SUBJECT: Revising certain sections of the Business Organizations Code

COMMITTEE: Business and Industry — committee substitute recommended

VOTE: 7 ayes — Oliveira, Simmons, Collier, Fletcher, Rinaldi, Romero, Villalba

0 nays

WITNESSES: For — Byron Egan, Lori Ann Fox, and Daryl Robertson, Texas Business Law Foundation; (*Registered, but did not testify*: Brittney Booth and John Kuhl, Texas Business Law Foundation)

Against — None

On — (*Registered, but did not testify*: Carmen Flores, Texas Secretary of State)

BACKGROUND: The Texas Business Organizations Code (BOC) was enacted in 2003 through HB 1156 by Giddings. It took effect January 1, 2006. BOC codified prior source laws pertaining to businesses. Effective January 1, 2010, the underlying source laws were repealed, and the transition to exclusive use of BOC was complete. Since then, technical and substantive amendments were made to BOC in 2011 and 2013.

DIGEST: CSHB 2142 would revise provisions of the state's Business Organizations Code (BOC) related to mergers, ratification and validation of defective corporate acts and putative shares, and approval of fundamental business actions. It also would make technical and conforming changes to BOC.

Mergers. CSHB 2142 would authorize corporations to engage in a type of merger, commonly referred to as a two-step merger, which did not require shareholder approval under certain circumstances, unless approval was required by the corporation's certificate of formation. This authorization would apply only to a domestic for-profit corporation that was part of the merger and whose shares, immediately before the date its board of directors approved the plan of merger, were either listed on a national

securities exchange or held of record by at least 2,000 shareholders.

The plan of merger expressly would have to permit or require this type of merger and to provide that any merger take place as soon as practicable after the consummation of a tender or exchange offer consummated under certain circumstances. The shares that would be converted and exchanged in the merger would be entitled to be valued like those of the holders who tendered shares to the acquirer in the tender or exchange offer.

The bill would allow those with ownership interests in a domestic entity subject to dissenter's rights to dissent from a merger if the shares of the shareholders were converted or exchanged, if that merger took place under a plan for a two-step merger described above. In the event of a two-step merger, the responsible organization would have to notify the shareholders who had a right to dissent of their rights no later than 10 days after the merger's effective date. The bill would require certain information to be included in the notice.

Governing documents of each domestic entity that survived a merger could be amended, restated, or amended and restated to the extent provided by the plan of merger. A certificate of amendment, a restated certificate of formation without an amendment, or a restated certificate of formation containing amendments of a surviving entity would supersede the original certificate of formation and prior changes to it. The restated certificate of formation would become the effective certificate of formation.

Except in a type of short-form merger, a certificate of merger that was required to be filed would have to include the amendments to the certificate of formation of any filing entity that was a party to the merger or a statement that amendments were being made to the certificate of formation of any filing entity involved in the merger. If no amendment was going to be made to the certificate of formation, the certificate of merger would have to include a statement to that effect, which also could refer to a restated certificate of formation attached to the certificate of merger. The bill would allow the following to be filed as an attachment to

a certificate of merger: a certificate of amendment, a restated certificate of formation without amendment, or a restated certificate of formation containing amendments for any filing entity that was a party to the merger. The bill also would allow a plan of merger to include similar amendments.

Ratification and validation of certain acts and shares. The bill would define a "defective corporate act" as:

- an overissue;
- an election or appointment of directors that was void or voidable due to a failure of authorization; or
- any act or transaction purportedly taken by or on behalf of the corporation that was within its power but was void or voidable due to a failure of authorization.

"Putative shares" would mean the shares of any class or series of the corporation that would constitute valid shares, if not for the failure of authorization, or that could not be determined by the board of directors to be valid shares. A "failure of authorization" would be the failure to authorize certain acts, documents, or agreements if and to the extent the failure would render the act or transaction void or voidable.

The bill would specify that a defective corporate act or putative shares were not void or voidable solely as a result of a failure of authorization if the act or shares were ratified or validated by the district court. To ratify a defective corporate act, the board of the directors of the corporation would adopt a resolution that stated the defective corporate act to be ratified, the time of the defective corporate act, if the defective corporate act involved the issuance of putative shares, the number and type of putative shares issued and the date of issue, the nature of the failure of authorization, and that the board of directors approved the ratification of the defective corporate act. The resolution also could state that the board of directors at any time before the validation effective time could abandon the resolution without further shareholder action, notwithstanding the adoption of the resolution by the shareholders.

Absent a ruling from the district court, the bill would prohibit the defective corporate acts or putative shares set forth in those resolutions from being considered void or voidable as a result of a failure of authorization identified in the resolution. The effect would be retroactive to the time of the defective corporate act, and the putative shares would be considered as an identical share or fraction of a share outstanding as of the time it purportedly was issued. The bill would require prompt notice to be given to the shareholders after a resolution was adopted.

CSHB 2142 specifies that ratification and validation would not be the exclusive means of ratifying or validating any act taken by a corporation and that the absence or failure of ratification of an act alone would not be enough to affect the validity of the act or transaction. This absence or failure of ratification also would not create a presumption that the act or transaction was a defective corporate act or that the shares in question were void or voidable.

Certain entities could bring an action regarding the validity of defective corporate acts and shares. In this kind of action, the district court could determine the validity and effectiveness of any defective corporate act that was ratified, the ratification of any defective corporate act, any defective corporate act either not ratified or not ratified effectively, and any corporate act or transaction of any shares, rights, or options to acquire shares. The court also could modify or waive any of the ratification procedures. The bill would provide a number of actions the district court could take and criteria the court could consider in making its decision.

In the absence of actual fraud, the bill would authorize as conclusive the judgment of the board of directors of a domestic for-profit corporation that its shares were valid or putative, unless otherwise determined by the district court.

Approval of fundamental business actions. The bill would stipulate approval procedures for a domestic non-profit corporation to approve certain business actions, including a voluntary winding up, reinstatement,

cancellation of an event requiring winding up, revocation of a voluntary decision to wind up, or distribution plan.

Domestic non-profit corporations would use different approval procedures depending on whether they had assets. If the corporation had no members or had no members with voting rights and the corporation held any assets or had solicited any assets, the corporation's board of directors would have to adopt a resolution by an affirmative vote of the majority of directors. If such a corporation did not hold any assets and had not solicited any assets, a majority of the organizers or the board of directors of the corporation would have to adopt a resolution by an affirmative vote of a majority of the organizers or a majority of the directors in office. That vote also would be required by such a corporation to approve certain other fundamental actions.

Shareholders of a corporation could give written consent, or the organizers of a corporation could adopt a resolution, to authorize a restated certificate of formation that contained an amendment to cancel an event requiring winding up.

Additional changes. CSHB 2142 would make numerous other changes to BOC that would include:

- requirements for shareholders agreements;
- authorization to use a formula to determine the value of the shares of a domestic for-profit corporation;
- authorization to make the terms of a plan of merger, exchange, or conversion dependent on facts ascertainable outside of the plan; and
- a definition of "owner liability," which would replace references to "personal liability" in the code.

The bill would take effect September 1, 2015.

SUPPORTERS SAY:

CSHB 2142 would help the Business Organizations Code (BOC) to continue serving its intended purpose of making Texas business laws

efficient and effective. Since BOC's inception, substantive and technical amendments have been made to it during each legislative session. The purpose of the updates is to ensure BOC constantly is evolving to match the needs of businesses in Texas and abroad.

Currently, because Texas law differs from that in other states such as Delaware, it is difficult for a multi-district business owner to comply with Texas requirements. This bill would help make those transactions more uniform with other states and would make explicit certain aspects of BOC that already are implied. Making certain implied options explicit under BOC would help Texas businesses better understand what current law allows and would promote consistency in business organization law across states.

OPPONENTS SAY:

No apparent opposition.

NOTES:

CSHB 2142 differs from the bill as filed in that the committee substitute would:

- allow any terms of a plan of merger, plan of exchange, and plan of conversion to be made dependent on facts ascertainable outside of the plan if the manner in which those facts would operate was clearly and expressly stated in the plan;
- specify that approval procedures stipulated in the bill apply only to a non-profit corporation that did not have assets and had not solicited assets; and
- make additional technical changes.

The Senate companion bill, SB 860 by Eltife, was approved by the Senate on the local and uncontested calendar on April 9.