

Introduction

GENERAL DESCRIPTION OF THE MODEL ACT

The Model Business Corporation Act Annotated (5th edition) contains the complete text of the Model Business Corporation Act (the “Model Act” or the “Act”), including its Official Comment, and Annotations for each section. The Model Act was initially promulgated and approved by the Corporate Laws Committee of the Business Law Section of the American Bar Association in 1950, and most recently revised in 2016.¹

The Model Act is designed as a free-standing general corporation statute that can be enacted substantially in its entirety by a state legislature. Thirty-three jurisdictions have adopted all or substantially all of the Model Act as their general corporation statute,² and two others have statutes based on the 1969 version of the Act.³ Many other states have adopted selected provisions of the Model Act.

Like most general business corporation statutes, the Model Act applies to for-profit business corporations. Although the Model Act does not generally distinguish between publicly held and privately held corporations, several provisions (sections 7.32, 14.30(a)(2), and 14.34) are designed for corporations that are not public corporations.⁴

1. Neither the Model Act nor any other Committee publications are approved by the ABA House of Delegates, the ABA Board of Governors or the ABA Business Law Section and thus do not represent policy of the ABA or any of its entities other than the Committee.

2. Alabama, Arizona, Arkansas, Connecticut, the District of Columbia, Florida, Georgia, Guam, Hawaii, Idaho, Indiana, Iowa, Kentucky, Louisiana, Maine, Massachusetts, Mississippi, Montana, Nebraska, New Hampshire, North Carolina, Oregon, Rhode Island, South Carolina, South Dakota, Tennessee, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, and Wyoming.

3. Alaska and New Mexico.

4. In light of these provisions, the Committee discontinued the Model Close Corporation Supplement, which the Committee had previously developed to address the needs of closely held corporations. For the same reason, the Committee also discontinued the Model Professional

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THE CORPORATE LAWS COMMITTEE

The Model Act has been drafted and revised by the Corporate Laws Committee (the “Committee”) of the Business Law Section of the American Bar Association. The membership of the Committee consists of a chair, appointed by the chair of the Business Law Section for a three-year term, and 25 members, one of whom is the reporter and 24 of whom serve for staggered six-year terms, appointed by the Business Law Section chair on the recommendation of the chair of the Committee. By tradition, in order to promote turnover and broader participation, members of the Committee are not reappointed at the end of their terms. Active former chairs participate as senior advisers, and the committee appoints, from time to time, liaisons from other committees of the Business Law Section and special consultants. Over the years there has been a tradition of balanced membership. Committee members have included present and former law firm partners, corporate counsel, law and business school professors, federal and state judges (from courts including the Delaware Supreme Court and the Delaware Court of Chancery), officials of the Securities and Exchange Commission, and a former director of the Central Intelligence Agency.

The Committee meets quarterly, generally for two days. Much of the work of the Committee is done in working groups (e.g., task forces and subcommittees) assigned to review and offer proposed revisions to various parts of the Model Act. After review and discussion, the working group may make recommendations to the Committee for revisions to the Model Act. After deliberation by the Committee (which may include referring matters back to the task force or subcommittee), the full Committee adopts proposed revisions to the Model Act on first reading and then, after further consideration generally at a subsequent meeting, on second reading. After second reading, the Committee publishes the proposed changes to the Model Act in *The Business Lawyer*,

Corporation Supplement. The Model Close Corporation Supplement and the Model Professional Corporation Supplement were never part of the Model Act but formerly were published as supplements to the Act.

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the law review published by the Business Law Section, and invites comments from all interested persons. After expiration of the comment period and the Committee's consideration of any comments received, the Committee considers the revisions on third reading. If adopted by the Committee on third and final reading, the revisions are adopted and notice of their approval is published in *The Business Lawyer*. Upon adoption, the revisions become part of the Model Act and are promulgated on, among other places, the Committee's website https://www.americanbar.org/groups/business_law/committees/corplaws/.

Each section of the Model Act is followed by an Official Comment, prepared by the Committee, which amplifies and explains the purpose and operation of the section. Some states that have adopted the Model Act have also adopted the Official Comment, sometimes with state-specific changes. Lists of cross-references to other relevant provisions of the Model Act are also included after each section. In this Annotated version, the Annotation that follows each section of the Model Act provides, among other things, the historical background to the section, a summary comparison of it to enacted versions of the section (or variations on it), caselaw developments regarding the section and citations to scholarly treatments of it. Although many members of the Committee assisted in preparing the Annotation, it has not been formally approved by the Committee as a whole.

The Committee also occasionally prepares and publishes white papers, policy statements, and guidebooks (including the recent 7th edition of the Corporate Director's Guidebook), and presents programs at ABA meetings. It also maintains a website (https://www.americanbar.org/groups/business_law/committees/corplaws/) which contains both current and historical materials relating to the development of the Act as well as other resources for corporate lawyers. The Committee has also developed a network of liaisons with state corporate bar leaders.

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HISTORY OF THE MODEL ACT

In 1928, the National Conference of Commissioners on Uniform State Laws (now the Uniform Law Commission) promulgated a Uniform Business Corporation Act, which was adopted by only three states (Louisiana, Washington, and Kentucky) and only partially adopted by a fourth (Idaho). See Robert W. Hamilton, *The Revised Model Business Corporation Act: Comment and Observation: Reflections of a Reporter*, 63 TEX. L. REV. 1455, 1457 n. 16 (1985). Professor Hamilton suggested that the lack of wide acceptance of the Uniform Business Corporation Act may be attributed in part to the fact that it was then “ahead of its time” and in part to the perception by state legislatures that they did not see the need for adopting a “uniform” general corporation statute that would be the same from state to state. *Id.*

One of the great benefits of state legislation of corporation law has been the proliferation of experiments with different approaches to various matters and issues arising in corporation law. “Model,” as opposed to “uniform,” legislation tends to suggest a greater opportunity for departure from the norm, for recognition of special local considerations, and for experimentation with new or different ideas. While there are undoubted benefits to uniform state legislation in areas of interstate commerce such as sales and secured transactions in personal property, these benefits are less significant in corporation law since a corporation can generally be governed by the corporation law of only one state. In any event, in 1943 the Uniform Business Corporation Act was withdrawn as a “uniform” act and was renamed the “Model Business Corporation Act.” *Id.* at 1457. It was finally withdrawn by the uniform laws commissioners altogether in 1958. *Id.*

Meanwhile, in 1950, the Committee on Corporate Laws of the Section of Corporation, Banking and Business Law (now the Corporate Laws Committee of the Business Law Section) of the American Bar Association promulgated its own Model Business Corporation Act. After 1950, the committee continued to review and periodically revise the Model Act. In 1984, after five years of work, publication and wide circulation of an exposure draft for

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comment, and consideration of the many comments received, the Committee published a complete revision of the Model Act. Since 1984, the Committee has continued to review and revise various provisions of the Model Act. In a project culminating in 2016, the Model Act was extensively revised, as more fully described below and as reflected in Appendix B to this Edition.

Today, the Model Act is not only the general corporation statute for more than 30 states and the source of many provisions in the general corporations statutes of states that have not adopted the Model Act in its entirety, it is also an important and often cited reference for courts, lawyers, and scholars as well as a useful source of study and discussion in law schools in the United States and elsewhere.

MODEL ACT INNOVATIONS THROUGH 2010

The Model Act, over the years, has made a number of important innovations to corporate statutory law. These include the following changes that were reflected in the Act as previously published in 2010:

- streamlining of the capital provisions by eliminating the concepts of par value, stated capital, and treasury shares, permitting the consideration for shares to consist of any tangible or intangible benefit to the corporation, and eliminating the distinction among classes of shares and between classes and series (sections 6.01-6.03 and 6.21);
- modernization of statutory financial provisions by establishing clearer tests for determining the legality of all types of distributions to shareholders (section 6.40);
- separation of director standards of conduct (section 8.30) from standards of liability (section 8.31) and inclusion of standards of conduct for officers (section 8.42);
- authorization of a provision in the articles of incorporation exculpating directors from liability for monetary damages to the corporation and its shareholders (section 2.02(b)(4));

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- modernization of the provisions on indemnification of directors and officers (section 2.02(b)(5) and subchapter 8E);
- creation of a new approach with greater certainty for dealing with directors' conflicting interest transactions (subchapter 8F);
- addition of a safe harbor for dealing with director and officer business opportunities (subchapter 8G);
- simplification and updating of the provisions on board and committee composition and procedures (subchapter 8A and section 8.25);
- provision for universal demand for bringing shareholder derivative actions and setting of certain independent determinations as a basis for dismissal of a derivative action (subchapter 7D);
- authorization of bylaw provisions requiring inclusion of shareholder director nominees in a corporation's proxy material and for majority vote for the election of directors (sections 2.06, 7.28, and 10.22);
- authorization of "force the vote" provisions in fundamental transactions by permitting directors to submit matters to shareholders for action without director recommendation (section 8.26);
- inclusion of provisions on shareholder actions that permit shareholder written consents that may be less than unanimous if authorized in the articles of incorporation (section 7.04), remote participation by shareholders in meetings if authorized by the board of directors (section 7.09), and use of bifurcated record dates for notice of a meeting and eligibility to vote to better align ownership and voting (section 7.07);
- authorization of a provision in the articles of incorporation to vary the percentage of shares required

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to call a special meeting of shareholders from the default 10 percent level (section 7.02);

- provision of shareholder inspection rights while minimizing the risk of abuse, and addition of reporting requirements (chapter 16);
- requirement for shareholder approval for issuance of shares, other than for cash, that will result in an increase of more than 20 percent of the voting power of the outstanding shares (section 6.21);
- authorization of statutory share exchanges (section 11.03), provision of mergers and share exchanges between a corporation and a noncorporate entity (chapter 11), and adoption of uniform voting rules for all fundamental changes, including rules regarding separate group voting;
- clarification of when shareholder approval is required for disposition of significant corporate assets by establishing a test of whether the disposition will leave the corporation without a significant continuing business activity and inclusion of a safe harbor if 25 percent of total assets and 25 percent of income or revenue from continuing operations are retained (chapter 12);
- introduction of the concept of domestication to change the state of incorporation and conversion to change the form of entity (chapter 9);
- modernization of the appraisal remedy for dissenting shareholders, including by reintroducing the “market out” provision for noninterested transactions (chapter 13);
- addition of flexibility for nonpublic corporations, including by authorizing shareholders to establish their own governance rules in unanimous shareholder agreements (section 7.32); and
- modernization of the Act to accommodate electronic means of transmission and filing and to recognize electronic signing and delivery (section 1.41).

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HIGHLIGHTS OF CHANGES SINCE THE 2010 PUBLICATION

REVISIONS TO THE STATUTORY PROVISIONS

1. Changes Related to the Uniform Business Organizations Code

Many of the amendments to the Act reflected in the 2016 revision of the Act (the “2016 Act”) stemmed from the 2011 adoption of Article 1 of the Uniform Business Organizations Code (“UBOC”) by the Uniform Law Commission (“ULC”). That uniform legislation contemplates what is commonly described as a “hub and spoke” form of business entity legislation in which a “hub” contains provisions generally applicable to all forms of business entities and a “spoke” contains the substantive provisions for each form of entity. The Committee, as agreed with the ULC, has been preparing a version of the Act that could serve as the “spoke” that governs business corporations for use by jurisdictions that adopt the UBOC. In preparing to create that “spoke,” the Committee decided that the freestanding version of the Act would benefit from revisions that would also make it more compatible with the terminology and concepts used in the UBOC. This decision accounted for many of the changes in chapter 9 (domestication and conversion), chapter 11 (merger and share exchange), and chapter 15 (foreign corporations) of the 2016 Act, as well as corresponding proposed changes in pertinent definitions in chapter 1 of the Act. In particular, chapter 9 was thoroughly revised, with the separate subchapters in the prior version of the Act for non-profit conversion, foreign nonprofit domestication, and entity conversion combined into the general conversion provisions. The most notable change to chapter 15 was the elimination of the concept of qualification to do business and the substitution of foreign corporation registration as a prerequisite to doing business within the state.

The Committee’s work in revising chapters 9 and 11 highlighted two topics on which the prior version of the Act appeared to take unnecessarily divergent approaches: the

treatment of group voting (sometimes known as “class voting”) and “interest holder liability” (referred to in the prior version of the Act as “owner liability”). The Committee reviewed those divergences and, where they seemed unjustified, revised the provisions to make them consistent. For example, in the 2016 Act, where transactions have a similar effect (whether structured as mergers, domestications, or conversions), the existence of a group voting right—and the ability to eliminate that right by a provision of the articles of incorporation—are treated similarly.

The Committee also added the concept of “new interest holder liability” to section 11.04. As revised, that section’s requirement of written consent of shareholders on whom interest holder liability is imposed is not triggered if the transaction alters, but does not increase, preexisting interest holder liability. Similar interest holder liability provisions are included in sections 9.21 and 10.03.

2. *Post-2010 Statutory Provisions*

The 2016 Act contains a number of changes to the Act since its publication in 2010 that reflect recent corporate law developments, including the following:

- addition of a new subchapter E of chapter 1 of the Act, permitting the ratification of defective corporate actions, including actions in connection with the issuance of shares;
- revisions to sections 2.02 and 8.70 to permit corporations to include in their articles of incorporation a provision that limits or eliminates a director’s or an officer’s duty to present a business opportunity to the corporation;
- addition of section 2.08 to permit the articles of incorporation or the bylaws to specify the forum or forums for litigation of internal corporate claims;
- clarifications in section 8.02 of the scope and operation of qualifications for nomination and election as directors;

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- elimination of the requirements in sections 8.53 and 8.54 that a director or officer seeking advancement of expenses provide a written affirmation that he or she has met the applicable standards for indemnification under the Act or, in the case of a director, that the proceeding involves conduct for which liability has been eliminated under the articles of incorporation;
- authorization in section 11.04(j) of the merger of corporations without a shareholder vote following a tender offer if certain conditions are met; and
- revision of section 16.20 and certain other sections of chapter 16 to address, among other things, the obligations of corporations to make financial statements available to shareholders, the maintenance of corporate records, and the inspection rights of shareholders and directors of corporations.

3. Procedures for Approving Fundamental Changes

The Act has long prescribed similar procedural steps for approval of mergers, share exchanges, amendments of the articles of incorporation, disposition of assets not in the ordinary course of business, dissolution, domestication, and conversion. Despite this substantive similarity, the statutory language of the Act varied depending on the form of the transaction. The 2016 Act amended sections 9.21, 9.32 (9.52 in the prior version of the Act), 10.03, 11.04, 12.02, and 14.02, to provide uniform language for the procedural steps for approval of fundamental changes. These revisions eliminated unnecessary variation and the possibility of unintended negative inferences.

4. Distributions in Liquidation

The Act did not clearly articulate the treatment of distributions to shareholders made in the course of liquidation after dissolution of the corporation. Accordingly, the 2016 Act reflected several changes that clarified, among other things, the establishment of a record date for determining shareholders entitled to receive

a distribution in liquidation. Related changes were made in sections 1.40 (defining record date) and 14.09 (director duties).

5. *Quorum and Voting Requirements*

Section 8.24 was amended to clarify the operation of its provisions regarding quorum and voting requirements applicable to the board of directors. The changes eliminated the use of the terms “fixed board size” and “variable-range size board” and substituted what the Committee believed is a clearer formulation in which the denominator for quorum and voting purposes would be the number of directors “specified in or fixed in accordance with the articles of incorporation or bylaws.”

For shareholder meetings, the revision to section 7.25(a) clarified that the articles of incorporation may not provide for a quorum lower than a specified quorum requirement in the Act (for example, the quorum requirement of section 8.63(d) applicable to approval of a director’s conflicting interest transaction by qualified shares and the quorum requirement specified in section 10.03 for amendments to the articles of incorporation).

6. *Corporation Voting Its Own Shares*

Section 7.21(b) of the Act disenfranchised shares held by majority-owned subsidiaries (direct and indirect) of the corporation. The changes to section 7.21 reflected in the 2016 Act more clearly prescribe disenfranchisement for shares in which the corporation has an economic interest, including shares owned by or belonging to the corporation indirectly through entities (corporate and noncorporate) that are controlled by the corporation.

7. *Director Duties and Eliminating the Term “Public Corporation”*

As a result of amendments adopted in 2005, section 8.01 of the Act prescribed “oversight duties” for directors of “public corporations” (as formerly defined in section 1.40). The Committee concluded that such a sharp demarcation of duties between directors of “public corporations” and other corporations has become increasingly artificial, especially in view of federal

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legislation in 2012 permitting a greater number of shareholders before a corporation must become an SEC registrant and the evolution of trading of shares of such non-SEC registrants in alternative, secondary securities markets. Accordingly, the 2016 Act deleted from the text of section 8.01 the specification of particular oversight duties for directors of “public corporations” and placed discussion of those duties in the Official Comment as an elaboration on the more general articulation in section 8.01(b) of the managerial and oversight responsibility of boards of directors. The 2016 Act also deleted the definition of “public corporation” from section 1.40.

Consistent with the deletion of the definition of “public corporation,” sections 7.32 and 10.22 were amended to eliminate the use of that term. Thus, a shareholders’ agreement under section 7.32 no longer automatically ceases to be effective when the corporation becomes a “public corporation.” Of course, the Act’s requirement of unanimous shareholder approval will likely make shareholders’ agreements under section 7.32 unavailable to public corporations as a practical matter, and, in any event, such agreements can still be drafted to effect automatic termination upon occurrence of a specific event such as an initial public offering. Similarly, section 10.22 no longer limits the use of a bylaw requiring a majority vote for election of directors to public companies; the Committee concluded that there was no continuing justification for limiting the flexibility of nonpublic companies to adopt the provision authorized in section 10.22.

8. Venue for Judicial Proceedings

In specifying a judicial remedy with respect to the rights and obligations it creates, the Act before 2016 directed that litigation to obtain such a remedy be commenced in the “appropriate court of the county where the corporation’s principal office (or, if none, its registered office) in this state is located.” Recognizing that many states had developed distinct “business courts” that may be more appropriate venues for such litigation, the 2016 Act enabled legislatures adopting the Act to fix a venue in the court believed to be best suited to handle litigation of the

type in question. Accordingly, former references in the Act to the “appropriate court, etc.” were changed simply to “[name or describe court].”

9. *Effective Date*

The Committee found that the provisions in the prior version of the Act defining when filings and transactions become effective were not internally consistent. The 2016 Act made those provisions more uniform and adopted a definition of “effective date” for filed documents in section 1.40 that applies throughout the Act by referring to section 1.23. Section 1.23 provides definitive rules for when a filing with the secretary of state becomes effective and was revised to improve its clarity.

10. *Shareholders’ Meeting Solely by Remote Participation*

In 2020 the Committee adopted amendments to chapters 7 and 10 permitting the conduct of shareholders’ meetings solely by means of remote participation.

11. *Benefit Corporations*

The Committee has added a new chapter 17 on “benefit corporations.” Benefit corporation statutes allow corporations to opt into a legal structure that expressly expands the purpose of the corporation beyond advancing the interests of its shareholders. Adoption of these statutes is a relatively recent phenomenon, but one that has expanded rapidly. These statutes require directors to consider environmental, social and other effects of corporate activity, and permit their resulting decisions to be based on an assessment of such effects, even at the expense of shareholder value.

CHANGES NOT INTENDED TO HAVE SUBSTANTIVE EFFECT

Many of the changes in the statutory provisions of the Act included in the 2016 Act were stylistic; others were intended to promote internal consistency with the Act’s provisions. The Committee did not intend for any of these changes to have substantive effect through negative implication or otherwise. The following are examples of such changes:

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- The Committee added the following provision to section 10.20:

(c) A shareholder of the corporation does not have a vested property right resulting from any provision in the bylaws.

This addition aligned section 10.20, dealing with bylaws, with section 10.01 of the Act, which disavows the vested rights concept in relation to the articles of incorporation. There should be no implication from adoption of the amendment to section 10.20 that the vested rights concept had any force in relation to bylaws that were in place before the amendment.

- In the Official Comment to various sections (e.g., section 11.04) that refer to provisions enabling a board of directors to submit a matter for shareholder approval without recommending adoption, the Committee deleted language noting that such provisions “are not intended to relieve the board of its duty to consider carefully the proposed transaction and the interests of shareholders.” Elimination of that language should not be interpreted to suggest that the board of directors no longer has such a duty. Rather, the language deleted was unnecessary and potentially confusing, as the Act provides that directors have duties with respect to all of their decisions, not just to decisions regarding submission of matters to shareholders. There is no reason to refer explicitly to those duties in one context while omitting any such reference in connection with the other provisions of the Act that involve decisions by the board of directors.
- The Committee deleted language in former sections 9.24 and 9.55 (corresponding to sections 9.24 and 9.35 of the 2016 Act) to the effect that upon a domestication or conversion a pending action against a corporation continues against the domesticated or converted entity as if the domestication or conversion had not occurred.

That language was not in the corresponding provisions of chapter 11 governing mergers and was unnecessary in view of the provision that liabilities of constituent corporations remain liabilities of the entity resulting from the merger. The deletion of that language was not intended to suggest that an action against a corporation does not continue against the domesticated or converted entity following a domestication or conversion.

- The Official Comment to section 6.28 of the Act formerly noted that this section “may be technically unnecessary,” because “there is no basis for the fear that shares issued properly under section 6.21 can be made assessable because of the subsequent use of the proceeds.” The Official Comment also said, “[t]his section has been rarely cited or referred to in court decisions even though it appears in a large number of state statutes.” The 2016 Act eliminated this unnecessary provision, although there was no intention to reject the proposition for which it has stood—namely, that a corporation may apply the proceeds of a share issuance toward the expenses of selling or underwriting the issuance.

REVISIONS TO THE OFFICIAL COMMENT

The Committee extensively revised the Official Comment to the Act in the 2016 Act so that the commentary functions solely as a guide to the interpretation of the statutory provisions. Thus, the 2016 Act:

- eliminated language in the Official Comment that merely restates operative statutory language;
- eliminated comparisons with prior versions of the Act or with state corporation statutes; and
- eliminated discussion of case law and law review articles.

The latter two points (comparisons with prior and specific versions and cases and scholarship) now appear in this edition of the Annotation.

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OTHER CHANGES

The 2016 Act included a revised and expanded Introduction as well as notes on adoption and revised transitional provisions in chapter 18 (formerly chapter 17) of the Act that were intended to facilitate legislative consideration in adopting the 2016 Act.