Annual Survey of Massachusetts Law

Volume 1964 Article 4

1-1-1964

Chapter 1: New Business Corporation Law

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PART I

Private Law

CHAPTER 1

New Business Corporation Law

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§1.1. **General.** In 1964 a new Business Corporation Law was enacted as General Laws, Chapter 156B by Chapter 723 of the Acts of 1964. This law is applicable to general business corporations organized under Massachusetts law and goes into effect October 1, 1965. After that date, Chapters 155 and 156 will no longer be applicable to Massachusetts business corporations, but those chapters will remain on the books to serve as the basis for references in other chapters of the General Laws regulating special categories of corporations such as trust companies, utilities, etc.

This chapter will describe briefly the principal changes made by the new Business Corporation Law. Before doing so, it would be well to make clear what the new law is not. It is not a complete rewrite or codification of the Business Corporation Laws such as has been adopted by a number of other states which have modernized their corporate laws.

Chapter 156B, which represents the first general overhaul of the Massachusetts corporate laws since 1903, is a consolidation and rearrangement of the provisions of pertinent Sections of Chapters 155 and 156 with such clarification and modernization of those provisions as was generally felt to be needed by practising corporate lawyers.

As a consequence of this approach, in many instances existing language of the prior Statutes is preserved and some sections are carried over unchanged into the new law.

Also by way of introduction, it should be noted that there has been filed with the Massachusetts Legislature, and is now pending, a Bill, House No. 2343, to make a few additional changes in Chapter

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156B. It is too early to state what the outcome of this Bill will be, but in the course of describing the principal changes made by Chapter 156B, notation will be made in a few places of additional changes which may result from the passage of the Bill now pending in the Legislature.

§1.2. **Organization.** In the new Statute the procedure for organizing a corporation is substantially streamlined. There will be one fundamental document, the Articles of Organization, and no Agreement of Association. The Articles will be signed by the incorporators and when filed with and approved by the Secretary of State, the corporation is legally organized. The meeting of the incorporators which adopts the Articles of Organization will also adopt By-Laws and elect all the initial officers. The first meeting of directors previously required will no longer be necessary.

The Articles of Organization are modernized in other ways. It is no longer necessary to set forth the stock "now to be issued" or make reference to stock subscribed for by incorporators. Certain information contained in the Articles of Organization, such as the initial principal office, the date of the annual meeting, the date of the fiscal year, etc., is expressly stated to be contained in but not part of the Articles of Organization. Any change in this data later made is to be reflected by certificates filed in the office of the Secretary of State. This means, among other things, that it will no longer be necessary to amend the Articles of Organization of the corporation to change its principal office from one city in the Commonwealth to another.

The new Statute lists in some detail the powers of a corporation such as are customarily enumerated by careful draftsmen in the Articles of Organization. Unless specifically excluded in its Articles, every corporation subject to the Act, whether organized prior to or after October 1, 1965, will automatically have these powers. In order not to change anymore than necessary the scope of existing corporations, it is provided, however, that such powers are granted only in furtherance of the purposes of the corporation.

The limitation of a fifty-year life for a real estate corporation has been eliminated. The reasons of policy, if any existed, for this limitation appear to have disappeared, and it has led to unnecessary confusion in some instances as to whether the owning of real estate was the principal activity of the corporation or incidental to other purposes.

In the Bill referred to, now pending in the Legislature, a provision is introduced for the first time permitting a registered agent in the Commonwealth. The registered agent may be an individual or a corporation. If one is appointed, the corporation need no longer have a resident of Massachusetts as its clerk.

§1.3. **Amendments to Articles of Organization.** The provisions of prior law with respect to amendments have been somewhat simplified and rearranged. Under this heading is contained the principal

change made by the law which represents a substantial change in policy. This has to do with amendments affecting outstanding stock.

Under prior law Section 42 of Chapter 156, which authorized the adoption by two-thirds vote of any lawful amendment, was interpreted by the courts as barring any amendments altering the rights of outstanding stock. As a result, corporations found that a needed recapitalization favored by most stockholders might be held up by the necessity of getting the consent of every stockholder. This concept of protecting the interests of existing minority stockholders found itself increasingly in conflict with the need for a corporation to adapt itself to changing conditions. This was one factor which has led to an increasing use of the laws of Delaware and other states for incorporation of Massachusetts enterprises.

The new Statute provides that with the consent of two-thirds of each class of the voting stock and two-thirds of any class adversely affected, any change whatever can be made in the Articles of Organization of the corporation including a change affecting outstanding stock.

Such a provision without more would be constitutional, but in the interests of preserving, to some extent, the protection afforded by prior law to the holders of outstanding stock, the new Statute provides that any stockholder whose rights are adversely affected by such a change is entitled to have his stock appraised and purchased by the corporation. To narrow the field somewhat as to what kind of a change can be claimed to have an adverse affect, the Statute specifies that only certain kinds of amendments (alteration of preferential rights or right of redemption, creation of restriction on transfer, etc.) shall be considered as adversely affecting the rights of a stockholder.

The result is that under the new Statute dissenting stockholders will be entitled to rights of appraisal not only upon sale of assets or merger, as under prior law, but upon an amendment to the Articles which adversely affects their rights. It should be noted, however, that a right of appraisal will no longer exist upon a change by a corporation of the "nature of its business."

The new Statute continues the pattern of prior law whereby certain amendments to the Articles of Organization may be made by majority vote and more fundamental amendments by a two-thirds vote. An amendment changing the corporate name, however, has been transferred from the two-thirds to the majority vote category.

A provision in the Bill now pending in the Legislature is designed to clarify the situation with respect to the voting rights of two or more classes which the Articles of Organization provide shall vote as a single class. Under prior law, some question has been raised as to whether, even with such a provision in the Articles, the Statute might not require that each class vote separately on an amendment, and therefore, if a two-thirds vote was required, two-thirds of each

class must vote in the affirmative to adopt the amendment. If the new Bill is passed, it will be clear that if the Articles of Organization provide that both classes shall vote as a single class, they may do so for all purposes unless the interests of a class are adversely affected. A class adversely affected will also be entitled to a separate class vote.

The new law contains several modernizing provisions respecting Articles of Amendment. By a two-thirds vote, Articles of Organization may be restated and thereby eliminate from the Articles of Organization of the corporation, as amended, obsolete material such as provisions for various classes of preferred stock which have been removed from the corporate structure by earlier amendments. Provision is made for amendment of the Articles of Organization by a trustee in reorganization. The Articles of Amendment may be filed within sixty rather than thirty days after the vote adopting the amendment. They must be signed by the president and clerk (or vice president or assistant clerk) and need not be signed by the treasurer and a majority of the directors as under prior law. Finally, the Statute permits a delayed effective date up to thirty days after filing. This means that a particular date and hour of the day can be determined in advance for the amendment to become effective, and it will no longer be necessary to have the physical filing of the amendment take place at the particular time.

§1.4. **By-Laws.** The new Statute expressly authorizes the directors to amend By-Laws if and to the extent that the Articles of Organization so provide. This means that it will be possible to authorize the directors to amend the By-Laws generally or to authorize the directors to amend the By-Laws except for specified provisions such as, for instance, changing the date of the annual meeting or increasing the number of directors.

§1.5. **Stock.** There are a number of minor changes in the new Statute affecting details of the required form of stock certificates. Facsimile signatures on stock certificates are permitted if the corporation has either an independent transfer agent or registrar and not both as required by previous law. The requirements as to statement of preferred stock provisions and restrictions on transfer are also clarified. In each case either the full text must be stated on the certificate or statement of the existence of the stock provisions or restrictions must be made together with a statement that the corporation will furnish a copy to a stockholder on request.

The new Statute specifically authorizes separate series of a single class of stock and expressly permits fractional shares and scrip. The statutory provisions requiring the corporation to keep certain records and produce them for inspection by stockholders have been modernized, and the situation with respect to pre-emptive rights made clear. Under the new Statute, no pre-emptive right exists except as any particular corporation may otherwise provide in its Articles or By-Laws.

§1.6. Stockholders. Meetings of stockholders may be held outside Massachusetts if authorized by the Articles of Organization. The new Statute also contains specific authorization for a number of provisions dealing with stockholders' meetings which are often included in corporate By-Laws. For instance, the hour and place of the annual meeting may be varied by corporate management, and if the annual meeting is not held when scheduled, a special meeting may be held in lieu of it with all the effect of an annual meeting.

To bring practice in Massachusetts more into line with that in other states, the Statute expressly authorizes action to be taken by stockholders without a meeting pursuant to written consent of all the stockholders.

The rule hitherto prevailing in the Federal courts in Massachusetts governing the bringing of a suit by minority stockholders has been adopted by the Statute, namely, that such suit can only be brought if the plaintiff was a stockholder at the time of the act complained of or acquired his stock by operation of law from such a holder.

The statutory liability of stockholders in connection with dividends received from a corporation which goes bankrupt has been clarified and modernized. The former Statute spoke in terms of reduction of capital stock, and a right of action was given directly to creditors. This required detailed provisions for the enforcement of such a right by the creditors in the event of bankruptcy. The new law makes clear that stockholders who receive a dividend, if the corporation is at the time, or is thereby rendered, bankrupt or insolvent, and if the corporation thereafter is adjudicated bankrupt, are liable to the extent of the amounts distributed. The liability runs to the corporation and, therefore, passes to a trustee in bankruptcy to be enforced for the benefit of creditors. At the same time, the liability of stockholders for money due to operatives for services rendered within six months has been eliminated. The rights of employees are adequately protected by other provisions of law.

§1.7. Directors and officers. The detailed provisions as to the term of office, election, and power of officers and directors have been somewhat clarified, and the corporate structure made more flexible.

Directors need not be stockholders unless affirmatively required by the By-Laws. This will obviate the need of the provision found in most By-Laws negativing the requirement for such stockholding.

Contrary to prior law, the By-Laws may provide for the treasurer and clerk to be elected by the directors as is done under the law of Delaware and other states. In the Bill now pending in the Legislature, a corresponding flexibility is provided with respect to the president who may, if the By-Laws so authorize, be elected by the stockholders and need not be a director.

The power of directors to fill vacancies is expanded. Unless the Articles of Organization or By-Laws provide to the contrary, any vacancy in office, including a vacancy in the board of directors resulting from the enlargement of the board, may be filled by the directors.

This provision must be considered in conjunction with another provision of the new Statute under which, if authorized by the By-Laws, the board of directors may be enlarged by vote of a majority of the directors then in office.

As in the case of stockholders, directors are authorized to act without a meeting, by unanimous written consent.

The right of the board of directors to delegate its powers to committees is expanded. The prior law authorized delegation only to an executive committee to which could be entrusted the management of the current and ordinary business of the corporation, whatever that meant, and such other duties as the By-Laws might prescribe. The permissible limits were not clear. The new Statute authorizes the delegation of any functions except certain specified ones to any committee of the directors with the proviso that such delegation does not have the effect of relieving directors from liability. To clarify the limits of delegation, certain specified powers are excluded, such as power to amend the By-Laws, issue stock, declare dividends, etc.

The new Statute expressly authorizes removal of officers and directors by the body which elected them, either the stockholders or the directors.

The requirement that the clerk of the corporation be sworn has been eliminated. By-Laws, of course, may continue to require such an oath.

The new Statute expressly empowers corporations to indemnify directors, officers and agents and contains a provision specifying the manner in which indemnification may be validly authorized. It should be noted that to comply with the machinery provided by the Statute, action by the incorporators or the stockholders will be needed. This provision of Chapter 156B has been the occasion of considerable study and discussion by corporate lawyers. The Massachusetts statute does not undertake, as does the New York statute, for instance, to set limits on the extent to which indemnification may be provided for such things as counsel fees or in the event of settlement of litigation.

The Bill pending in the Legislature does contain a proposed further addition to this Section to make clear that no indemnification may be provided for a corporate official if he has been adjudicated to have acted otherwise than in good faith in what he reasonably believed to be the best interests of the corporation. The new Bill also makes clear that the statutory provision is not necessarily exclusive. Some right of indemnification of an agent by his principal may exist independently of any statute, and there should be no inference that whatever rights otherwise exist are reduced.

The new Statute contains some rearrangement and clarification of the statutory liability of officers and directors for the issue of stock for improper consideration, the declaration of a dividend which renders the corporation insolvent, the making of loans to stockholders, directors and officers, and the filing of false statements with the Secretary of State.

No basic change in public policy is reflected by any modifications of these Sections, but there have been minor revisions. For instance, directors who vote for certain acts are held liable under the new law, whereas under the old law all directors were prima facie liable unless they voted against. In the case of improper loans, they are also liable if they assent to, i.e., know about and do not take action to prevent a loan. The measure of liability has been brought into line with the damage to stockholders or creditors resulting from the act complained of. The old Statute was based on the earlier concept that if improper corporate action was taken, those responsible lost the protection of the limited liability characteristics of a corporation and were liable to creditors for the "debts of the corporation." This produced a situation under prior law where, by the wording of the statute, a director might be liable to a creditor because he authorized an improper loan to a stockholder or director even though before the creditor brought suit the loan had been repaid. The liability of the officers and directors has, in certain instances, been made to run to the corporation rather than directly to a creditor. This has the effect of simplifying enforcement procedure in the event of subsequent bankruptcy.

In the brief treatment of this chapter, it is hardly practical to enumerate the precise changes in each of these four categories of statutory liability. To attempt to do so would probably be the opposite of helpful because, in the last analysis, the exact wording of each paragraph is important and a paraphrase might be misleading.

Finally, on the subject of officer and director liability, the new Statute introduces a prudent man rule as the basis for defense against claimed statutory liability. If a director or officer has acted in good faith and with the diligence, care and skill of a prudent man, he is entitled to be protected from liability if, for instance, he relied on a valuation by competent engineers in authorizing the issue of par value stock for property.

Most states that have modernized their corporate laws have attempted to deal with this problem in one way or another. Some states have provided that directors are entitled to be protected in relying on certain independent experts or on financial statistics furnished by the management. This, of course, begs the question as to whether it was reasonable in a given case to rely on the particular expert.

This prudent man provision has no application by its terms to Common Law liability of officers and directors for mismanagement of the business of a corporation. It is directed solely to the specific statutory liabilities referred to above.

§1.8. Consolidation and merger. Unlike the other main divisions of the new Business Corporation Law, the Sections dealing with consolidation and merger have been, for all practical purposes, entirely rewritten. In general, the Delaware form has been followed with

some modification to adapt it to Massachusetts practice, viz., a prior vote of directors is not required before action by stockholders.

The terminology of what constitutes a consolidation and what a merger is revised to accord with that used throughout the rest of the United States, contrary to the prior Massachusetts statute.

A merger of a 90 percent-owned, as distinguished from a 100 percent-owned, subsidiary into its parent by directors' vote of the parent is expressly authorized. The Statute permits payment of cash or other consideration to minority stockholders of the subsidiary and gives such stockholders appraisal rights.

The requirements with respect to mergers and consolidations involving foreign corporations are liberalized by providing that the foreign corporation need only comply with the law of its state to adopt the merger. The Statute further provides that if the surviving corporation is to be governed by the laws of another state, the Articles of Merger or Consolidation need only comply with the laws of that state. Practising lawyers are aware of the difficulty encountered in the past because of the requirement that an out-of-state corporation comply with Massachusetts procedural provisions.

As in the case of amendments to Articles of Organization, provision is also made for fixing a future effective date of a merger so that simultaneous filing at a particular moment of time in several jurisdictions is not required.

Finally, Chapter 156B authorizes the resulting or surviving corporation to issue bonds or other securities as well as stock in exchange for stock of the absorbed corporations. The Bill at present before the Legislature further expands this to specifically authorize the delivery of cash or other consideration for shares of constituent corporations. This provision, taken from the New York statute, will, for instance, permit a subsidiary which is going to be the surviving corporation to deliver stock of its parent to stockholders of the constituent corporations.

§1.9. **Appraisal.** The machinery with respect to appraisal has also been radically revised. As indicated above, rights of appraisal will exist hereafter in many more situations than under prior law. The notice of a meeting at which corporate action is proposed to be taken which might give rise to appraisal rights must contain a statement of such rights. Thereafter, to perfect his rights, a stockholder must object in writing before the taking of the vote. This enables corporate management and other stockholders to know the extent of possible financial demands to be made on the corporation before acting on the matter.

The appraisal process itself is modernized by providing for all proceedings to be gathered into one court action. Thus, the corporation will not have to conduct a multiplicity of proceedings with different stockholders.

§1.10. **Liquidation and dissolution.** Chapter 156B clarifies the deadlock situation for voluntary dissolution by adopting the defini-

tions of the A.B.A. Model Act and deals with the determination of the vote required in case more than one class of stock is outstanding.

The Bill pending before the Legislature introduces, for the first time in Massachusetts, machinery for voluntary dissolution coupled with administrative action by the Secretary of State's office without recourse to a court proceeding. The procedure used for many years in most cases of voluntary dissolution has been to request the Secretary of State to petition the court for dissolution. This, as a practical matter, gives no certainty as to the actual date of dissolution in cases in which that is desired, and it is apparent that the former Statute was not designed for the average case of voluntary dissolution.

The provisions of the pending Bill are similar to those found in many other states with modern corporation laws by which Articles of Dissolution, adopted by a two-thirds vote, are filed with the Secretary of State, provision being made for the protection of creditors and the tax department.

§1.11. **Miscellaneous filing requirements.** Chapter 156B provides for filing with the Secretary of State rather more certificates of corporate changes than did the prior law. These will include certificates as to change of principal office, change of fiscal year, change of date of annual meeting, change of officers, change of resident agent and a certificate with respect to establishment by directors of the characteristics of a series of stock, which last certificate has the effect of an amendment to the Articles of Organization.

The troublesome Certificate of Issue has been eliminated. As is well known, this has long ceased to serve much useful purpose, and in many cases has been misleading. The certificate previously required as to stock "to be issued," of necessity, frequently covered stock issuable under options or otherwise which, in fact, never was issued. The annual Certificate of Condition still required of corporations is a more reliable guide to stock actually issued by a corporation. With the discontinuance of the requirement of the filing of Certificates of Issue, there goes the elimination of similar data from Articles of Organization and Articles of Amendment, Consolidation or Merger.

§1.12. **Conclusion.** The foregoing resumé does not attempt to list many minor, procedural changes made by the new Business Corporation Law, such as provisions governing waivers of notice or the elimination of ballots in elections by stockholders. Furthermore, this brief summary cannot make clear all the details of even those new provisions which are mentioned.

A careful reading of the new Chapter is essential for practising lawyers. The Committee on Corporation Law of the Boston Bar Association has prepared two booklets describing in considerable detail the changes made by the new law and indicating where the language of each section of the Statute came from. These are available to interested lawyers upon application to the Boston Bar Associa-

tion, 16 Beacon Street, Boston, at their cost of printing, $2.50 for the pair. There are also available from the same source, without charge, copies of House Bill No. 2343 of 1964, together with a memorandum prepared by the same Committee describing the changes made by the Bill and the reasons therefor.