Changes in the Model Business Corporation Act—Proposed Amendments to Section 7.23, Definitions in Section 1.40 and Related Sections

By the Corporate Laws Committee, ABA Section of Business Law*

The Corporate Laws Committee of the ABA Section of Business Law (the “Committee”) develops, and from time to time proposes changes in, the Model Business Corporation Act (the “Act” or “Model Act”).

The Committee has approved the changes described in this report on second reading and invites comments from interested persons. Comments should be addressed to A. Gilchrist Sparks, III, Chair, Corporate Laws Committee, 1201 N. Market Street, Wilmington, Delaware 19801-1147, or sent to him by e-mail at asparks@mnat.com. Comments should be received by March 1, 2013, in order to be considered by the Committee before adoption of the amendments on third reading.

Section 7.23 of the Act authorizes a corporation to establish a procedure for recognition of “beneficial owners” (the term currently used in the Act) of its shares. Although the Committee is not aware of the procedure authorized by section 7.23 being used much in practice, and recognizes that the relationship between a public corporation and the beneficial owners of its shares is addressed as a matter of federal securities law, the Committee nevertheless believes that it is useful for state corporation law to continue to allow for recognition of beneficial owners, especially as the separation of record and beneficial ownership of shares of public corporations has increased under the current centralized shareholding system. However, in examining section 7.23, the Committee identified a number of deficiencies, including the failure to reference a “nominee certificate” assumed elsewhere in the Act to be required. The examination of section 7.23 also revealed inconsistencies throughout the Act in the treatment of “beneficial owners” or “beneficial shareholders” (terms sometimes used interchangeably or with differences). This led to consideration of relevant definitions and a need to unify and harmonize those definitions. As a result, the Committee is proposing (i) changes to the definitions in section 1.40 of “shareholder,” “record shareholder,” and “beneficial shareholder” (in place of “beneficial owner”), and to add a definition of “voting trust beneficial owner,” (ii) a revision of section 7.23, and (iii) amendments to various sections of the Act where the foregoing terms are used.

* A. Gilchrist Sparks, III, Chair.
The proposed amendments are set forth below. Changes to the existing provisions are marked with deletions shown by strikeout and additions by underscoring.

1. Amend Section 1.40 and related Official Comments as follows:
   a. Add clause (2A) and Official Comment 1, renumbering existing Official Comment “Conspicuous” to be 1A, as follows:

   (2A) “Beneficial shareholder” means a person who owns the beneficial interest in shares, which may be a record shareholder or a person on whose behalf shares are registered in the name of an intermediary or nominee.

   ***

OFFICIAL COMMENT

1. Beneficial Shareholder

Because various provisions of the Act allow beneficial owners of shares to take actions as a shareholder even in the absence of a beneficial ownership certificate under section 7.23, the term “beneficial shareholder” has been defined in section 1.40(2A).

The definition does not specify what interests are necessary for a person to be a beneficial shareholder, but consistent with section 8-207(a) of the Uniform Commercial Code, it is contemplated that the corporation is entitled to treat the beneficial shareholder as having the full bundle of economic and voting rights associated with the shares. For this reason, the beneficial owner of shares in a voting trust has been defined separately in section 1.40(27A) as a “voting trust beneficial owner.”

Unlike section 7.23, which provides for a procedure to specify a beneficial owner in a beneficial ownership certificate, the definition of “beneficial shareholder” does not prescribe a procedure for establishing beneficial ownership. Where a court proceeding is involved, as it is, for example, in sections 7.41 (derivative proceeding), 13.02 (appraisal rights), and 14.30 (judicial dissolution), the court can determine what is necessary to establish beneficial ownership. In other situations, custom and practice and the reasonable requirements of the corporation should apply. Thus, a certification of a broker-dealer or other financial institution or a current account statement from such an institution often is sufficient to establish beneficial ownership. In the case of a public corporation, a filing with the Securities and Exchange Commission identifying beneficial ownership might be sufficient, as contemplated, for example, by SEC Rule 14a-8 (Question 2).

When shares of a public corporation are held, as explained in the Official Comment to section 7.23, indirectly in street name with a broker-dealer or other financial institution, which may in turn have the shares on deposit with
Depositary Trust Company ("DTC") as a clearing agency, the reference to shares in this Act is technically a reference to a "securities entitlement" under section 8-102(a)(17) of the Uniform Commercial Code, which is an undivided interest in a mass of shares held by the financial intermediary or on deposit with DTC. Nevertheless, the Act and other corporation statutes continue for convenience to refer to the interests as "shares," and thus references to shares should be read to include securities entitlements with respect to those shares.

b. Add clause (19A) and Official Comment 6A as follows:

(19A) “Record shareholder” means (i) the person in whose name shares are registered in the records of the corporation or (ii) the person identified as the beneficial owner of shares in a beneficial ownership certificate pursuant to section 7.23 on file with the corporation to the extent of the rights granted by such certificate.

***

OFFICIAL COMMENT

6A. Record Shareholder

The definition of “record shareholder” in section 1.40(19A), added in 2012, includes a beneficial owner of shares named in a beneficial ownership certificate under section 7.23, but only to the extent of the rights granted the beneficial owner in the certificate—for example, the right to receive notice of, and vote at, shareholders’ meetings. Various substantive sections of the Model Act also permit holders of voting trust certificates or beneficial owners of shares (not subject to a beneficial ownership certificate under section 7.23) to exercise some of the rights of a “shareholder.” See, for example, section 7.40 (derivative proceedings). Separate definitions of “voting trust beneficial owner” and “unrestricted voting trust beneficial owner” (section 1.40(27A)) and “beneficial shareholder” (section 1.40(2A)) also were added for this purpose in 2012.

c. Amend clause (21) and Official Comment 7 to read as follows:

(21) “Shareholder” means, unless varied for purposes of a specific provision, a record shareholder, the person in whose name shares are registered in the records of a corporation or the beneficial owner of shares to the extent of the rights granted by a nominee certificate on file with a corporation.

***

OFFICIAL COMMENT

7. Shareholder

The term definition of “shareholder” is usually used in this Act to mean a “record shareholder” as defined in section 1.40(19A), but the definition of
“shareholder” in section 1.40(21) contemplates that the term may be expanded or limited for purposes of specific provisions, includes a beneficial owner of shares named in a nominee certificate under section 7.23, but only to the extent of the rights granted the beneficial owner in the certificate—for example, the right to receive notice of, and vote at, shareholders’ meetings. Various substantive sections of the Model Act also permit holders of voting trust certificates or beneficial owners of shares (not subject to a nominee certificate under section 7.23) to exercise some of the rights of a “shareholder.” See, for example, section 7.40 (derivative proceedings).

d. Add clause (27A) and Official Comment 12A as follows:

(27A) “Voting trust beneficial owner” means an owner of a beneficial interest in shares of the corporation held in a voting trust established pursuant to section 7.30(a). “Unrestricted voting trust beneficial owner” means, with respect to any shareholder rights, a voting trust beneficial owner whose entitlement to exercise the shareholder right in question is not inconsistent with the voting trust agreement.

***

OFFICIAL COMMENT

12A. Voting Trust Beneficial Owner and Unrestricted Voting Trust Beneficial Owner

Section 1.40(27A) has a separate definition of “voting trust beneficial owner” because the number of them and value of their shares can enter into determinations under sections 13.02(b)(1) and 14.30(b)(ii). It also has a separate definition of “unrestricted voting trust beneficial owner” because rights are given under some provisions of the Act for a beneficial owner of shares deposited in a voting trust established under section 7.30 to take actions as a shareholder. These owners have the economic interest in the shares but the voting rights have been given to the voting trustee. In addition to the typical grant of voting rights, section 7.30 permits the voting trust agreement to confer on the voting trustee the right otherwise to act with respect to the shares, and thus could vest in the trustee the exclusive right to exercise statutory shareholder rights. Accordingly, the 2012 revision uses the term “unrestricted voting trust beneficial owner” to account for this possible limitation. If the voting trust agreement grants the trustee the exclusive right to act with respect to the shareholder right in question, then the voting trustee, and not the voting trust beneficial owner, may exercise those rights.

2. Amend subsection (a)(2) of Section 7.02 and the first paragraph of Comment 1 of the Official Comment as follows:

(2) if the holders of shareholders holding at least 10% of all the votes entitled to be cast on an issue proposed to be considered at the proposed
special meeting sign, date, and deliver to the corporation one or more
written demands for the meeting describing the purpose or purposes
for which it is to be held, provided that the articles of incorporation
may fix a lower percentage or a higher percentage not exceeding
25% of all the votes entitled to be cast on any issue proposed to be con-
sidered. Unless otherwise provided in the articles of incorporation, a
written demand for a special meeting may be revoked by a writing
to that effect received by the corporation prior to the receipt by the cor-
poration of demands sufficient in number to require the holding of a
special meeting.

* * *

OFFICIAL COMMENT

1. Who May Call a Special Meeting

A special meeting may be called under section 7.02(a) by the board of di-
rectors or the person or persons authorized to do so by the articles of incor-
poration or bylaws. Typically, the person or persons holding certain design-
nated offices within the corporation, e.g., the president, chairman of the
board of directors, or chief executive officer, are given authority to call spe-
cial meetings of the shareholders. In addition, the holders of shareholders
holding at least 10% of all the votes entitled to be cast on a proposed
issue at the special meeting may require the corporation to hold a special
meeting by signing, dating, and delivering one or more writings that demand
a special meeting and set forth the purpose or purposes of the desired meet-
ing. That percentage may be decreased or increased (but to not more than
25%) by a provision in the articles of incorporation fixing a different per-
centage. Shareholders demanding a special meeting do not have to sign a
single document, but the writings signed must all describe essentially the
same purpose or purposes. Revocations of written demands will be effective
if delivered to the corporation in the manner contemplated by section 1.41
and received before the corporation receives the requisite number of de-
mands requiring that a special meeting be called. However, revocations re-
ceived after that time will be a nullity and will have no effect. Upon receipt
of demands from holders with the requisite number of votes, the corporation
(through an appropriate officer) must call the special meeting at a reasonable
time and place. The shareholders’ demand may suggest a time and place but
the final decision on such matters is the corporation’s. If no meeting is held
within the time periods specified in section 7.03, the shareholders may
obtain a summary court order under that section requiring that the meeting
be held.

* * *
3. Amend subsection (a)(1) of Section 7.03 by deleting “entitled to participate in an annual meeting” and add new subsection (c), and amend the first paragraph of the Official Comment by adding a new third sentence, as follows:

(1) on application of any shareholder of the corporation entitled to participate in an annual meeting if an annual meeting was not held or action by written consent in lieu thereof did not become effective within the earlier of 6 months after the end of the corporation’s fiscal year or 15 months after its last annual meeting; or

(c) For purposes of subsection (a)(1), “shareholder” means a record shareholder, a beneficial shareholder, and an unrestricted voting trust beneficial owner.

**OFFICIAL COMMENT**

Section 7.03 provides a remedy if the corporation refuses or fails to hold a shareholders’ meeting or action by written consent in lieu thereof is not taken as required by section 7.01 or 7.02 within specified time limits. A shareholder entitled to participate in a meeting may apply for a summary court order to command the holding of a meeting if (1) an annual meeting or action by written consent in lieu thereof is not held within 6 months after the end of the corporation’s fiscal year or 15 months after its last annual meeting, or (2) a special meeting is not properly noticed within 30 days after a valid demand is delivered to the secretary of the corporation or, if properly noticed, is not held in accordance with the notice. Section 7.03(c) provides that the right to apply for a court order for the holding of a meeting applies to record shareholders, beneficial shareholders and unrestricted voting trust beneficial owners. Since a meeting must be held within 60 days of the notice date under section 7.05, the maximum delay between the demand for a special meeting and the right to petition a court for a summary order is 90 days.

4. Amend Section 7.23 and the Official Comment in their entirety by substituting the following:

§ 7.23. SHARES HELD BY INTERMEDIARIES AND NOMINEES

(a) A corporation’s board of directors may establish a procedure by which the beneficial owner of a person on whose behalf shares that are registered in the name of an intermediary or nominee is recognized may elect to be treated by the corporation as the record shareholder by filing with the corporation a beneficial ownership certificate. The extent of this recognition may be determined in the procedure, terms, conditions, and limitations of this treatment.
shall be specified in the procedure. To the extent such person is treated under such procedure as having rights or privileges that the record shareholder otherwise would have, the record shareholder shall not have those rights or privileges.

(b) The procedure may set forth shall specify:

(1) the types of intermediaries or nominees to which it applies;

(2) the rights or privileges that the corporation recognizes in a person with respect to whom a beneficial ownership certificate is filed;

(3) the manner in which the procedure is selected by the nominee, which shall include that the beneficial ownership certificate be signed or assented to by or on behalf of the record shareholder and the person or persons on whose behalf the shares are held;

(4) the information that must be provided when the procedure is selected;

(5) the period for which selection of the procedure is effective;

(6) requirements for notice to the corporation with respect to the arrangement; and

(7) the form and contents of the beneficial ownership certificate.

(c) The procedure may specify any other aspects of the rights and duties created by the filing of a beneficial ownership certificate.

Official Comment

Traditionally, a corporation recognizes only the person in whose name shares are registered as the owner of shares. Indeed, section 1.40 defines “shareholder” basically as the registered owner of shares. But it has become a common practice for persons purchasing shares of a public company to have them registered in the “street name” of a broker-dealer or other financial institution, principally to facilitate transfer by eliminating the need for the beneficial owner’s signature and delivery. In addition, in order to avoid the burdens of processing securities transfers, which caused a crisis in the securities industry in the late 1960s, a system of securities depositories (defined as “clearing corporations” in section 8.102(3) of the Uniform Commercial Code) has been developed. In this system, under which financial institutions deposit securities with the depository, which whose nominee becomes the registered owner of the shares, or the “record shareholder.” Transfers between depositories are then accomplished by book
entry of the depository. As a result, there may be several entities interposed between the corporation and the beneficial owner, with the depository being the registered owner for the account of the brokerage firm that in turn holds the shares for the account of the beneficial owner.

The purpose of section 7.23 is to facilitate direct communication between the corporation and the beneficial owner by authorizing the corporation to create a procedure for bypassing both the registered owner and intermediate brokerage firms, the depository and its intermediary participants or other intermediaries and nominees. The adoption of this procedure is discretionary with each corporation and affirmative action by the corporation's board of directors is necessary to accomplish it. The procedure is also discretionary with the shareholder—ultimate beneficial owner, who must elect, and the intermediary or nominee who holds on behalf of the beneficial owner as record shareholder, who must assent, to follow the applicable procedure prescribed by the corporation. The shareholder retains all rights except those granted to the beneficial owner.

The corporation may limit or qualify the procedure as it deems appropriate. For example, the corporation may:

The signature or assent of the record shareholder and the person or persons on whose behalf the shares are held, as required by subsection (b)(3), can be provided on behalf of any such person by another person authorized to do so. Thus, in a typical situation where the record shareholder is Cede & Co., the nominee of Depository Trust Company, and the shares are ultimately beneficially owned by a shareholder who has an account with a broker-dealer that is a participant in the Depository Trust Company, a beneficial ownership certificate could be signed by both the ultimate beneficial owner and the broker-dealer shown on the position list of Depository Trust Company, acting under authority granted to it by Cede & Co., as the record shareholder. The statute does not prescribe the notices that must be provided to the corporation, but provides that the procedure shall specify whatever notice provisions will be required. For example, the corporation may wish to include provisions for notice to it by the ultimate beneficial owner and the broker-dealer upon the sale or other disposition of the shares, which normally should be accompanied by notice to the corporation of termination or modification of the effect of the beneficial ownership certificate.

The corporation also may limit or qualify the procedure as it deems appropriate. For example, the corporation may:

(1) limit the procedure to certain classes of shareholders, such as depositories, broker-dealers and banks, and their nominees, or make the procedure available to all shareholders, and define requirements to be a beneficial owner eligible to use the procedure;

(2) permit a record shareholder and beneficial owner to adopt the procedure with respect to some but not all of the shares registered or held on behalf of the beneficial owner in the record shareholder's name.
(and in that case the record shareholder continues to be treated as the shareholder with respect to the balance);

(3) specify the purpose or purposes for which the certification beneficial ownership certificate is effective, e.g., for giving notice of, and voting at, shareholders’ meetings, for the distribution of proxy statements and annual reports, or for payment of cash dividends;

(4) specify the form of the certification beneficial ownership certificate, e.g., a written list writing or an electronic file record;

(5) specify the type of information that must be provided, e.g., the name, address, and taxpayer identification number of the person for whose benefit a beneficial owner ownership certificate is filed, and the number of shares registered directly in the shareholder’s name;

(6) establish deadlines for receipt of the certifications after beneficial ownership certificate in connection with the establishment of a record date so that the corporation may schedule its deliveries of notices, proxy statements and other communications; or

(7) provide that a new certification beneficial ownership certificate is required following in connection with each record date or that a certification beneficial ownership certificate as of a certain date may continue until changed by the certifying shareholder person or persons.

This listing is illustrative and not exhaustive. It is expected that experimentation with various devices under this section may reveal other areas which the corporation’s plan should address.

Adoption of the amendments to section 7.23 in 2012 specifying in subsection (b) requirements for the procedure is not intended to affect the validity of a procedure previously adopted under any prior version of section 7.23.

The definition of “record shareholder” in section 1.40(19A) includes beneficial owners to the extent they obtain the rights of record shareholders through the filing of a beneficial ownership certificate pursuant to the procedure authorized by this section.

5. Amend subsection (b)(2) of Section 7.29A as follows:

(2) a any record shareholder of the corporation, which for purposes of this section includes a beneficial owner of shares whose shares are

---

held in a shareholder, or unrestricted voting trust or held by a nominee on the beneficial owner’s behalf owner of the corporation;

6. Amend clause (2) of Section 7.40 and the second paragraph of the Official Comment as follows:

(2) “Shareholder” includes means a beneficial owner record shareholder, whose shares are held in a voting trust or held by a nominee on the beneficial owner’s behalf shareholder, and an unrestricted voting trust beneficial owner.

* * *

OFFICIAL COMMENT

* * *

The definition of “shareholder,” which applies only to subchapter D, includes all beneficial owners and therefore goes beyond the definition in section 1.40(22) which includes only record holders and beneficial owners who are certified by a nominee pursuant to the procedure specified in section 7.23. Similar definitions are found in section 13.01 (appraisal rights) and section 16.02(f) (inspection of records by a shareholder). In the context of subchapter D, extends the right to bring a derivative proceeding to a beneficial shareholder and an unrestricted voting trust beneficial owner means a person having a direct economic interest in the shares. The definition is not intended to adopt the broad definition of beneficial ownership in SEC Rule 13d-2 under the Securities Exchange Act of 1934, 17 C.F.R. § 240.13d-2, which includes persons with the right to vote or dispose of the shares even though they have no. The inclusion of beneficial shareholder and unrestricted voting trust beneficial owner recognizes that these persons have or hold on behalf of others an economic interest in the shares.

7. Amend Section 7.48 by adding a new subsection (g) and add a new paragraph to the Official Comment as follows:

(g) In this section, “shareholder” means a record shareholder, a beneficial shareholder, and an unrestricted voting trust beneficial owner.

OFFICIAL COMMENT

* * *

Section 7.48(g) extends the right to seek court appointment of a custodian or receiver to a beneficial shareholder and an unrestricted voting trust beneficial owner. This recognizes that these persons have or hold on behalf of others an economic interest in the shares.
8. Amend subsection (c) of Section 8.63 by changing clause (1) to read as follows:

(c) For purposes of this section: (1) “holder” means and “held by” refers to shares held by both a record shareholder (as defined in section 13.01(7)) and a beneficial shareholder, (as defined in section 13.01(2)) and an unrestricted voting trust beneficial owner; and (2) “qualified shares” means all shares entitled to be voted with respect to the transaction except for shares that the secretary or other officer or agent of the corporation authorized to tabulate votes either knows, or under subsection (b) is notified, are held by (A) a director who has a conflicting interest respecting the transaction or (B) a related person of the director (excluding a person described in clause (vi) of Section 8.60(5)).

9. Amend Section 13.01 by deleting clauses (2) and (7) and changing clause (9) to read as set forth below, and amend Comment 2 of the Official Comment by deleting the comment entitled “Beneficial Shareholder,” changing the fourth sentence of the second paragraph under “Interested Transaction” to read as set forth below, and by substituting for the Comment under “Shareholder” the following:

§ 13.01. Definitions

In this chapter:

* * *

(2) “Beneficial shareholder” means a person who is the beneficial owner of shares held in a voting trust or by a nominee on the beneficial owner’s behalf.

* * *

(7) “Record shareholder” means the person in whose name shares are registered in the records of the corporation or the beneficial owner of shares to the extent of the rights granted by a nominee certificate on file with the corporation.

* * *

(9) “Shareholder” means both a record shareholder, and a beneficial shareholder, and a voting trust beneficial owner.

* * *

Official Comment

* * *

2. Definitions

Section 13.01 contains specialized definitions applicable only to chapter 13.
Beneficial Shareholder

The definition of “beneficial shareholder” means a person who owns the beneficial interest in shares; “shares” is defined in section 1.40(22) to include, without limitation, a holder of a depository receipt for shares. Similar definitions are found in section 7.40(2) (derivative proceedings) and section 16.02(f) (inspection of records by a shareholder). In the context of chapter 13, beneficial shareholder means a person having a direct economic interest in the shares. The definition is not intended to adopt the broad definition of beneficial ownership in SEC Rule 13d-2, which includes persons with a right to vote or dispose of the shares even though they have no economic interest in them. However, section 13.02(b)(5) includes the concept of the right to vote in determining whether the event represents a conflict transaction that renders the market exception unavailable.

* * *

Interested Transaction

* * *

Section 13.01(5.1)(i)(A) covers the acquisition or exchange of shares or assets of the corporation by a shareholder or an affiliate of the shareholder that could be considered controlling by virtue of ownership of a substantial amount of voting stock (20%). Section 13.01(5.1)(i)(B) covers the acquisition or exchange of shares or assets of the corporation by an individual or group, or by an affiliate of such individual or group, that has the ability to exercise control, through contract, stock ownership, or some other means, over at least one fourth of the board’s membership. The definition of “beneficial owner” in section 13.01(5.1)(ii) serves to identify possible conflict situations by deeming each member of a group that agrees to vote in tandem to be a beneficial owner of all the voting shares owned by the group. In contrast, the term “beneficial shareholder,” as defined in section 13.01(21.40(2A), is used to identify those persons entitled to appraisal rights. The exclusions of “excluded shares,” as defined in subsection (5.1)(iii), in subsections (5.1)(i)(A) and (B) recognize that an acquisition effected in two steps (a tender offer followed by a merger) within one year, where the two steps are either on the same terms or the second step is on terms that are more favorable to target shareholders, is properly considered a single transaction for purposes of identifying conflict transactions, regardless of whether the second-step merger is governed by section 11.04 or 11.05.

* * *

Shareholder

The definition of “shareholder” in section 13.01(9) for purposes of chapter 13 differs from the definition of that term used elsewhere in the Model Act. Section 1.40(21) defines “shareholder” as used generally in the Act to mean only a “record shareholder”; that term is specifically defined in section 13.01(7). Section
13.01(0), on the other hand, defines “shareholder” to include not only a “record shareholder” but also a “beneficial shareholder,” a term that is itself defined in section 13.01(2). The specially defined term extends to beneficial shareholders and voting trust beneficial owners the right to take advantage of the provisions of this chapter with respect to appraisal, subject to their fulfilling the applicable requirements of this chapter. This recognizes that these persons have or hold on behalf of others an economic interest in the shares. Use of the term “beneficial shareholder” for this purpose is to be contrasted with use of the term “beneficial owner” in section 13.01(5.1) to identify possible conflict situations. The distinction between “record shareholder” and “beneficial shareholder” appears primarily in section 13.03, which establishes the manner in which beneficial shareholders, and record shareholders who are acting on behalf of beneficial shareholders, perfect appraisal rights. The word “shareholder” is used generally throughout chapter 13 in order to permit both record and beneficial shareholders to take advantage of the provisions of this chapter, subject to their fulfilling the applicable requirements of this chapter.

10. Amend clause (ii) of subsection (b)(1) of Section 13.02 to add “voting trust beneficial owner” and the last sentence of the second paragraph of Comment 2. of the Official Comment as follows:

§ 13.02. Right to Appraisal

* * *

(b) Notwithstanding subsection (a), the availability of appraisal rights under subsections (a)(1), (2), (3), (4), (6), and (8) shall be limited in accordance with the following provisions:

(1) Appraisal rights shall not be available for the holders of shares of any class or series of shares which is:

* * *

(ii) traded in an organized market and has at least 2,000 shareholders and a market value of at least $20 million (exclusive of the value of such shares held by the corporation’s subsidiaries, senior executives, directors, and beneficial shareholders and voting trust beneficial owners owning more than 10% of such shares); or

* * *

Official Comment

* * *
2. Market Out to Appraisal Rights

* * *

For purposes of this chapter, the market out is provided for a class or series of shares if two criteria are met: the market in which the shares are traded must be “liquid” and the value of the shares established by the appraisal-triggering event must be “reliable.” Except as provided in section 13.02(b)(1)(iii), liquidity is addressed in section 13.02(b)(1) and requires the class or series of stock to satisfy either one of two requirements: (1) The class or series must be a covered security under section 18(a)(1)(A) or (B) of the Securities Act of 1933. This means that it must be listed on the New York Stock Exchange or the American Stock Exchange, or on the NASDAQ Global Select Market or the NASDAQ Global Market (successors to the NASDAQ National Market), or on certain other markets having comparable listing standards as determined by the Securities and Exchange Commission. (2) If not in these categories, the class or series must be traded in an organized market and have at least 2,000 record or beneficial shareholders or voting trust beneficial owners (provided that using both these concepts does not result in duplication) and have a market value of at least $20 million, excluding the value of shares held by the corporation’s subsidiaries, senior executives, directors, and beneficial shareholders and voting trust beneficial owners owning more than 10% of the class or series.

11. Amend Section 13.03 and the Official Comment by substituting the following:

§ 13.03. Assertion of Rights by Nominees and Beneficial Owners

(a) A record shareholder may assert appraisal rights as to fewer than all the shares registered in the record shareholder’s name but owned by a beneficial shareholder or a voting trust beneficial owner only if the record shareholder objects with respect to all shares of the class or series owned by the beneficial shareholder or the voting trust beneficial owner and notifies the corporation in writing of the name and address of each beneficial shareholder or voting trust beneficial owner on whose behalf appraisal rights are being asserted. The rights of a record shareholder who asserts appraisal rights for only part of the shares held of record in the record shareholder’s name under this subsection shall be determined as if the shares as to which the record shareholder objects and the record shareholder’s other shares were registered in the names of different record shareholders.

(b) A beneficial shareholder and a voting trust beneficial owner may assert appraisal rights as to shares of any class or series held on behalf of the shareholder only if such shareholder:
(1) submits to the corporation the record shareholder's written consent to the assertion of such rights no later than the date referred to in section 13.22(b)(2)(ii); and

(2) does so with respect to all shares of the class or series that are beneficially owned by the beneficial shareholder or the voting trust beneficial owner.

**Official Comment**

Section 13.03 addresses the relationship between those who are entitled to assert appraisal rights and the widespread practice of nominee or street name ownership of publicly held shares. Generally, a shareholder must demand appraisal for all the shares of a class or series which the shareholder owns. If a record shareholder is a nominee for several beneficial shareholders, some of whom wish to demand appraisal and some of whom do not, section 13.03(a) permits the record shareholder to assert appraisal rights with respect to a portion of the shares held of record by the record shareholder but only with respect to all the shares beneficially owned by a single person. The same rule applies to shares held by voting trustees. This limitation is necessary to prevent abuse by a single beneficial shareholder who is not fundamentally opposed to the proposed corporate action but who may wish to speculate on the appraisal process, as to some of that shareholder’s shares, on the possibility of a high payment. On the other hand, a shareholder who owns shares in more than one class or series may assert appraisal rights for only some but not all classes or series that the shareholder owns. This is permitted because fair treatment of one class or series does not guarantee fair treatment of other classes or series.

Section 13.03(a) also requires a record shareholder who demands appraisal with respect to a portion of the shares held by the record shareholder to notify the corporation of the name and address of the beneficial owner or voting trust beneficial owner on whose behalf the record shareholder has demanded appraisal rights.

Section 13.03(b) permits a beneficial shareholder or voting trust beneficial owner to assert appraisal rights directly if the beneficial shareholder or voting trust beneficial owner submits the record shareholder's written consent. Although generally the record shareholder is treated as the owner of shares, this section recognizes that sometimes the record shareholders are holding shares on behalf of beneficial shareholders. It would be foreign to the premises underlying nominee and street name ownership to require these record shareholders to forward demands and participate in litigation on behalf of their clients. Similarly, voting trustees hold shares on behalf of voting trust beneficial owners and may want to or be required to pass the decision on asserting appraisal rights on to the voting trust beneficial owners. In order to make appraisal rights effective without burdening record shareholders, beneficial shareholders and voting trust beneficial owners should be allowed to assert their own claims.
as provided in this subsection. The beneficial shareholder or voting trust beneficial owner is required to submit, no later than the date specified in section 13.22(b)(2)(ii), a written consent by the record shareholder to the assertion of appraisal rights to verify the beneficial shareholder’s entitlement and to permit the protection of any security interest in the shares. In practice, a broker’s customer who wishes to assert appraisal rights may request the broker to supply the customer with the name of the record shareholder (which may be a house nominee or a nominee of the Depository Trust Company), and a form of consent signed by the record shareholder. At the same time, the customer may want to obtain certificates for the shares so that they may be deposited pursuant to section 13.23. After the corporation has received the form of consent, the corporation must deal with the beneficial shareholder or, in the case of a voting trust, the voting trust beneficial owner.

12. Amend the last paragraph of the Official Comment to Section 13.21 by adding “voting trust beneficial owner” to read as follows:

**OFFICIAL COMMENT**

***

In order for a shareholder to remain eligible to demand payment, section 13.21(a)(2) mandates that the shareholder must not vote (or, in the case of a beneficial shareholder or a voting trust beneficial owner, cause or permit to be voted) any shares of any class or series for which the shareholder is demanding appraisal in favor of the proposal.

13. Amend subsections (b) and (c) of Section 14.30 and the first paragraph of Comment 2 of the Official Comment to add new second and third sentences as follows:

(b) Section 14.30(a)(2) shall not apply in the case of a corporation that, on the date of the filing of the proceeding, has shares which are:

(i) listed on the New York Stock Exchange, the American Stock Exchange or on any exchange owned or operated by the NASDAQ Stock Market LLC, or listed or quoted on a system owned or operated by the National Association of Securities Dealers, Inc.; or

(ii) a covered security under section 18(b)(1)(A) or (B) of the Securities Act of 1933, as amended; or

(i) not so listed or quoted a covered security, but are held by at least 300 shareholders and the shares outstanding have a market value of at least $20 million (exclusive of the value of such shares held by the corporation’s subsidiaries, senior executives, directors, and
beneficial shareholders and voting trust beneficial owners owning more than 10% of such shares).

(c) In subsection (a) of this section, “beneficial shareholder” has the meaning specified in section 13.01(2). “Shareholder” means a record shareholder, a beneficial shareholder, and an unrestricted voting trust beneficial owner; in subsection (b) of this section, “shareholder” means a record shareholder, a beneficial shareholder, and a voting trust beneficial owner.

OFFICIAL COMMENT

* * *

2. Involuntary Dissolution by Shareholders

Section 14.30(a)(2) provides for involuntary dissolution at the suit of a shareholder under circumstances involving deadlock or significant abuse of power by controlling shareholders or directors. Section 14.30(c) extends the ability to seek judicial dissolution to beneficial shareholders and unrestricted voting trust beneficial owners. This is because these persons have or hold on behalf of others an economic interest in the shares. The remedy of judicial dissolution under section 14.30(a)(2) is appropriate only for shareholders of corporations that are not widely held. Even in those situations, however, the court can take into account the number of shareholders and the nature of the trading market for the shares in deciding whether to exercise its discretion to order dissolution. Shareholders of corporations that meet the tests of section 14.30(b) will normally have the ability to sell their shares if they are dissatisfied with current management. In addition, (i) they may seek traditional remedies for breach of fiduciary duty; (ii) they may seek judicial removal of directors in case of fraud, gross abuse of power, or the intentional infliction of harm on the corporation, under section 8.09, or (iii) in the narrow circumstances covered in section 7.48(a), if irreparable injury is occurring or threatened, they may seek the appointment of a custodian or receiver outside the context of a dissolution proceeding. In contrast, a resort to litigation may result in an irreparable breach of personal relationships among the shareholders of a nonpublic corporation, making it impossible for them to continue in business to their mutual advantage, and making liquidation and dissolution (subject to the buy-out provisions of section 14.34) the appropriate solution. The grounds for dissolution under section 14.30(a)(2) are broader than those required to be shown for the appointment of a custodian or receiver under section 7.48(a). The difference is attributable to the different focus of the two proceedings. While some of the grounds listed in 14.30(a)(2), such as deadlock, may implicate the welfare of the corporation as a whole, the primary focus is on the effect of actions by those in control on the value of the complaining shareholder’s individual investment: for example, the
“oppression” ground in section 14.30(a)(2)(ii) is often cited in complaints for dissolution and generally describes action directed against a particular shareholder. In contrast, the primary focus of an action to appoint a custodian or receiver under section 7.48(a) is the corporate entity, and the action is intended to protect the interests of all shareholders, creditors and others who may have an interest therein. In other instances, action that is “illegal” or “fraudulent” under 14.30(a)(2) may be severely prejudicial to the interests of the individual complaining shareholder, whereas conduct that is illegal with respect to the corporation may be remedied by other causes of action available to shareholders, and “fraudulent” conduct or a board deadlock under section 7.48(a) must be accompanied by or threaten irreparable harm to warrant the appointment of a custodian or receiver. An action under section 7.48(a) may be brought by a shareholder of any corporation.

14. Amend subsection (g) of Section 16.02 and Comment 6 of the Official Comment to read as follows:

(g) For purposes of this section, “shareholder” includes a beneficial owner whose shares are held in a voting trust or by a nominee on the shareholder’s behalf, a record shareholder, a beneficial shareholder, and an unrestricted voting trust beneficial owner.

OFFICIAL COMMENT

* * *

6. Section 16.02(g)

Section 16.02(g) extends the inspection rights provided by section 16.02 to beneficial owners of shares held by a nominee or in a shareholders and unrestricted voting trust beneficial owners. It was added as a technical correction to the revised Model Act in 1986.