prior law, the articles can be amended to include any provision which would have been permissible in the original articles. In lieu of an illustrative list of allowable amendments the new statute merely states that existing shareholders have no property right in any provision of the articles.⁸⁹ One innovation of the New MBCA is a list of certain essentially technical amendments which can be made by the directors without shareholder action.⁹⁰ Among these is one of significance to all Mississippi corporate practitioners: *i.e.*, an amendment to extend the corporation's duration if incorporated at a time when limited duration was required by law.⁹¹ Now that the Mississippi Constitution has been amended to delete the ninety-nine year limitation on corporate life,⁹² counsel should avail themselves of this opportunity to obtain the privilege of perpetual existence.⁹³

The procedure for other article amendments is much the same as the old statute: proposal by the directors and approval by the shareholders at a meeting called for that purpose.⁹⁴ The

⁸⁸ See generally Old MBCA, *supra* note 1, §§ 115-129.

⁸⁹ See New MBCA, *supra* note, 1, § 10.01. Thus the statute rejects the "vested rights" theory which some courts extrapolated from *Trustees of Dartmouth College v. Woodward*, 17 U.S. (4 Wheat.) 518 (1819), requiring unanimous shareholder consent for any article amendment. For background on this problem, see 3 REVISED MODEL BUSINESS CORP. ACT ANN. 1150-51 (3d ed. 1985); HENN & ALEXANDER, *supra* note 62, § 340, at 951-55. In any event the vested rights theory was constitutionally rejected in Mississippi. See MISS. CONST. art. 7, § 178.

⁹⁰ See New MBCA, *supra* note 1, § 10.02.

⁹¹ *Id.* § 10.02(1).

⁹² 1987 Miss. Senate Concurrent Resolution No. 549, *amending* MISS. CONST. art. 7, § 178 (approved by the electorate November 10, 1987). This restriction was codified in Old MBCA, *supra* note 1, § 109. See also *Part One*, *supra* note 3, at 172 n. 27.

⁹³ Appropriate amendments to New MBCA § 3.02 and § 10.02 were enacted in 1988. MISS. CODE ANN. §§ 79-4-3.02, -10.02(1)(Supp. 1988).

⁹⁴ See New MBCA, *supra* note 1, § 10.03. The directors are called upon to "recommend" the amendment to the shareholders unless precluded from this by a conflict of

major substantive deviation from prior law is that in the absence of a contrary provision in the articles requiring a greater vote, approval of the amendment requires only the vote of a *majority*, rather than two-thirds, of the votes of each voting group⁹⁵ entitled to vote thereon.⁹⁶ The statute actually imposes a two-fold test: if the amendment would not trigger dissenters' rights, then an affirmative majority of votes cast at a meeting where a quorum was present would suffice;⁹⁷ however, as to any voting group for whom the amendment invokes dissenters' rights, a majority of the outstanding shares of that group is also needed for approval.⁹⁸

As under prior law, the concept of class voting on amendments is preserved although under the designation of votes by voting groups. This right is extended to shares with no general voting rights if the rights of such shares would be affected in one of nine enumerated ways.⁹⁹

The amendment once approved is effected by filing articles of amendment with the Secretary of State, including prescribed information concerning the text of the amendment and the vote thereon. Consistent with the approach taken under the New MBCA generally, the formal issuance of a "certificate of amendment" is eliminated.¹⁰⁰ Also as under prior law, the board can restate the corporation's articles without shareholder action,¹⁰¹

interest or "other special circumstances" which must be communicated to the shareholders. The board may also condition its submission "on any basis." *Id.* § 10.03 (b)-(c).

Prior to the issuance of shares either the board or incorporators have plenary power to amend the articles. *Id.* § 10.05.

⁹⁵ The concept of voting groups is discussed in *Part One, supra* note 3, at 235-36.

⁹⁶ See New MBCA, *supra* note 1, § 10.03(e). The statute also allows the board to alter the ordinary voting rights of shareholders by appropriately conditioning its submission to the shareholders. *Id.* § 10.03(c). See also REVISED MODEL BUSINESS CORP. ACT § 10.03 Official Comment (1984)(examples of conditions commonly imposed in order for amendment approval).

⁹⁷ This is the customary requirement for effective shareholder action, and treats abstentions as such, not as negative votes. See *Part One, supra* note 3, at 233-34 (majority of votes cast is sufficient to indicate shareholder approval).

⁹⁸ See New MBCA, *supra* note 1, § 10.03(e).

⁹⁹ *Id.* § 10.04.

¹⁰⁰ See New MBCA, *supra* note 1, §§ 1.25(b), 2.03; *Part One, supra* note 3, at 173.

¹⁰¹ See New MBCA, *supra* note 1, § 10.07. This presupposes, of course, that the restatement contains no changes not previously approved by the shareholders; in such event shareholder approval must to that extent be obtained. *Id.* § 10.07(b).

and amendments pursuant to federal bankruptcy reorganization proceedings require neither board nor shareholder action.¹⁰²

The provisions of the New MBCA on bylaw amendments are substantially more detailed than those of the previous statute and make at least one substantive change. Under the Old MBCA, the power to adopt or amend bylaws rested exclusively with the board absent a provision in the articles which "reserved" such power to shareholders.¹⁰³ Conversely, under the new statute the power to amend or repeal bylaws is essentially coterminous between the board and stockholders. Indeed, the New MBCA actually shifts the balance in favor of the shareholders since the board's power may be limited either by an exclusive reservation in the articles to the shareholders, or by a statement in any action by the shareholders amending or repealing a bylaw which provides that the board may not thereafter amend or repeal it.¹⁰⁴

Unlike the prior law, the New MBCA deals expressly with supermajority provisions for both shareholders and directors. If authorized by the articles, shareholders may adopt or amend bylaws providing for a greater vote or quorum requirement than imposed by statute. Such action requires compliance with the greater of the existing or proposed requirements for quorum and votes. Any such bylaw cannot be adopted, amended or repealed by the board.¹⁰⁵ Bylaws dealing with supermajority requirements for the board are treated differently: if adopted by the shareholders, only they can amend; if by the directors, either the di-

¹⁰² *Id.* § 10.08.

¹⁰³ See Old MBCA, *supra* note 1, § 51.

¹⁰⁴ See New MBCA *supra* note 1, § 10.20. Presumably the initial bylaws would be adopted by the board absent contrary provision in the articles, although the act does not directly address this question.

While there was some split of authority, the prevailing view under statutes like the Old MBCA appeared to be that the shareholders retained inherent power to amend or repeal bylaws. See 3 REVISED MODEL BUSINESS CORP. ACT ANN. 1211-12 (3d 1985) (statutory and case law background of shareholders rights to repeal or amend bylaws); HENN & ALEXANDER, *supra* note 62, § 133, at 308 & nn. 11-12 (formulation of initial bylaws is power enjoyed in different jurisdictions by incorporators, shareholders or board). The New MBCA eliminates any ambiguity on this issue.

¹⁰⁵ See New MBCA, *supra* note 1, § 10.21. Thus, for example, any attempt by shareholders to amend an existing bylaw fixing a 75% vote requirement to reduce it to 50% would itself require a 75% affirmative vote.

rectors or shareholders can amend.¹⁰⁶

B. Sales of Assets

The Old MBCA followed the traditional statutory approach of requiring shareholder approval (by a two-thirds majority) of the "sale, lease, exchange, mortgage, pledge, or other disposition" of all or substantially all of a corporation's assets other than in the ordinary course of business.¹⁰⁷ The New MBCA changes this in three substantial respects.

First, the board is authorized to *mortgage* or otherwise encumber all or substantially all assets, either in or out of ordinary course of business, without shareholder action (unless required by the articles).¹⁰⁸ This is clearly a salutary change; matters of corporate financing (as opposed to the disposition of all or the bulk of a corporation's property) should appropriately be delegated to the board's discretion, subject only to the restrictions of the duties of care and loyalty.¹⁰⁹

Second, transfers to a wholly-owned subsidiary are not subject to shareholder approval.¹¹⁰

The third change, consistent with the general tenor of the New MBCA, is that for those transactions subject to shareholder approval, only a majority of votes entitled to be cast, rather than two-thirds, is required absent contrary provisions in the articles.¹¹¹

¹⁰⁶ *Id.* § 10.22(a). Consistent with the previous sections, such a bylaw adopted by the shareholders may contain a provision requiring a specified vote of either shareholders or directors for any change to be effective. In addition, any board action to change a supermajority bylaw provision must also comply with the greater of the existing or proposed standard. *Id.* § 10.22(b)-(c). See *supra* text accompanying note 105.

¹⁰⁷ Old MBCA, *supra* note 1, § 157. The converse, expressly provided in the statute, is that no such approval was required for transfers made in the "usual and regular course of business." *Id.* § 155.

¹⁰⁸ See New MBCA, *supra* note 1, § 12.01(a)(2), (b).

¹⁰⁹ The requirement of shareholder approval of mortgages of property seems particularly anomalous in view of the board's unrestricted power to *borrow* without shareholder action. See Hodge & Perry, *supra* note 9, at 384-85 (emphasizing expense and delay caused by requiring shareholder approval of mortgages). The requirement has been deleted from the Model Act since 1962. 3 REVISED MODEL BUSINESS CORP. ACT ANN. 1321 (3d ed. 1985).

¹¹⁰ See New MBCA, *supra* note 1, § 12.01 (a)(3).

¹¹¹ *Id.* § 12.02 (e). The procedure for authorizing sales or other dispositions not in

C. Mergers and Share Exchanges

The New MBCA makes a number of highly significant changes in current law dealing with corporate combinations: elimination of the concept of consolidations; introduction of cash mergers and share exchanges to Mississippi; and liberalization of the provisions on short-form mergers.

Chapter 11 of the New MBCA makes no mention of the consolidation procedure provided by the Old MBCA.¹¹² This is a rational omission: consolidations rarely occurred, since it is desired in most combination transactions that one of the constituents survive. In any event, the practical effect of a consolidation can be achieved by the simple expedient of forming a new corporation and merging the constituents into it.¹¹³

Of much greater practical importance is the availability of the cash merger as a means of eliminating shareholders from the combined business. Under the Old MBCA cash mergers were impermissible, since the general merger statute required that the plan of merger state the basis for "converting the shares of each merging corporation into *shares or other securities or obligations* of the surviving corporation or any other corporation."¹¹⁴ Thus, with the exception of short-form mergers of subsidiaries,¹¹⁵ a merger could not be used as a "cash-out" device in Mississippi. The New MBCA, however, allows the shares of the constituents to be converted as well "into cash or other property in whole or part."¹¹⁶ This gives management an enormous element

the regular course of business is essentially the same as for amendments to the articles, discussed at notes 97-99 *supra* and accompanying text. See New MBCA, *supra* note 1, § 12.02(f)-(g).

Two other features of the new law should be briefly noted. The first is that the board is empowered to abandon any transaction once approved without further shareholder action (without, of course, prejudicing any contractual rights of third parties). The other is that transactions which involve a transfer of assets but which actually serve the purpose of a distribution (*e.g.*, a "spin-off" or other divisive reorganization) are governed by the rules on distributions. *Id.* § 12.02(f)-(g).

¹¹² See Old MBCA, *supra* note 1, § 143. In a traditional consolidation, two or more corporations would combine to form a third, new corporation, *i.e.*, neither of the combining corporations would survive.

¹¹³ REVISED MODEL BUSINESS CORP. ACT Ch. 11, Introductory Comment (1984).

¹¹⁴ See Old MBCA, *supra* note 1, § 141(c)(emphasis added).

¹¹⁵ *Id.* § 149; see *infra* notes 128-29 and accompanying text.

¹¹⁶ See New MBCA, *supra* note 1, § 11.01(b)(3). Cash mergers were added to the

of flexibility in the merger process. However, it likewise injects into Mississippi law the highly volatile issue of whether a merger intended to freeze out minority shareholders may constitute a breach of fiduciary obligation by those in control.¹¹⁷ Since the statute permits this procedure it is obviously not automatically voidable; the appropriate standard of review is of course not addressed by the statute and will be a matter with which Mississippi courts will ultimately grapple.

Even more innovative is the New MBCA provision for share exchanges. This procedure, unknown to common law and traditional statutes, was added to the Model Act in 1976 in order to provide a direct means whereby a corporation being acquired does not disappear but becomes a subsidiary of the acquiring corporation.¹¹⁸ Under the Old MBCA this result could be accomplished only by the so-called reverse triangular merger: the acquiring corporation forms a subsidiary in which it places securities or cash; the subsidiary then merges with the target corporation, which receives securities or cash of the parent for its shares and ceases to exist.¹¹⁹ The Old MBCA authorized the

Model Act in the 1969 revision. See 2 MODEL BUSINESS CORP. ACT ANN. § 71(c) (2d ed. 1971) (examines allowance of cashout mergers); Garrett, *Merger Meets the Common Law*, 63 TEX. L. REV. 1509, 1515 (1985) [hereinafter Garrett] (discussion of impact of allowing cash out mergers).

¹¹⁷ A useful summary of the recent cases (mostly from Delaware) on this issue is found at 3 REVISED MODEL BUSINESS CORP. ACT ANN. 1261-67 (3d ed. 1985). For further background, see Herzel & Colling, *Establishing Procedural Fairness in Squeeze-Out Mergers After Weinberger v. UOP*, 39 BUS. LAW. 1525 (1984) (discussion of current state of procedural fairness standard); Berger & Allinham, *A New Light on Cash - Out Mergers: Weinberger Eclipses Singer*, 39 BUS. LAW. 1 (1984) (examination of evolution of courts' treatment of mergers); Fischel, *The "Race to the Bottom" Revisited: Reflections on Recent Developments in Delaware Corporation Law*, 76 NW. U.L. REV. 913 (1982) (recent Delaware cases expand ability of dissident shareholders to challenge mergers); Greene & Junewicz, *A Reappraisal of Current Regulation of Mergers and Acquisitions*, 132 U. PA. L. REV. 647 (1984) (general review of statutory and case law limitations); Comment, *Freezeouts Under the 1983 Illinois Business Corporation Act: The Need for Protection of Minority Shareholders From "Going Private" Transactions*, 1985 U. ILL. L. REV. 679 (1985) (limited protection available to minority shareholders).

¹¹⁸ See Garrett, *supra* note 116, at 1516. The equivalent of a share exchange has, of course, always been possible assuming the unanimous consent of the shareholders of the target corporation; the innovation of the new procedure is to permit this, like a merger, in the absence of unanimity.

¹¹⁹ For a somewhat more detailed description, see Norton, *The Acquisition Process and the Closely-Held Corporation: Selected Legal Aspects*, 36 MERCER L. REV. 567,577-

reverse triangular merger by permitting conversion of shares of the target into securities of "the surviving corporation or *any other corporation*."¹²⁰

Section 11.02 of the New MBCA again modernizes Mississippi law by providing a direct means to the same result: a plan of share exchange, whereby the shares of the target are exchanged for securities of the acquiring or any other corporation, or cash or other property.¹²¹ The exchange is subject to all of the procedural safeguards, including dissenters' rights, as a merger.¹²²

Procedurally, the plan of merger or share exchange, once adopted, is submitted either to the shareholders of both corporations (merger) or the acquired corporation (share exchange)¹²³ for approval.¹²⁴ Essentially the same steps for approval are required as apply to amendments of the articles, including majority vote rather than two-thirds as under the Old MBCA, and voting by voting groups under some circumstances.¹²⁵

The New MBCA diverges from prior law in specifying limited circumstances in which the shareholders of the surviving corporation need not approve a merger.¹²⁶ In effect it is a *de minimis* exception for instances in which the merger does not significantly affect the survivor's shareholders; *e.g.*, the articles of the survivor are not substantively changed, the shareholders of the survivor hold the identical number of shares as before the

78 (1985) [hereinafter Norton] (discussion of triangular mergers).

¹²⁰ Old MBCA, *supra* note 1, § 141(c)(emphasis added). As previously noted, however, cash was not a permissible item of exchange. See *supra* notes 114-15 and accompanying text.

¹²¹ See New MBCA, *supra* note 1, § 11.02 (b)(3).

¹²² The statute does not, of course, preclude the acquisition of another corporation's shares through a voluntary tender offer or other consensual transaction. *Id.* § 11.02(d).

For additional background on share exchanges, see Norton, *supra* note 119, at 581-82.

¹²³ Therein lies, obviously, one of the advantages of the share exchange: since the interests of the shareholders of the *acquiring* corporations are not directly affected, there is no necessity for their approval of the acquisition.

¹²⁴ See New MBCA, *supra* note 1, § 11.03 (outlining procedure for approval of merger or share exchange).

¹²⁵ *Id.* § 11.03(e)-(f). See *supra* notes 94-99 and accompanying text (procedure for article amendments).

¹²⁶ See New MBCA, *supra* note 1, § 11.03(g).

merger, and the shares issued as part of the merger do not increase the outstanding voting and participating shares of the survivor by more than twenty percent. While this avoids the necessity of a shareholder meeting for the survivor, it is probably of limited practical significance. A shareholder's meeting can, in any event, be avoided by a three-step transaction: the survivor can create a wholly-owned subsidiary; it can cause the subsidiary and target to merge; then, if desired, it can effect a short-form merger of the subsidiary without a shareholder vote.¹²⁷

As under the Old MBCA,¹²⁸ the new statute provides for the short-form merger of a substantially owned subsidiary without any shareholder action. The major change effected by the New MBCA is that the necessary ownership threshold is now ninety, rather than ninety-five, percent.¹²⁹

After approval of a plan of merger or share exchange by the shareholders (or by the directors alone if shareholder action is unnecessary) articles of merger or share exchange are filed with the Secretary of State.¹³⁰ Consistent with the general approach of the New MBCA, the articles are self-effectuating and no certificate of merger is issued by the Secretary.

The provisions of the New MBCA involving the effects of a merger or share exchange, and addressing combinations between domestic and foreign corporations, do not materially differ from the prior statute.¹³¹

D. Dissolution

The New MBCA provisions on dissolution do not, for the most part, differ significantly from the old statute.¹³² In a few

¹²⁷ See Murphy, *The New Virginia Stock Corporation Act: A Primer*, 20 U. RICH. L. REV. 67, 122 (1985) [hereinafter Murphy] (analyzing effect of not having shareholders meeting on merger or share exchange).

¹²⁸ See Old MBCA, *supra* note 1, § 149.

¹²⁹ See New MBCA, *supra* note 1, § 11.04.

¹³⁰ *Id.* § 11.05.

¹³¹ Compare Old MBCA, *supra* note 1, §§ 151, 153, with New MBCA, *supra* note 1, §§ 11.06, 11.07.

¹³² *E.g.*, plenary authority to effect a dissolution is still granted to incorporators or directors of a corporation which has not issued shares nor commenced business. Compare Old MBCA, *supra* note 1, § 163, with New MBCA, *supra* note 1, § 14.01. In addition, the provisions on judicial dissolution are not materially different. Compare Old

respects, however, the new act makes important changes in the prior law.

Regarding voluntary dissolution, the New MBCA alters present law in two ways. First, the New MBCA requires action of both directors and shareholder to effect dissolution of an organized corporation;¹³³ the former provision for dissolution by unanimous written consent of shareholders is now eliminated.¹³⁴ Thus, the formality of a board resolution will have to be observed in any dissolution of a corporation which has begun business or issued stock. Second, consistent with the preceding discussions, dissolution now requires the consent of only a bare majority of shares entitled to vote in the absence of a provision in the articles increasing the threshold;¹³⁵ the prior act, of course, required a two-thirds affirmative vote.¹³⁶

Procedurally, the separate steps of filing an intent to dissolve, followed by winding up of the corporate affairs and the filing of formal articles of dissolution,¹³⁷ are eliminated. Rather, after dissolution, articles of dissolution will now be filed with the Secretary of State, and the corporation will be deemed dissolved as of their effective date.¹³⁸ This, in turn, triggers the winding up and liquidation of its business and affairs, the procedure for which is outlined in section 14.05.¹³⁹ The most significant procedural changes are in the area of liabilities. More detail is now included involving notice to known creditors; this must be done in writing and allow not less than 120 days for the filing of a claim. Any such claim will be barred if the claimant fails to respond or to file an action to enforce a claim within 90 days of its

MBCA, *supra* note 1, §§ 193, 195, with New MBCA, *supra* note 1, §§ 14.30, 14.31.

¹³³ See New MBCA, *supra* note 1, § 14.02.

¹³⁴ See Old MBCA, *supra* note 1, § 165.

¹³⁵ See New MBCA, *supra* note 1, § 14.02(e). The board can also increase the required vote by so conditioning its submission to shareholders. *Id.* § 14.02(c).

¹³⁶ See Old MBCA, *supra* note 1, § 167(c).

¹³⁷ *Id.* §§ 167(d), 169-173, 183-85.

¹³⁸ See New MBCA, *supra* note 1, § 14.03.

¹³⁹ *Id.* § 14.05. This includes the collection of assets, disposition of all property not to be distributed to shareholders, payment of outstanding liabilities, distribution of the remaining property to shareholders, and such other acts "necessary to wind up and liquidate its business and affairs." *Id.* § 14.05(a). The statute also outlines those matters not affected by dissolution per se, including title to the corporation's property. *Id.* § 14.05(b).

rejection by the corporation.¹⁴⁰

Perhaps more significant is the New MBCA's treatment of unknown claims. The new act allows the corporation to publish notice in a newspaper of general circulation providing a procedure for the filing of unknown or contingent claims, and a statement that any such claim will be barred if an action to enforce is not filed within five years.¹⁴¹ This provision now provides, in effect, a uniform statute of limitations for unknown or contingent claims.¹⁴² Moreover, it effectively overrules *Naugher v. Fox River Tractor Company*.¹⁴³ In that case, the court held under section 209 of the Old MBCA that while a product liability action against a dissolved corporation arose at the time of manufacture, it would not be barred until six years from the date of injury,¹⁴⁴ thereby creating virtually unlimited exposure for such claims.¹⁴⁵

In the area of involuntary dissolution, two important changes are made by the New MBCA. The first is an entirely new set of provisions for administrative dissolution. The grounds for dissolution by the Secretary of State now include failure to pay franchise taxes or penalties; failure to file an annual report; failure to maintain a registered office, or agent, or to notify the Secretary of State of changes thereto; and the expiration of a corporation's duration.¹⁴⁶ Given the largely ministerial nature of

¹⁴⁰ *Id.* § 14.06. The prior statute required that written notice be sent but did not specify any sanction for failure to respond. Old MBCA, *supra* note 1, § 173(a). Rather, such claims survived for the period of the applicable statute of limitations. *Id.* § 209.

¹⁴¹ See New MBCA, *supra* note 1, § 14.07. This would have the effect, after the five year period, of barring known claimants not receiving notice; claimants who filed a claim but were not paid; and contingent claims or those based on events occurring after dissolution. *Id.* § 14.07. If an action is timely filed, the corporation (to the extent of the assets it has retained) or shareholders (for their pro rata share or the amount of assets distributed to them, whichever is less) can be held liable. *Id.* § 14.07(d).

¹⁴² *Id.* § 14.07(c). Under the Old MBCA the limitation period varied according to the nature of the claim. See *supra* note 140.

¹⁴³ 446 F.Supp. 1281 (N.D. Miss. 1977).

¹⁴⁴ *Id.* at 1282-83 (analyzing Mississippi's general statute of limitations).

¹⁴⁵ *Id.* at 1283. See also New MBCA, *supra* note 1, § 14.07(c)(3). Presuming that the requisite notice is published, any such claim would either be "contingent" (if the injury was incurred before dissolution) or "based on an event occurring after the effective date of dissolution" (if the injury was incurred at that time), and thus would be barred by the passage of five years under New MBCA § 14.07(c)(3).

¹⁴⁶ See New MBCA, *supra* note 1, § 14.20. Under the MBCA certain grounds would

such vices, however, the statute also provides a fairly simple procedure for reinstatement upon cure, together with a right of judicial appeal from any denial of reinstatement.¹⁴⁷

The other principal innovation of the New MBCA is the power granted to a court conducting a proceeding for judicial dissolution to appoint a custodian to manage its business as an alternative to a liquidating receiver.¹⁴⁸ Although the statute is silent as to those factors to be weighed by the court in determining whether a custodianship would be appropriate, presumably it is intended as a less drastic alternative to liquidation and a device to effect a resolution of the internal difficulties which gave rise to the proceeding.¹⁴⁹ If nothing else, since the statute allows the delegation of "all powers of the corporation through or in place of its board of directors or officers" to the custodian,¹⁵⁰ this may provide the requisite impetus to a buy-out of complaining shareholders or other voluntary settlement of the underlying controversy. If appropriate, the court may also convert a custodianship to a receivership, and vice versa.¹⁵¹

E. Dissenters' Rights

The traditional approach to dissenters' rights, as embodied in the Old MBCA,¹⁵² has been the subject of criticism both by shareholder and management interests. For the shareholder who

have justified involuntary judicial dissolution through an action filed by the Attorney General, or suspension of the corporation's charter by the Secretary of State. Old MBCA, *supra* note 1, §§ 187-89. As a practical matter, however, few such actions were pursued by the Attorney General, and the sanction of suspension (although theoretically carrying with it denial of the privilege of doing business) often failed to provide the requisite impetus for corrective action by a recalcitrant corporation's managers. The device of administrative dissolution is both more economically efficient and, at the same time, may carry a connotation of seriousness that mere "suspension" did not.

For the procedure to be followed by the Secretary, including the requisite notice periods, see New MBCA, *supra* note 1, § 14.21.

¹⁴⁷ See New MBCA, *supra* note 1, § 14.22-14.23.

¹⁴⁸ *Id.* § 14.32(a). The Old MBCA recognized only the receivership concept. Old MBCA, *supra* note 1, § 195-97.

¹⁴⁹ See REVISED MODEL BUSINESS CORP. ACT. § 14.32 Official Comment (1984).

¹⁵⁰ New MBCA, *supra* note 1, § 14.32 (c)(2).

¹⁵¹ *Id.* § 14.32(d). For other matters involving the procedure for judicial dissolution, see *id.* §§ 14.31, 14.33.

¹⁵² See Old MBCA, *supra* note 1, §§ 159, 161.

objected to one of the enumerated transactions that triggered dissenters' rights,¹⁵³ this dissatisfaction was eminently understandable: the procedure for asserting them was highly complex, thus subjecting the dissenter to the risk of losing his rights by technical noncompliance,¹⁵⁴ and in any event involved the expense of a court action to determine the "fair value" of his shares if the parties could not agree.¹⁵⁵ In turn, that complexity and expense created from management's perspective an inherent potential for nuisance litigation motivated by settlement value, or demands based upon unrealistic visions of a stock's worth.¹⁵⁶ Finally, the generally worded definition of "fair value" in the statute offered no guidance as to how it should be determined.¹⁵⁷

¹⁵³ *Id.* § 159. Under the Old MBCA these included only (1) mergers and consolidations and (2) the sale or exchange of all or substantially all of the corporation's assets other than in the ordinary course of business. *Id.*

¹⁵⁴ In brief, the Old MBCA demanded the following: (1) written objection by the shareholder prior to or at the meeting where action was to be taken; (2) the shareholder had to vote against the action; (3) the shareholder had to make written demand for payment of the "fair value" of his shares within 10 days of the vote (15 days if a short-form merger); (4) if within 30 days thereafter the corporation and shareholder could not agree on such fair value, then the corporation could, within 60 days of the transaction complained of, file an action to determine the fair value of his shares; (5) if the corporation failed to bring such an action within the 60 day period, then any shareholder could commence the action. In all events, the shareholder was required to deposit his share certificates with the corporation within 20 days of his initial demand; failure to do so would result in the termination of his rights unless his failure was excused by a court "for good and sufficient cause." *Id.* § 161.

Of course the corporation and shareholder might agree upon the question of valuation, in which instance payment was to be made within 90 days of the transaction. *Id.*

¹⁵⁵ Committee on Corporate Laws, *Changes in the Model Business Corporation Act Affecting Dissenters' Rights*, 32 BUS. LAW. 1855, 1856 (1977)[hereinafter *Dissenters' Rights*]. Under the Old MBCA, the expense of a valuation proceeding was borne by the corporation unless the court found that the refusal by the shareholder to accept the corporation's offer was "arbitrary or vexatious or not in good faith," in which instance all or part of the expense could be taxed to the shareholder. In all events, each party had to pay his own attorneys' fees. Old MBCA, *supra* note 1, § 161.

¹⁵⁶ See *Dissenters' Rights*, *supra* note 155, at 1856.

¹⁵⁷ The most commonly accepted procedure is the so-called "Delaware block" method where the three elements of value, *i.e.*, assets, market value, and earnings, are assigned a designated weight, and the amounts thereby determined are added to reach a per share value. Norton, *supra* note 119, at 585. A recent Mississippi case suggests an emphasis on historical earnings as the most significant component in the closely-held business. *Hernando Bank v. Huff*, 796 F.2d 803 (5th Cir. 1986). For general background see, *e.g.*, Comment, *Valuation of Shares in a Closely Held Corporation*, 47 MISS. L.J. 715 (1976)(examination of factors used in determining fair share value); Note, *The Dissent-*

The drafters of the Model Act fundamentally restructured the concept of dissenters' rights in 1977 to strike a more equitable balance of competing policies.¹⁵⁸ The New MBCA adopts the Model Act approach, which broadly seeks to encourage the parties to compromise their differences privately, with judicial appraisal available only as a matter of last resort.¹⁵⁹ Technically the statute changes prior law in several significant respects.

Initially, the New MBCA expands the scope of dissenters' rights over the limitations previously imposed.¹⁶⁰ Dissenters' rights now apply to mergers as to which the dissenter has a right to vote; short-form mergers where the dissenter owns shares of the corporation which does not survive; share exchanges if the dissenter is a shareholder of the acquired corporation and has a right to vote on the plan; sales or exchanges of all or substantially all assets not in the ordinary course of business (excluding judicial sales and liquidation sales in which the proceeds are distributed to shareholders within one year); amendments to the articles that affect a dissenter's shares in any of five enumerated ways; and other transactions as to which the articles, bylaws, or board resolution provide dissenters' rights.¹⁶¹ In addition, dissenters' rights are now extended to beneficial shareholders as well as shareholders of record.¹⁶²

In another respect, however, the New MBCA is more restrictive than the old law. Dissenters' rights are now made the exclusive remedy of a shareholder to whom the rights accrue un-

ing Shareholder's Appraisal Remedy, 30 OKLA. L. REV. 629 (1977)(general discussion of relevant factors in determining value of shares held by dissenting shareholder).

¹⁵⁸ See *Dissenters' Rights*, *supra* note 155, at 1856-57.

¹⁵⁹ REVISED MODEL BUSINESS CORP ACT Ch. 13 Introductory Comment (1984).

¹⁶⁰ See *supra* note 153.

¹⁶¹ See New MBCA, *supra* note 1, § 13.02. The inclusion of article amendments remedies perhaps the most glaring deficiency of the Old MBCA, under which, for example, shares could be stripped of preferences, redemption rights, or preemptive rights without a right to dissent. *Cf. id.* § 13.02 (4).

¹⁶² Compare Old MBCA, *supra* note 1, § 3(g)(defining shareholder as a "holder of record") with New MBCA, *supra* note 1, § 13.01 (7)(defining shareholder as "the record shareholder or the beneficial shareholder" for purposes of dissenters' rights provisions). A 1988 amendment makes it clear that "beneficial shareholders" include the beneficial owners of shares held by a voting trust. MISS. CODE ANN. § 79-4-13.01(6) (Supp. 1988). For the mechanics of the assertion of dissenters' right by a beneficial owner, see *id.* § 13.03(b).

less the proposed action is "unlawful or fraudulent" as to either the shareholder or corporation.¹⁶³ This aspect of the law is likely to engender controversy. The rationale advanced by the drafters of the RMA is that so long as a majority of shareholders approve a transaction, their decision should prevail against a minority interest which deems it unwise or disadvantageous even if a court should side with the minority.¹⁶⁴ While logic supports this proposition, it is defensible only if one assumes that the minority shareholder is assured of a fair payment for his shares. Although the question is certainly debatable, on balance by adopting the broad unlawfulness or fraud exception the statute is probably sufficiently flexible to alleviate any concerns that it unduly favors majority interests.¹⁶⁵

While the overall goal of the New MBCA is to make the assertion of dissenters' rights a more practicable remedy, it should be noted that the enforcement procedure has not by any means been significantly simplified. The procedure is outlined in sections 13.20 through 13.28. Initially, if a meeting is called to consider an action triggering dissenters' rights, the notice of the meeting must state this and be accompanied by a copy of Chapter 13 of the New MBCA. If the transaction does not require shareholder approval then the corporation must notify the shareholders of the action and send a dissenters' notice described in section 13.22.¹⁶⁶

If the action requires a shareholder vote then the shareholder must give written notice of his intent to exercise dissenters' rights before the vote is taken and either vote against the

¹⁶³ See New MBCA, *supra* note 1, § 13.02(b). Consistent with this approach, the new statute also forecloses the former right of a shareholder to dissent only as to part of his shares. See Old MBCA, *supra* note 1, § 159. Such action is now permissible only in those instances where the shareholder acts as a nominee for several beneficial shareholders, some of whom do not wish to dissent. New MBCA, *supra* note 1, § 13.03(a).

¹⁶⁴ REVISED MODEL BUSINESS CORP. ACT § 13.02 Official Comment 2 (1984).

¹⁶⁵ While eschewing any attempt at comprehensiveness, the RMA suggests actions in violation of legal voting provisions, in violation of the articles, and those involving deception or breach of fiduciary duties as examples of transactions not protected from judicial intervention. *Id.* It should be noted that the clear trend is to make dissenters' rights exclusive. For a collection of statutes and cases on point, see 3 MODEL BUSINESS CORP. ACT ANN. 1372, 1374.2-1377 (Supp. 1987).

¹⁶⁶ See New MBCA, *supra* note 1, § 13.20.

action or abstain. Failure to do so results in the forfeiture of his right to payment under Chapter 13.¹⁶⁷ Thus, as under prior law, strict attention to question of technical compliance is required.

Following the meeting and within 10 days, the corporation must send a "dissenters' notice" to all shareholders who properly asserted dissenters' rights. The notice must *inter alia* state the time and place for demanding payment and tendering shares, supply a form for demanding payment, and set a date not less than 30 nor more than 60 days from the date of the notice by which the demand for payment must be received.¹⁶⁸ Thereafter the onus is upon the recipient to demand payment and deposit his shares pursuant to the terms of the notice; again his failure to comply will result in the loss of his rights under Chapter 13.¹⁶⁹

Within 60 days after the deadline for demanding payment and depositing shares,¹⁷⁰ the corporation is required to pay each complying dissenter the amount estimated by the corporation to be the fair value of his shares with accrued interest. The corporation must transmit with the payment financial statements for a fiscal year ended not more than 16 months prior to payment, an explanation of the method used to determine fair value and to calculate interest, a statement of the dissenters' rights under section 13.28 if he is dissatisfied with the offer, and yet another copy of Chapter 13.¹⁷¹

¹⁶⁷ *Id.* § 13.21.

¹⁶⁸ *Id.* § 13.22. The notice must also advise holders of uncertified shares of any restrictions that will be placed upon transfer after demand, and include a copy of Chapter 13. Of course, as to the latter one may legitimately question the layperson's ability to understand such a complex statute, but clearly no harm is done by its inclusion.

¹⁶⁹ *Id.* § 12.23(a), (c). The statute makes it clear, however, that the demanding shareholder retains all other rights as a shareholder until his rights are cancelled or modified by effectuation of the transaction. *Id.* § 13.23(b).

¹⁷⁰ *See id.* § 13.26(a).

¹⁷¹ *Id.* § 13.25. Similar to the Old MBCA, the new act defines "fair value" as "the value of the shares immediately before the effectuation of the corporate action to which the dissenter objects, excluding any appreciation or depreciation in anticipation of the corporate action unless exclusion would be inequitable." *Id.* § 13.01(3). The drafters of the RMA candidly admit, however, that this offers little guidance (other than timing) as to the methodology to be employed in calculating "fair value." REVISED MODEL BUSINESS CORP. ACT § 13.01 Official Comment 3 (1984). *See supra* note 157 and accompanying text.

If the corporation does not make the required payment within the 60 day limit it

Should a shareholder be dissatisfied with the amount tendered, or if payment is not made by the corporation within the 60 day period, under section 13.28 the dissenter may within 30 days after payment is made transmit to the corporation his own estimate of the fair value of his shares together with a demand for that amount. Failure to do so waives his right to such demand.¹⁷²

Only if the parties fail to agree upon fair value after the exhaustion of this procedure can they resort to judicial appraisal. The corporation must within 60 days after receiving demand under section 13.28 file an action to determine the fair value of the dissenters' shares if no agreement is reached. Corporate counsel should note well the importance of timing; failure to file the action obligates the corporation to pay the demanded sum.¹⁷³ All dissenters whose claims are unresolved are to be joined, and the court is empowered to appoint and define the responsibilities of appraisers. The dissenters are to receive judgment for the amount, if any, by which the court-determined fair value, plus interest, exceeds the corporation's payment.¹⁷⁴

Interestingly, the New MBCA is somewhat ambiguous as to what a dissatisfied dissenter should do with the payment he receives from the corporation if he intends to make a supplemental demand under section 13.28. The only light that the RMA comments shed upon the issue is that the statute is meant to force the corporation to pay without taking advantage of any delay pending final agreement, thereby eliminating the leverage that dilatory tactics would provide. Likewise, the shareholder is to be afforded immediate use of the amount tendered.¹⁷⁵ The statutory formulation of judicial relief, *i.e.*, the difference be-

must return the certificates to the shareholder; if thereafter the transaction complained of is consummated, the above procedure of notice and demand must be repeated. New MBCA, *supra*, note 1, § 13.26.

¹⁷² See New MBCA, *supra* note 1, § 13.28. The right to make his own estimate and demand is also provided if the corporation does not consummate the transaction of which he complains, but fails to return his certificates or release transfer restrictions on uncertificated shares under section 13.26(a).

¹⁷³ *Id.* § 13.03(a). Under the Old MBCA no such sanction existed; rather it only freed the dissenter to file the action. See *supra* note 154.

¹⁷⁴ *Id.* § 13.30(c)-(e).

¹⁷⁵ REVISED MODEL BUSINESS CORP. ACT § 13.25 Official Comment (1984).

tween fair value and the corporation's payment, suggests that the shareholder should be free to avail himself immediately of the initial payment without risking a waiver of his rights. Moreover, the statutory right to make the supplemental demand should foreclose the addition of any "accord and satisfaction" language to the corporation's check. Nonetheless, an explicit statement of the shareholder's right to use the initial payment pending resolution of his supplemental demand would be a desirable amendment to the new MBCA; absent this the prudent dissenter negotiating a check tendered pursuant to section 13.25 might well include a reservation of rights in his endorsement.¹⁷⁶

While the costs of the judicial proceeding, including expenses incurred by appraisers, are ordinarily borne by the corporation, the statute grants broad discretion to the court to tax such expenses to dissenters if it deems them to have acted arbitrarily, vexatiously or in bad faith. Likewise, attorneys' fees can be imposed upon either the corporation or dissenters if the court finds that either party did not comply in good faith with the provisions of Chapter 13.¹⁷⁷

Only experience will show whether the new act accomplishes the avowed goal of rendering dissenters' rights a more realistic remedy. While the New MBCA is far clearer and better organized than its predecessor, in frankness it has not simplified the procedure for exercising dissenters' rights to any appreciable extent. The same pitfalls exist as before for the shareholder who lacks diligence in pursuing his rights, and it would be foolhardy indeed for a dissenter not to engage the services of competent counsel. On the other hand, procedural aspects aside, the statutory incentives for negotiated settlement — particularly mandatory early payment by the corporation (as opposed to a simple offer) and the right for dissenters to make a supplemental demand — seem real and substantial. In this regard the New MBCA represents a positive step towards more satisfactory resolution of these disputes.

¹⁷⁶ Cf. MISS. CODE ANN. § 75-1-207 (1972)(UCC provision for reservation or preservation of rights).

¹⁷⁷ See New MBCA, *supra* note 1, § 13.31 (a), (b). This discretion also extends to requiring that some dissenters contribute to the attorney's fees of other dissenters if they substantially benefitted from the services performed by the latter. *Id.* § 13.31(c).

IV. CLOSE CORPORATIONS

A. Introduction

The overwhelming majority of Mississippi corporations are closely held, and surely there is no debate that such entities are different, not just in degree but in kind, from the public corporation. One of the dominant themes in corporate scholarship and legislation, at least since the mid-1950's, has been the attempt to respond effectively to problems peculiar to the close corporation.¹⁷⁸ General corporation statutes have commonly adapted to meet some of the needs of close corporations, but traditional statutes such as the Old MBCA have proven deficient in many particulars. Moreover, while judicial recognition of the special nature of the close corporation has increased in recent years,¹⁷⁹ this trend has not been universal, particularly in instances where shareholder control over board discretion has been involved.¹⁸⁰ Clearly, additional statutory "safe harbors" are desirable to facilitate effective planning where variations of the statutory

¹⁷⁸ Some common examples are (1) supermajority vote and quorum provisions; (2) provision for informal shareholder or director action by unanimous consent or conference telephone call; (3) broad powers of delegation to board committees; (4) broad power to restrict transfers of shares; (5) authorization of voting trusts; (6) provisions for one incorporator; (7) provision for fewer than three directors; and (8) broader provisions for dissolution, *e.g.*, by unanimous shareholder consent. Miller, *Illinois Close Corporations: Analysis of the New Act*, 27 DEPAUL L. REV. 587, 601 (1978). Of these it is noteworthy that the Old MBCA had no provision as to (4), (6), or (7), and as to (2) did not recognize conference telephone calls as a permissible means of shareholder or director action. Old MBCA, *supra* note 1.

¹⁷⁹ Perhaps the best-known example is *Donahue v. Rodd Electrotpe Co.*, 328 N.E. 2d 505, 515-16 (Mass. 1975), which states that shareholders in a close corporation owe one another substantially the same fiduciary duties as partners.

The Mississippi Supreme Court has followed this trend in an important recent decision involving issues of authority. In *Baxter Porter & Sons Well Servicing Co. v. Venture Oil Corp.*, 488 So. 2d 793, 796 (Miss. 1986), the court equated the authority of a shareholder, executive officer and director of a close corporation to that of a partner in a partnership as to matters that constitute carrying on the usual business of the corporation. *Cf.* Miss. CODE ANN. § 79-12-17(a)(Supp. 1987)(authority of partnership as agent for partnership). While the result reached in *Baxter Porter*, *i.e.*, binding the corporation to acts undertaken by such a person without formal board approval, is not surprising, the court's candid admission that the pristine rules of agency simply should not apply in the close corporation setting is a praiseworthy move towards more honest and realistic decisionmaking in this area.

¹⁸⁰ See *infra* notes 199-201 and accompanying text.

model are appropriate. Paradoxically, though, the Old MBCA reflected a large corporation orientation.¹⁸¹

The recent response to this need has been broadly twofold: in some states, the enactment of special "close corporation" statutes either as a supplement or alternative to the general corporation statute;¹⁸² in others, the addition of special provisions of particular significance to the close corporation to a general corporation statute. The RMA, from which the New MBCA was derived, takes the latter approach.¹⁸³ I believe this is fundamentally sound,¹⁸⁴ and certainly the New MBCA is a vast improvement over its predecessor. Nonetheless, there remain

¹⁸¹ See *Part One*, *supra* note 3, at 170 n. 15.

¹⁸² These statutes generally adopt criteria for classification as a statutory close corporation, and a set of special rules applicable only to such corporations. For an extensive discussion of such statutes, see 1 H. O'NEAL, *CLOSE CORPORATIONS* § 1.14b (2d ed. 1971 & Supp. 1987) [hereinafter O'NEAL]. A list of states with integrated close corporation provisions can be found at 4 *MODEL BUSINESS CORP. ACT ANN.* 1868 (3d ed. Supp. 1987).

¹⁸³ In 1981, the ABA Committee on Corporate Laws first promulgated a proposed supplement to the Model Act, presenting an integrated close corporation statute. See Committee on Corporate Laws, *Statutory Close Corporation Supplement to the Model Business Corporation Act*, 37 *BUS. LAW.* 269 (1981)(results of committee's work). The Supplement was formally adopted with amendments in 1983. See Committee on Corporate Laws, *Statutory Close Corporation Supplement to the Model Business Corporation Act*, 38 *BUS. LAW.* 1031 (1983)(detailing adoption of amendments). The current text can be found at 4 *MODEL BUSINESS CORP. ACT ANN.* 1803-1862 (3d ed. 1985). The Supplement was, however, not proposed by the Task Force as a part of the Business Law Reform legislative package. For a summary and critique of the Supplement, see Kessler, *The ABA Close Corporation Statute*, 36 *MERCER L. REV.* 661 (1985).

¹⁸⁴ Author's Note: The debate over the desirability of integrated close corporation statutes is of long standing, and I will make no effort to resolve it here. A useful summary of the arguments pro and con is found in O'NEAL, *supra* note 182, §§ 1.13-1.14(c). I have been convinced by those who argue that a well-drafted general incorporation act with provisions that respond to basic close corporation issues offers sufficient flexibility to planners without the necessity for the creation of an arbitrarily defined "statutory close corporation." A well-reasoned statement of this proposition is Karjala, *A Second Look at Special Close Corporation Legislation*, 58 *TEX. L. REV.* 1207 (1980)[hereinafter Karjala]. It is noteworthy that Florida, which adopted one of the pioneering integrated close corporation acts, subsequently repealed it.

Perhaps more germane is whether it is rational to maintain artificial demarcations between the partnership and corporation in the small business setting. The ultimate goal in this area more appropriately might be a new unified small business form combining the most desirable features of the laws of partnerships and corporations. For a discussion of this question, see Haynsworth, *The Need for a Unified Small Business Legal Structure*, 33 *BUS. LAW.* 849 (1978). This, however, goes beyond the scope of the present article.

some problem areas which the new act does not address, and to which the legislature should give close attention in the future. Before dealing with those issues, however, I will discuss the major innovations of the New MBCA.

B. Share Transfer Restrictions.

The Old MBCA did not directly validate restrictions on the transfer of shares, thus leaving the efficacy of such devices to be determined by judicial precedent.¹⁸⁶ The New MBCA greatly improves the law by explicitly authorizing share transfer restrictions and delineating the types of restrictions which may be permissible.

Under section 6.27, transfer restrictions are authorized to maintain a corporation's status where determined by the number of its shareholders (*e.g.*, an election under Subchapter S of the Internal Revenue Code), to preserve a securities law exemption, or for "any other reasonable purpose."¹⁸⁶ The types of restrictions authorized by the statute are (1) rights of first refusal, (2) obligations to purchase restricted shares, presumably upon the occurrence of some contingency, (3) consent provisions if not "manifestly unreasonable," and (4) disqualifications of certain purchasers (*e.g.*, competitors) if not "manifestly unreasonable."¹⁸⁷

¹⁸⁶ The leading case was *Fayard v. Fayard*, 293 So. 2d 421 (1974), which adopted the rule that transfer restrictions in close corporations would be sustained if determined to be "reasonable in the light of the relevant circumstances." *Id.* at 423. The court went on to enumerate the factors to be considered as including: (1) size of the corporation, (2) degree of the restraint, (3) duration of the restraint, (4) method of fixing share value, (5) relation of the restraint to corporate objectives, (6) the threat posed by a hostile shareholder, and (7) the likelihood that the restriction would serve the corporation's best interest. Applying this test the court held that a restriction in a family corporation requiring consent of all shareholders to any transfer was valid as to transfers outside of the family but invalid as to intrafamily transactions. *Id.* at 424. One might, however, question the court's premise that transfers to third parties would be inherently more disruptive and prone to create disharmony than transfers to other family members.

¹⁸⁶ See New MBCA, *supra* note 1, 6.27(c). Of course this still leaves the definition of such "reasonable purposes" ultimately in the hands of courts, but there is a substantial body of caselaw nationwide from which guidance can be drawn. For a collection and summary of cases, see 1 MODEL BUSINESS CORP. ACT ANN. 432-443 (3d ed. Supp. 1987).

¹⁸⁷ See New MBCA, *supra* note 1, § 6.27(c). Consent restrictions have been particularly risky at common law, despite the *Fayard* court's acceptance in the family corpora-

The usefulness of share transfer restrictions, both for controlling entry to and exit from a business venture and for providing liquidity of investment, are well known and need not be repeated here. In light of the preceding discussion of dissenters' rights, however, one might note a particular advantage that such provisions can serve in the closely-held corporation as a contractual alternative to Chapter 13. A provision mandating the buy-out of a minority interest upon the occurrence of some condition can not only be extended beyond the statutory events triggering dissenters' rights, but also has the advantage of allowing the parties to fix the price of shares in advance of any dispute and thereby avoid the possible necessity of judicial appraisal.

The statute permits transfer restrictions in either the articles, bylaws or separate contracts; of course those owning shares prior to the adoption of a restriction are bound only if they vote for it or become parties to the contract. In order to be enforceable against third party transferees the restriction must be conspicuously legended on the front or back of a certificate.¹⁸⁸

C. Shareholders' Agreements.

While the Old MBCA had no provisions on shareholders' agreements other than formal voting trusts,¹⁸⁹ the common law generally recognized the validity of agreements among shareholders dictating how they would vote their shares.¹⁹⁰ Rather, the problems encountered with so-called "pooling agreements"¹⁹¹ have generally been of two types. The first is to fash-

tion context. *See, e.g.*, *Rafe v. Hindin*, 29 App. Div. 2d 481, 288 N.Y.S. 2d 662, 663-64 (1968)(restriction which did not provide that consent would not be unreasonably withheld was invalid restraint on alienation). Of course, even where such a restriction was validly entered into, a court might refuse to enforce it if consent is wrongfully withheld, *e.g.*, as a means of forcing a sacrifice sale.

¹⁸⁸ *See* New MBCA, *supra* note 1, § 6.27 (a), (b). This is likewise necessary under the Mississippi Uniform Commercial Code. MISS. CODE ANN. § 75-8-204 (1972).

¹⁸⁹ *See* Old MBCA, *supra* note 1, § 65.

¹⁹⁰ *See, e.g.*, *E.K. Buck Retail Stores v. Harkert*, 157 Neb. 867, 881, 62 N.W. 2d 288, 302 (1954)(upholding agreement by majority and minority stockholders to vote their shares in such a way as to maintain equal board representation).

¹⁹¹ It should be emphasized that this discussion deals only with agreements respecting matters as to which shareholders are competent to act, primarily the election of directors. Agreements by shareholders encroaching upon board authority are dealt with at

ion an appropriate enforcement mechanism.¹⁹² An irrevocable proxy to an arbitrator or non-defaulting shareholder would seem an obvious answer. In those states without specific statutory authorization for irrevocable proxies, however, one would have to argue that it was rendered irrevocable as a proxy coupled with an interest.¹⁹³ This was not clearcut by any means. Moreover, it bore upon the second problem, *i.e.*, whether a pooling agreement might be invalidated as constituting a voting trust that did not comply with statutory requirements.¹⁹⁴ Clearly, statutory definition of the acceptable parameters of such agreements is the preferable approach.

The New MBCA responds to both concerns. Section 7.31 grants broad authority for shareholders to enter into agreements defining "the manner in which they will vote their shares."¹⁹⁵ The statute makes such agreements specifically enforceable, and

infra notes 199-201 and accompanying text.

¹⁹² The classic case was *Ringling v. Ringling Bros. Barnam & Bailey Combined Shows, Inc.*, 29 Del. 318, 49 A.2d 603 (Ch. 1946), *modified*, 29 Del. 610, 53 A.2d 441 (1947), in which the parties agreed that in the event of a disagreement, the matter would be submitted to an arbitrator whose decision would be binding. Since the agreement did not provide a right for the arbitrator to actually vote a defaulting party's shares, however, the Delaware Supreme Court reversed the Chancellor's decision to imply a proxy. Thus, the Supreme Court remedied the breach by refusing to count the defaulters' shares in the election of directors. Unfortunately for the plaintiff, without the defaulter's votes the plaintiff was outvoted by a competing shareholder, who thereby gained control of the corporation. *Ringling*, 29 Del. at 614, 53 A.2d at 244. See Note, *Specific Enforcement of Shareholder Voting Agreements*, 15 U. CHI. L. REV. 738 (1947)(specific enforcement of unobjectionable voting agreements desirable as matter of public policy).

¹⁹³ Prior Mississippi law had no express provision for irrevocable proxies. See Old MBCA, *supra* note 1, § 63.

¹⁹⁴ Again the classic case came from Delaware. In *Abercrombie v. Davies*, 36 Del. 371, 130 A. 2d 338 (1957), the court struck down an "Agent's Agreement" under which shareholders deposited their shares with agents who were granted irrevocable proxies to vote the shares for a period of ten years. *Id.* at 376, 130 A. 2d at 344. The court held that this was a secret voting trust that violated the requirements of the voting trust statute. *Id.* In distinguishing this arrangement from the valid pooling agreement in *Ringling*, the court emphasized *inter alia* the absence of irrevocable proxies in *Ringling*. *Id.* at 377-78, 130 A. 2d at 345-46. *Abercrombie* was subsequently overruled in substance by the Delaware Legislature, see DEL. CODE ANN. tit. 8, § 218(c), (e)(1968), and the Delaware Supreme Court has apparently retreated somewhat from its rigorous application. See *Oceanic Exploration Co. v. Grynberg*, 428 A.2d 1, 6-7 (Del. 1981)(voting trust provisions which were part of broad agreement of corporate reorganization were not subject to voting trust statute restrictions).

¹⁹⁵ See New MBCA, *supra* note 1, § 7.31(a).

provides that proxies granted by parties to such agreements are irrevocable.¹⁹⁶ Finally, the act specifically excludes such agreements from the voting trust statute, section 7.30.¹⁹⁷

On the other hand, it must be emphasized that these sections do not govern shareholder control agreements that affect the discretion of the board of directors. Under the 1988 amendments, the New MBCA now conforms to the RMA and allows a corporation with fifty or fewer shareholders to dispense entirely with the board of directors and be governed by its shareholders in the fashion of partnerships.¹⁹⁸ Absent this right of direct shareholder management, planners must draft cautiously any provisions that seek to control the board's powers of management lest they run afoul of common-law resistance to such attempts.¹⁹⁹ While courts have tended recently to view such agreements more favorably,²⁰⁰ even unanimous shareholder agreement

¹⁹⁶ *Id.* §§ 7.22(d)(5), 7.31(b).

¹⁹⁷ *Id.* § 7.31(a). The voting trust provisions do not materially differ from prior law.

¹⁹⁸ Miss. CODE ANN. § 79-4-8.01(c) (Supp. 1988); see REVISED MODEL BUSINESS CORP. ACT § 8.01(c) (1984). This issue is also discussed in *Part One, supra* note 3, at 183-84 n.68. The legal impediment to this originally was section 194 of the Mississippi Constitution, which could have been interpreted as requiring a board of directors for all corporations. As previously noted, section 194 has since been repealed. See *supra* note 36.

Of course, the 50 shareholder limit is subject to the criticism of arbitrariness, but since it appears in the RMA it has the merit of uniformity.

¹⁹⁹ See, e.g. *Long Park, Inc. v. Trenton-New Brunswick Theatres Co.*, 297 N.Y. 174, 175-76, 77 N.E.2d 633, 634-35 (1948)(agreement delegating management powers to majority shareholder for 19 years "completely sterilized" board and was therefore against public policy); *McQuade v. Stoneham*, 263 N.Y. 323, 325-26, 189 N.E. 234, 236-37 (1934)(agreement providing *inter alia* that shareholders would occupy certain offices and be paid fixed salaries was invalid attempt to control board where non-party minority interest existed). But see *Clark v. Dodge*, 269 N.Y. 410, 412, 199 N.E. 641, 643 (1936)(slight invasions of powers of directorate by shareholders is permissible where all shareholders are parties and creditors are not threatened).

²⁰⁰ The leading case is probably *Galler v. Galler*, 32 Ill. 2d 16, 203 N.E.2d 577 (1964), which upheld an agreement between two shareholders owning 208 of 220 shares that required the payment of annual dividends and fixed salaries to their wives for five years after the death of a signatory shareholder. *Id.* at 27, 203 N.E. 2d at 587. The court formulated the applicable test as no public injury, no complaining minority interest, and no prejudice to creditors. *Id.* at 25, 203 N.E. 2d at 585. Again, however, even *Galler* cannot be interpreted as meaning that "anything goes" if all shareholders agree. See e.g., *Somers v. AAA Temporary Services, Inc.*, 5 Ill. App.3d 931, 932-33, 284 N.E.2d 462, 464-65 (1972)(voiding bylaw amendment passed by shareholders rather than directors; held that *Galler* did not permit direct contravention of statute).

cannot guarantee that such agreements are immune to attack.²⁰¹ Unfortunately, the range of judicially permissible options remains murky at best.

From a policy perspective it would seem that shareholders of a close corporation, acting unanimously, should have the same freedom to order and manage their affairs by agreement as partners of general partnerships have, without regard to the artificial distinctions of shareholders and directors.²⁰² This flexibility can now be achieved in Mississippi under the amended New MBCA;²⁰³ however simply providing for direct shareholder management for a qualified corporation does not obviate the need for carefully structured control agreements analogous to those utilized in partnerships. As with partners such matters are appropriately governed contractually, not through a statutory model which is simply unrealistic in most close corporations.

D. Dissention and Deadlock

It is in the area of remedies for deadlock that the New MBCA is perhaps most deficient. As previously discussed, the act now allows a court to appoint a custodian to manage the affairs of a solvent corporation, which is certainly an improvement over prior law.²⁰⁴ However, the grounds for judicial dissolution under section 14.30 are basically the same as under prior law, requiring a showing of irreparable harm in the event of director deadlock, shareholder deadlock preventing election of directors for two years, "illegal, oppressive or fraudulent" actions of directors or majority shareholders, or misapplication or waste of assets.²⁰⁵ Thus the new act does not include more liberal provisions of some modern statutes allowing, *e.g.*, dissolution where the business cannot function to the benefit of shareholders gen-

²⁰¹ The *Long Park* decision is a frequently cited example. See *supra* note 199.

²⁰² See Bradley, *Toward A More Perfect Close Corporation - The Need for More and Improved Legislation*, 54 GEO. L. J. 1145, 1183 (1966) (close corporation should provide for validity of unanimous agreements affecting management on control of corporation).

²⁰³ See *supra* note 198 and accompanying text.

²⁰⁴ See *supra* notes 148-151 and accompanying text.

²⁰⁵ See New MBCA, *supra* note 1, § 14.30(2).

erally or pursuant to any provision in the articles.²⁰⁶ Given the traditional disinclination of courts to order dissolution and the stringency of such standards as irreparable injury, fraud, oppression, and waste, the statute is arguably an inadequate response to the plight of the minority shareholder who may find himself locked into an inviable investment without the "Wall Street Option" of public corporation shareholders to sell in a waiting market.

The problem of illiquidity of the close corporation investment, particularly a minority interest, is probably the most vexing one still facing legislators and close corporation planners. The "liquidation right"²⁰⁷ of partners in a general partnership, even one constituted for a term,²⁰⁸ simply is not part of the corporate model. While the appropriate statutory response has been much debated, I would favor the approach of authorizing provisions in the articles of smaller corporations (to be consistent, those with fifty or fewer shareholders) granting any shareholder, or holders of a specified number or percentage of shares, the option to cause dissolution at will or upon the occurrence of a specified event or contingency.²⁰⁹ While this may be criticized as giving individual shareholders too much leverage over the majority, it simply approximates the partnership model and, in any event, would be subject to arms-length negotiation at the time of incorporation. Such a statute should require unanimous consent of shareholders to any amendment of the articles to provide the right, and for legending share certificates to protect innocent purchasers. So long as all parties approach the issue with eyes open, this seems a preferable alternative to the risks run by minority shareholders without such a cash-out option.²¹⁰

²⁰⁶ E.g., S.C. CODE § 33-21-150 (1976).

²⁰⁷ This was the term coined by Professor Bromberg. Bromberg, *Partnership Dissolution — Causes, Consequences, and Cures*, 43 TEX. L. REV. 631, 647 (1965).

²⁰⁸ See MISS. CODE ANN. § 79-12-75 (Supp. 1987)(Mississippi Uniform Partnership Act provision on withdrawal of partners).

²⁰⁹ See, e.g., DEL. CODE ANN. tit. 8, § 355 (a)(1968)(allows stockholders option to dissolve corporation at will or upon specified event or contingency).

²¹⁰ Of course, the minority can also be protected in the event of dissent by buy-out agreements, but these presuppose both the willingness of majority shareholders to assume this obligation and the financial ability to follow through. On the other hand, it would be disingenuous to think that "at-will dissolution" will not in some instances be

V. MISCELLANEOUS

A. Foreign Corporations

The New MBCA provisions on foreign corporations²¹¹ do not merit extensive discussion. There is, however, one important change in the area of qualification to do business. As is well known, the "door closing" provision of the Old MBCA,²¹² which denied access to state courts to foreign corporations that transacted business in Mississippi without a certificate of authority, was narrowly construed by the Mississippi Supreme Court to preclude a corporation from suing on any cause of action that arose prior to qualification. Subsequent qualification would not retroactively cure the defect.²¹³ This punitive rule is reversed by the New MBCA, which expressly provides that a foreign corporation transacting business without a certificate of authority cannot bring an action in state court "until it obtains a certificate of authority," and allows a court to stay any proceeding un-

used as a leverage device in negotiations between dissenting factions.

It should be noted that the suggested approach is by no means the most radical one that has been advanced. It does not, for example, protect the shareholder who does not bargain for and obtain the right to dissolve at will. In an important article, Professors Hetherington and Dooley advocated that this gap be closed statutorily by granting any minority shareholder in a close corporation the right to force the corporation to purchase all his shares at their fair value, so long as this would not render the corporation insolvent. This right would also be nonwaivable after two years from incorporation. Hetherington & Dooley, *Illiquidity and Exploitation: A Proposed Statutory Solution to the Remaining Close Corporation Problem*, 63 VA. L. REV. 1, 50-52 (1977). While provocative, I do not view this as a workable proposal at this time. For other criticisms, see Hillman, *The Dissatisfied Participant in the Solvent Business Venture: A Consideration of the Relative Permanence of Partnerships and Close Corporations*, 67 MINN. L. REV. 1, 69-75 (1982) (questioning assumptions upon which advocacy of at will dissolution by minority shareholders is based).

²¹¹ See New MBCA, *supra* note 1, Chapter 15.

²¹² See Old MBCA, *supra* note 1, § 247.

²¹³ *Parker v. Lin-Co. Producing Co.*, 197 So. 2d 228, 230 (Miss. 1967). This, of course, was contrary to the general rule in other states. See Dunn-Cooper, *An Analysis of Mississippi's Treatment of Foreign Corporations*, 55 MISS. L. J. 259, 261-62 (1985) (examination of Mississippi's rule).

Ironically, the Mississippi Supreme Court reached the opposite conclusion as to foreign limited partnerships, holding that qualification applied retroactively. *MISS CAL 204, Ltd. v. Upchurch*, 465 So.2d 326 330 (Miss. 1985) (construing Miss. CODE ANN. § 79-13-213(1) (Supp. 1987), *repealed*, 1987 Miss. Laws ch. 448, § 1105).

til the foreign corporation obtains the certificate.²¹⁴

B. Conflicts of Interest

While director conflicts of interest were discussed extensively in Part One of this Article,²¹⁵ one aspect of the New MBCA as enacted deserves additional comment. I previously advocated the adoption of a statute modeled after Illinois law and the Exposure Draft of the RMA explicitly providing that director or shareholder ratification of a conflict of interest transaction did not validate it for all purposes, but simply shifted the burden of proof on the ultimate issue of fairness to those attacking the transaction. The Legislature, however, adopted the approach of the RMA, with one modification: shareholder ratification requires the vote of two-thirds of eligible shares, rather than a majority.²¹⁶

I believe that the Legislature intended to enact only a savings statute that defines the burden of proof of fairness, but does not otherwise validate an unfair transaction. However, this provision — while apparently adopted with the salutary objective of making ratification logistically more difficult—may ultimately yield an undesirable result. By increasing the requisite percentage for ratification, the statute may be susceptible to a construction that the more onerous vote requirement should thereafter shield the transaction from judicial review. For reasons I have already discussed in Part One at length, I do not believe that this is sound policy. Thus I would urge the Legislature to correct this ambiguity in the New MBCA by express provision that it is intended only to shift the burden of proof, not to imbue a conflict of interest transaction with absolute validity.²¹⁷

²¹⁴ See New MBCA, *supra* note 1, § 15.02 (a), (c)(emphasis added).

²¹⁵ See *Part One*, *supra* note 3, at 202-11 (discussion of duty of loyalty).

²¹⁶ See New MBCA, *supra* note 1, § 8.31 (d).

²¹⁷ In fairness I should note that this is clearly not the position now adopted by the ABA Committee on Corporate Laws. The most recent amendment to the RMA proposed by the Committee is a new Subchapter F governing directors' conflict of interest transactions. Among other things the proposed amendment would absolutely prohibit any judicial attack on a transaction that was approved by either the board or shareholders according to statutorily prescribed procedures. See Committee on Corporate Laws, *Changes in the Model Business Corporation Act — Amendments Pertaining to Director's Conflicting Interest Transactions*, 43 Bus. Law. 691 (1988).

C. Cumulative Voting

Part One of this article advocated the elimination of mandatory cumulative voting.²¹⁸ Thus it is satisfying to note that, with the repeal of section 194 of the Constitution,²¹⁹ the Legislature has now amended the new Act to make cumulative voting permissive, although the right to cumulate applies unless eliminated by the articles.²²⁰

VI. CONCLUSION

The 1987 Mississippi Business Corporation Act undoubtedly represents a substantial improvement over its predecessor. Nonetheless, as both Parts of this Article have attempted to illustrate, there is much room for further refinement of the statute, and the experience of the bench and bar will undoubtedly expose even more areas which need legislative attention. One hopes that the Mississippi Legislature's history of "benign neglect" of the 1962 MBCA will not be indicative of its attitude towards our new Act; the 1988 amendments are an encouraging sign to the contrary.²²¹ In any event, the sweeping changes that it has already effected sound a call to immediate attention by Mississippi corporate practitioners.

²¹⁸ *Part One, supra* note 3, at 228-31.

²¹⁹ *See supra* note 36.

²²⁰ Miss. CODE ANN. § 79-4-7.28(b) (Supp. 1988). A conforming amendment was also made to section 8.08, dealing with director removal.

The 1988 amendments also now permit, *inter alia*, directors to fill vacancies in the board, unless prohibited by the articles. Miss. CODE ANN. § 79-4-8.10 (a) (2) (Supp. 1988).

²²¹ *See generally* 1988 Miss. Laws Chs. 368-69.