

- SUBJECT:** Shareholder standing in derivative proceeding after a merger
- COMMITTEE:** Business and Industry — committee substitute recommended
- VOTE:** 8 ayes — Deshotel, Orr, Bohac, Garza, Giddings, S. Miller, Quintanilla, Workman
- 0 nays
- 1 absent — Solomons
- WITNESSES:** For — Charles Still, Texas Business Law Foundation; (*Registered, but did not testify*: John Kuhl, Texas Business Law Foundation)
- Against — None
- On — (*Registered, but did not testify*: Nancy Hentschel)
- BACKGROUND:** Business Organizations Code, ch. 21 governs domestic for-profit corporations created under Texas law and foreign for-profit corporations engaging in business in Texas. A beneficial owner in a corporation is one who possesses the enjoyment of benefits associated with ownership, although title of the owner's share may be in another name. Whether in a direct or indirect method, a beneficial owner may individually, or through an associate or affiliate, own shares or similar securities in a corporation.
- Subch. J governs fundamental business transactions such as mergers, conversions, exchanges, or sales of assets. In addition, it details voting requirements and procedures for submitting fundamental business transactions to shareholders. Ch. 10 of the Business Organizations Code also addresses mergers, interest exchanges, conversions, and sales of assets.
- Derivative actions usually involve a shareholder suing the board of directors, management, or other shareholders of a corporation on the corporation's behalf. The issue in contention generally arises from an alleged failure of the defendant to act in the best interests of the corporation. Under Texas law, a derivative proceeding is a civil lawsuit on behalf of a corporation. A shareholder under the subchapter governing

derivative proceedings includes a beneficial owner of the corporation whose shares are held in a voting trust or by another representative on the beneficial owner's behalf.

Sec. 21.552 details requirements for a shareholder wishing to initiate or maintain a derivative proceeding, including the shareholder's status at the time of the issue forming the complaint and whether the shareholder fairly and adequately represents the corporation's interests. To whatever extent a shareholder has standing to institute or maintain a derivative proceeding on behalf of a corporation before a merger, sec. 21.552(b) prohibits the application of subch. J or ch. 10 of the Business Organizations Code to limit or end the shareholder's standing after the merger.

DIGEST: CSHB 3244 would delete sec. 21.552(b) of the Business Organizations Code prohibiting application of subch. J or ch. 10 to affect a shareholder's post-merger standing for a derivative proceeding.

The bill would take effect September 1, 2011.

NOTES: The companion bill, SB 1568 by Estes, passed the Senate by 31-0 on April 18 and was reported favorably, without amendment, by the House Business and Industry Committee on April 28, making it eligible to be considered in lieu of HB 3244.