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Bill Analysis

Legislative Service Commission

Sub. H.B. 374

127th General Assembly

(As Passed by House)

Reps. Coley, J. McGregor, Wagoner, Huffman, Combs, Stebelton, Hughes, Bacon, Barrett, Beatty, Blessing, Boyd, Budish, Celeste, DeBose, Dolan, Domenick, Driehaus, Dyer, Evans, Flowers, Gardner, Gibbs, Goyal, Harwood, Jones, Letson, Luckie, R. McGregor, Mecklenborg, Raussen, Sayre, Schindel, Schneider, Sears, Setzer, Szollosi, Webster, White, S. Williams, Wolpert, Zehringer

BILL SUMMARY

- Permits the original articles of incorporation to set forth a provision eliminating the right of every shareholder to vote cumulatively in the election of directors.
- Retains the existing provision permitting the articles to be amended to eliminate the right of every shareholder to vote cumulatively in the election of directors or to delete a provision eliminating that right, but removes the provision imposing certain conditions for eliminating that right with respect to certain corporations.
- Provides that for purposes of continuing law that governs the lease, sale, exchange, transfer, or other disposition of all, or substantially all, of the assets of a corporation, the assets of a corporation include the assets of any other entity wholly owned by the corporation and provides that unless otherwise provided in the articles the procedures in continuing law do not apply to the lease, sale, exchange, transfer, or other disposition of all, or substantially all, of the assets of a corporation to any entity wholly owned by the corporation.
- Provides that a holder of shares is entitled to one or more certificates signed, executed, and effective under existing law, unless the articles of the corporation, the regulations adopted by the shareholders, or the regulations adopted at the organizational meeting by the initial directors named in the articles provide otherwise and permits the articles or those

regulations to provide that some or all of any or all classes and series of shares of the corporation must be uncertificated shares.

- Specifies that any provision of the articles or regulations of a corporation with respect to which a close corporation agreement is in effect providing for the issuance of shares in uncertificated form is ineffective during any period in which the close corporation agreement is in effect.
- Authorizes the directors, if no shares of a series created by an amendment to the articles have been issued and no option or right to acquire any share of that series is outstanding, to adopt an amendment to the articles to reduce the number of shares in that series or to eliminate from the articles all references to the series.
- Authorizes the directors to adopt an amendment to the articles to reduce the authorized number of shares of any series that have been redeemed, or have been surrendered to or acquired by the corporation, by the number so redeemed, surrendered, or acquired or to eliminate from the articles all references to the shares of a series when all of the issued shares of that series have been so redeemed, surrendered, or acquired.

CONTENT AND OPERATION

Articles of incorporation

Existing law

Under existing law, any person, singly or jointly with others, may form a corporation by signing and filing with the Secretary of State articles of incorporation that are required to set forth specified information. The articles are also permitted to set forth the following information: (1) the names of the individuals who are to serve as initial directors, (2) generally the purpose or purposes for which the corporation is formed, (3) any lawful provision for the purpose of defining, limiting, or regulating the exercise of the authority of the corporation, incorporators, directors, officers, shareholders, or holders of any class of shares, (4) any provision that may be set forth in the regulations, (5) a provision specifying the corporation's period of existence if it is to be otherwise than perpetual, and (6) any additional provision permitted by the General Corporation Law, but *the original articles of a corporation may not set forth any provision that eliminates the rights of shareholders under that Law to cumulate the voting power that they possess in the election of directors.* (R.C. 1701.04(B) and (C).)

Operation of the bill

The bill deletes the provision that prohibits the original articles of a corporation from setting forth any provision that eliminates the rights of shareholders to cumulate the voting power that they possess in the election of directors. Instead, the bill provides that the articles of incorporation may set forth a provision eliminating the right of every shareholder to vote cumulatively in the election of directors. (R.C. 1701.04(B)(6).)

The bill also modifies the Revised Code sections pertaining to the election of directors and the removal of directors to delete references to the *amendment* of the articles eliminating a shareholder's right to vote cumulatively (see "**Amendment of articles of incorporation**," below). The bill permits the *original* articles to eliminate cumulative voting, thus making those references to the *amendment* of the articles unnecessary. (R.C. 1701.55(C) and (D) and 1701.58(D).)

Amendment of articles of incorporation

Existing law

Existing law provides that without limiting the generality of the authority to amend the articles, the articles may be amended to do any of specified actions. One of these actions is the elimination of the right of every shareholder to vote cumulatively in the election of directors or the deletion of a provision that eliminates that right, *except that, if a corporation is formed after July 24, 1986, or if a corporation that exists on that date does not have issued and outstanding shares that are listed on a national securities exchange or are regularly quoted in an over-the-counter market by one or more members of a national or affiliated securities association, the articles may be amended to eliminate the right of every shareholder to vote cumulatively in the election of directors only upon compliance with both of the following (R.C. 1701.69(B)(10)):*

(1) Except as otherwise provided below in connection with surviving corporations in mergers and new corporations resulting from consolidations, the shareholder action on the amendment to the articles must not occur earlier than 90 days after July 24, 1986, or 90 days after the date that the corporation was formed, whichever date is later;

(2) A notice must have been sent to the shareholders by mail, overnight delivery service, or any other means of communication authorized by the shareholder to whom the notice is sent that states, in solid capital letters, that an effect of the amendment to the articles will be to do both of the following: (a) permit a majority of a quorum of the voting power in the election or removal of

directors to elect or remove every director, and (b) preclude a minority of a quorum of the voting power in the election or removal of directors from electing or preventing the removal of any director.

In the case of a surviving corporation as a result of a merger or of a new corporation resulting from a consolidation, if immediately prior to the merger or consolidation at least one of the constituent corporations had issued and outstanding shares listed on a national securities exchange or regularly quoted in an over-the-counter market by one or more members of a national or affiliated securities association, then the 90-day limitation described in paragraph (1), above, does not apply and the agreement of merger or consolidation, as adopted pursuant to R.C. 1701.78 or 1701.80, may eliminate, subject to paragraph (2), above, the right of every shareholder to vote cumulatively in the election of directors. An agreement of merger or consolidation that is so adopted and that eliminates the right of every shareholder to vote cumulatively in the election of directors is considered an amendment permitted by the above provision of law. (R.C. 1701.69(B)(10).)

Operation of the bill

The bill retains the provision in existing law permitting the articles to be amended to eliminate the right of every shareholder to vote cumulatively in the election of directors or to delete a provision eliminating that right, but it repeals the exception to this provision italicized under "**Existing law**," above (R.C. 1701.69(B)(10)).

Disposition of all or substantially all of the assets of a corporation

Continuing law

Continuing law generally provides that a lease, sale, exchange, transfer, or other disposition of all, or substantially all, of the assets, with or without the good will, of a corporation, if not made in the usual and regular course of its business, may be made upon the terms and conditions and for the consideration, that may consist, in whole or in part, of money or other property of any description, including shares or other securities or promissory obligations of any other corporation, domestic or foreign, that may be authorized by the directors, either before or after authorization by the shareholders as required by law, and at a meeting of the shareholders held for that purpose, by the affirmative vote of the holders of shares entitling them to exercise two-thirds of the voting power of the corporation on the proposal, or, if the articles so provide or permit, by the affirmative vote of a greater or lesser proportion, but not less than a majority, of the voting power, and by the affirmative vote of the holders of shares of any particular class that is required by the articles. At that shareholder meeting or at

any subsequent shareholder meeting, shareholders, by the same vote that is required to authorize the lease, sale, exchange, transfer, or other disposition of all, or substantially all, of the assets may grant authority to the directors to establish or amend any of the terms and conditions of the transaction, except that the shareholders cannot authorize the directors to: (1) alter or change the amount or kind of shares, securities, money, property, or rights to be received in exchange for the assets, (2) alter or change to any material extent the amount or kind of liabilities to be assumed in exchange for the assets, or (3) alter or change any other terms and conditions of the transaction if any of the alterations or changes, alone or in the aggregate, would materially adversely affect the shareholders or the corporation. Notice of the meeting of the shareholders must be given to all shareholders whether or not entitled to vote at the meeting and must be accompanied by a copy or summary of the terms of the transaction.

The corporation by its directors may abandon the transaction, subject to the contract rights of other persons, if the power of abandonment is conferred upon the directors either by the terms of the transaction or by the same vote of shareholders and at the same meeting of shareholders as described above or at any subsequent meeting. Dissenting holders of shares of any class, whether or not entitled to vote, are entitled to relief under R.C. 1701.85. An action to set aside a conveyance by a corporation, on the ground that any section of the Revised Code applicable to the lease, sale, exchange, transfer, or other disposition of all, or substantially all, of the assets of that corporation has not been complied with, must be brought within 90 days after that transaction, or the action is forever barred.

If a resolution of dissolution is adopted pursuant to R.C. 1701.86, the directors may dispose of all, or substantially all, of the corporation's assets without the necessity of a shareholders' authorization as described above.

The terms and conditions of any transaction disposing of all, or substantially all, of the corporations' assets are subject to the limitations specified in R.C. 2307.97. The above provisions do not apply to the distribution, pursuant to R.C. 1701.33, to the shareholders of an issuing public corporation of shares owned by the issuing public corporation in one or more of its domestic or foreign subsidiary corporations, unless either of the following applies: (1) the former subsidiary is a party to one or more agreements pursuant to which it is obligated to engage in an additional transaction that, if the transaction were authorized after the time at which the distribution becomes effective, would require the approval of its shareholders, or (2) immediately prior to the time at which the distribution becomes effective, the issuing public corporation has more than one class of shares outstanding. (R.C. 1701.76(A) to (G).)

Operation of the bill

The bill provides that, for purposes of the above provisions only, the assets of a corporation include the assets of any other entity that is wholly owned, directly or indirectly, by the corporation. Unless otherwise provided in the articles, those provisions in continuing law do not apply to any lease, sale, exchange, transfer, or other disposition of all, or substantially all, of the assets of a corporation to any entity that is wholly owned, directly or indirectly, by the corporation. (R.C. 1701.76(H).)

Certificates for shares; uncertificated shares

Existing law entitles each holder of shares to one or more certificates, signed by specified officers of the corporation, that certifies the number and class of shares held by the holder in the corporation, but no certificate for shares may be executed or delivered until such shares are fully paid. The bill provides that a holder of shares is entitled to one or more certificates signed, executed, and effective in accordance with the provisions of existing law, unless the articles, the regulations adopted by the shareholders, or the regulations adopted by the directors pursuant to R.C. 1701.10(A)(1) (see **COMMENT**) provide otherwise. (R.C. 1701.24(B).)

Unless otherwise provided by the articles or regulations, under existing law the directors may provide by resolution that some or all of any or all classes and series of shares of a corporation must be uncertificated shares, provided that the resolution cannot apply to shares represented by a certificate until the certificate is surrendered to the corporation and that the resolution cannot apply to a certificated security issued in exchange for an uncertificated security. The bill expands existing law by specifically permitting the articles of a corporation, the regulations adopted by the shareholders of a corporation, or the regulations adopted by the directors of a corporation pursuant to R.C. 1701.10(A)(1) (see **COMMENT**) to provide that some or all of any or all classes and series of shares of that corporation must be uncertificated shares. (R.C. 1701.24(F).)

Close corporation agreement

Existing law prohibits any corporation with respect to which a close corporation agreement is in effect from issuing shares in uncertificated form and provides that any resolution of the directors of such a corporation providing for the issuance of shares in uncertificated form is ineffective during any period in which a close corporation agreement is in effect.

The bill adds the provision that *any provision of the articles or regulations* of a corporation with respect to which a close corporation agreement is in effect

providing for the issuance of shares in uncertificated form is ineffective during any period in which a close corporation agreement is in effect. (R.C. 1701.591(L).)

Amendment of articles by the directors

Existing law authorizes the directors to adopt an amendment of the articles in specified cases. Two of these cases are as follows:

(1) When and to the extent authorized by the articles, the directors may adopt an amendment determining, in whole or in part, the express terms, within the limits set forth in the General Corporation Law, of any class of shares before the issuance of any shares of that class, or of one or more series within a class before the issuance of shares of that series. The bill provides that when no shares of a series created by an amendment to the articles under this provision have been issued and no option or right to acquire any share of that series is outstanding, the directors may adopt an amendment to reduce the number of shares in that series or to eliminate from the articles all references to the series and to make other appropriate changes that are required by the elimination of the series. (R.C. 1701.70(B)(1).)

(2) Whenever shares of *any class* have been redeemed, or have been surrendered to or acquired by the corporation upon conversion, exchange, purchase, or otherwise, the directors may adopt an amendment to reduce the authorized number of shares of the class by the number so redeemed, surrendered, or acquired; and when all of the authorized shares of a class have been redeemed or surrendered to or acquired by the corporation, the directors may adopt an amendment to eliminate from the articles all references to the shares of the class and to make other appropriate changes that are required by the elimination.

The bill modifies this provision by providing that whenever shares of any class *or series* have been redeemed, or have been surrendered to or acquired by the corporation upon conversion, exchange, purchase, or otherwise, the directors may adopt an amendment to reduce the authorized number of shares of *that class or series* by the number so redeemed, surrendered, or acquired; and when all of the *issued* (instead of *authorized*) shares of a class *or series* have been redeemed or surrendered to or acquired by the corporation, the directors may adopt an amendment to eliminate from the articles all references to the shares of *that class or series* and to make other appropriate changes that are required by the elimination (italicized terms are added by the bill). (R.C. 1701.70(B)(3).)

COMMENT

R.C. 1701.10(A)(1), not in the bill, provides that after incorporation, if the initial directors are named in the articles, the initial directors must hold an

organizational meeting, at the call of a majority of the directors, to complete the organization of the corporation by receiving subscriptions, appointing officers, *adopting regulations*, and carrying on any other business brought before the meeting.

HISTORY

ACTION	DATE
Introduced	11-01-07
Reported, H. Civil & Commercial Law	01-31-08
Passed House (94-0)	03-11-08

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