

June 15, 2014

Providing for the Ratification of Defective
Corporate Action, Oregon State Bar Legislative
Proposal (2014), citing Bigler & Tillman's Void or
Voidable? -- Curing Defects in Stock Issuances
Under Delaware Law

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OREGON STATE BAR
Legislative Proposal
Part I – Legislative Summary

RE: PROVIDING FOR THE RATIFICATION OF DEFECTIVE CORPORATE ACTION

Submitted by: Business Law Section Executive Committee

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1. Does this amend current law or program?

a. Yes ☒ Add new ORS Statute sections:

ORS 60.972 – Ratification of defective corporate acts

ORS 60.973 – Proceedings regarding validity of defective corporate acts and putative shares.

Amend the following ORS statues:

ORS 60.011 – Effective date and time of document

ORS 60.084 – Validity of corporate acts

ORS 60.207 – Court-ordered meeting

b. No ☐

2. PROBLEM PRESENTED (including level of severity):

Oregon has no statutory procedure for correcting defective corporate action. When an Oregon corporation's directors or shareholders take corporate action without proper authorization, or without strictly adhering to corporate formalities, that action is likely, or at least could be, invalid. For example, the issuance of stock in excess of the number of shares authorized in the corporation's articles of incorporation, the subsequent election of directors by the shareholders, and corporate action later approved by the defective board may all be invalid corporate actions. Upon realizing the potential invalidity of past corporate acts, a company's directors or shareholders may wish to fix the problem by ratifying the defective acts. However, Oregon law is unclear about what defective acts can be ratified after the fact.

While there is little legal precedent in Oregon law on this issue, case law in some jurisdictions has developed a distinction between corporate acts that are "void" and incapable of ratification and cure, and acts that are merely "voidable" and may be ratified and cured. According to the U.S. Court of Appeals for the D.C. Circuit, "[T]he essential distinction between voidable and void acts are that those acts which the corporation could accomplish lawfully but which it has undertaken to accomplish in an inappropriate manner are voidable. Acts which the corporation could not accomplish lawfully, no matter how undertaken, are void and cannot be cured." *CarrAmerica Realty Corp. v. Kaidanow*, 321 F.3d 165, 170 (D.C. Cir. 2003). The distinction is not a clear one, however, and there remains no definite line between which defective corporate acts may be cured and which may not. *See, e.g., Staar Surgical Co. v. Waggoner*, 588 A.2d 1130, 1136 (Del. 1991); Bigler & Tillman, *Void or Voidable?—Curing*

This lack of clarity led the Delaware legislature to recently amend the Delaware General Corporation Law to allow for ratification of defective corporate acts. Under the amendment, which took effect April 1, 2014, invalid corporate actions can be ratified through board and shareholder resolutions if specific criteria are met. Providing a statutory procedure to ratify defective corporate acts gives certainty and clarity to an otherwise opaque area of law. Delaware's new law protects shareholders by requiring a strict ratification procedure and at the same time eliminates the unclear distinction between void and voidable corporate acts: all corporate acts may be ratified and cured. The Delaware law also provides a procedure for contesting ratification where appropriate.

Oregon has no substantive case law distinguishing between void and voidable corporate acts and no statute that provides a procedure for curing defective corporate actions. This uncertainty may hamper an Oregon business's ability to raise capital or conduct its business because a prior defective action may taint future corporate actions.

3. SOLUTION:

Add new sections to the Oregon Business Corporation Act, modeled after the Delaware amendments, to provide a procedure for ratification of defective shareholder or director corporate action and a process for affected parties to contest the ratification.

Substantially similar changes are proposed for the Oregon Professional Corporation Act.

OREGON STATE BAR
Legislative Proposal
Part II – Legislative Language

Please provide your legislative language below:

O.R.S. § 60.011 Effective date and time of document [Inserted language in bold, deleted language with strikethrough]

(1) Except as provided in subsection (2) of this section, ~~and~~ ORS 60.014(3), **60.972(1)(a)(G) and 60.973(2)(a)**, a document accepted for filing is effective on the date it is filed by the Secretary of State and at the time, if any, specified in the document as its effective time or at 12:01 a.m. on that date if no effective time is specified.

(2) If a document specifies a delayed effective time and date, the document becomes effective at the time and date specified. If a document specifies a delayed effective date but no time, the document becomes effective at 12:01 a.m. on that date. A delayed effective date for a document may not be later than the 90th day after the date it is filed.

O.R.S. § 60.084 Validity of corporate acts [Inserted language in bold]

(1) Except as provided in subsection (2) of this section **or ORS 60.973**, the validity of corporate action may not be challenged on the ground that the corporation lacks or lacked power to act.

(2) A corporation's power to act may be challenged:

(a) In a proceeding by a shareholder against the corporation to enjoin the act;

(b) In a proceeding by the corporation, directly, derivatively, or through a receiver, trustee or other legal representative against an incumbent or former director, officer, employee or agent of the corporation; or

(c) In a proceeding by the Attorney General under ORS 60.661.

(3) In a shareholder's proceeding under subsection (2)(a) of this section to enjoin an unauthorized corporate act, the court may enjoin or set aside the act, if equitable and if all affected persons are parties to the proceeding, and may award damages for loss other than anticipated profits suffered by the corporation or another party because of enjoining the unauthorized act.

O.R.S. § 60.207 Court-ordered meeting [Inserted language in bold, deleted language with strikethrough]

(1) The circuit court of the county where a corporation's principal office is located, or, if the principal office is not in this state, where the registered office of the corporation is or was last located, may summarily order a meeting to be held:

(a) On application of any shareholder of the corporation entitled to participate in an annual meeting if an annual meeting was not held within the earlier of six months after the end of the corporation's fiscal year or 15 months after its last annual meeting; ~~or~~

(b) On application of a shareholder who signed a demand for a special meeting valid under ORS 60.204 and notice of the special meeting was not given within 30 days after the date the demand was delivered to the corporation's secretary or the special meeting was not held in accordance with the notice; **or**

(c) In accordance with ORS 60.973(2)(g).

(2) The court may fix the time and place of the meeting, determine the shares entitled to participate in the meeting, specify a record date for determining shareholders entitled to notice of and to vote at the meeting, prescribe the form and content of the meeting notice, fix the quorum required for specific matters to be considered at the meeting or direct that the votes represented at the meeting constitute a quorum for action on those matters and enter other orders necessary to accomplish the purpose or purposes of the meeting.

(3) The shareholders' request shall be set for hearing at the earliest possible time and shall take precedence over all matters, except matters of the same character and hearings on preliminary injunctions under ORCP 79 B(3). No order shall be issued by the court under this section without notice to the corporation at least five days in advance of the time specified for the hearing unless a different period is fixed by order of the court.

O.R.S. § 60.972 Ratification of defective corporate acts [New ORS statute section added]

(1)(a) As used in this section and in ORS 60.973 only, the term:

(A) "Adopted resolutions" means the resolution(s) ratifying one or more defective corporate acts that are duly adopted by the corporation's board of directors in accordance with subsection (3) of this section.

(B) "Defective corporate act" means an overissue, an election or appointment of directors that is void or voidable due to a failure of authorization or any act or transaction purportedly taken by or on behalf of the corporation that is, and at the time the act or transaction was purportedly taken would have been, within the power of a corporation under this chapter, but is void or voidable due to a failure of authorization.

(C) "Failure of authorization" means the failure to authorize or effect an act or transaction in compliance with the provisions of this chapter, the articles of incorporation or bylaws of the corporation or any plan or agreement to which the

corporation is a party, if and to the extent the failure would render the act or transaction void or voidable.

(D) "Overissue" means the purported issuance of:

- (i) Shares of a class or series in excess of the number of shares of such class or series the corporation has the power to issue under ORS 60.137(1) and 60.147 at the time of the issuance; or
- (ii) Shares of any class or series that is not then authorized for issuance by the articles of incorporation of the corporation.

(E) "Putative shares" means the shares of any class or series of the corporation (including shares issued upon exercise of options, rights, warrants or other securities convertible into shares of the corporation, or interests with respect thereto that were created or issued pursuant to a defective corporate act) that:

- (i) But for any failure of authorization, would constitute valid shares; or
- (ii) Cannot be determined by the board of directors to be valid shares.

(F) "Time of the defective corporate act" means the date and time the defective corporate act was purported to have been taken.

(G) "Validation effective time" with respect to any defective corporate act ratified pursuant to this section means the later of:

- (i) The time at which the adopted resolutions submitted to the shareholders for approval pursuant to subsection (5) of this section are approved by the shareholders, or if no vote of shareholders is required to approve the adopted resolutions, the time at which the notice required by subsection (6) of this section is given; and
- (ii) The time at which a certificate of validation filed pursuant to subsection (7) of this section becomes effective in accordance with ORS 60.011.

(H) "Valid shares" means the shares of any class or series of the corporation that have been duly authorized and validly issued in accordance with this chapter.

(b) In the absence of actual fraud in the transaction, the judgment of the board of directors that shares are valid shares or putative shares is conclusive, unless otherwise determined by a circuit court in a proceeding brought pursuant to ORS 60.973.

(2) Subject to subsection (8) of this section, no defective corporate act or putative shares is or are void or voidable solely as a result of a failure of authorization if ratified as provided in this section or validated by a circuit court in a proceeding brought under ORS 60.973.

(3) (a) To ratify a defective corporate act pursuant to this section, the board of directors of the corporation must adopt one or more resolutions setting forth:

(A) The defective corporate act to be ratified;

(B) The date the defective corporate act occurred;

(C) If the defective corporate act involved the issuance of putative shares, the number and type of putative shares issued and the date(s) upon which the putative shares were purported to have been issued;

(D) The nature of the failure of authorization in respect of the defective corporate act to be ratified; and

(E) That the board of directors approves the ratification of the defective corporate act.

(b) The quorum and voting requirements applicable to the board of directors adopting the resolution(s) proposed pursuant to subsection 3(a) of this section are the quorum and voting requirements applicable at the time of such adoption for the type of defective corporate act proposed to be ratified; provided that if the articles of incorporation or bylaws of the corporation, any plan or agreement to which the corporation was a party or any provision of this chapter, in each case as in effect as of the time of the defective corporate act, would have required attendance by a greater number of directors or specified directors for a quorum to be present or to approve the defective corporate act, such greater number of directors or specified directors are required for a quorum to be present or to adopt the resolution(s) proposed pursuant to subsection 3(a) of this section, as applicable, except that the presence or approval of any director elected, appointed or nominated by holders of any class or series of which no shares are then outstanding, or by any person that is no longer a shareholder, is not required.

(c) The adopted resolutions may also provide that, at any time before the validation effective time, notwithstanding approval of the adopted resolutions by shareholders as provided in subsection (5) of this section, the board of directors may abandon the adopted resolutions without further action of the shareholders.

(4) The adopted resolutions must be submitted to shareholders of the corporation for approval as provided in subsection (5) of this section, unless:

(a) No other provision of this chapter, and no provision of the articles of incorporation or bylaws of the corporation, or of any plan or agreement to which the corporation is a party, would have required shareholder approval of the defective corporate act to be ratified, either at the time of the defective corporate act or at the time when the adopted resolutions are adopted by the board of directors; and

(b) The defective corporate act to be ratified did not result from a failure to comply with ORS 60.835.

(5) If subsection (4) of this section requires that the adopted resolutions be submitted to shareholders, due notice of the time, place, if any, and purpose of the meeting must be given at least 20 days but no more than 60 days before the date of the meeting to each holder of valid shares and putative shares, whether voting or nonvoting, of record as of the date the adopted resolutions were adopted pursuant to subsection (3) of this section, at the address of such holder as it appears or most recently appeared, as appropriate, on the records of the corporation. The notice must also be given to the holders of valid shares and putative shares, whether voting or nonvoting, of record as of the time of the defective corporate act, other

than holders whose identities or addresses cannot be determined from the records of the corporation. The notice must contain a copy of the adopted resolutions and a statement that any claim that the defective corporate act or putative shares to be ratified by the adopted resolutions is void or voidable due to the identified failure of authorization, or any claim that the circuit court should declare in its discretion that a ratification in accordance with this section is not effective or is effective only on specified conditions, must be brought within 120 days after the validation effective time. The quorum and voting requirements applicable to the approval of adopted resolutions by the shareholders are the quorum and voting requirements applicable at the time of the shareholders' approval for the type of defective corporate act to be ratified, except that:

- (a) If the articles of incorporation or bylaws of the corporation, any plan or agreement to which the corporation was a party or any provision of this chapter in effect as of the time of the defective corporate act would have required a greater number of shares or of any class or series thereof or specified shareholders for a quorum to be present or to approve the defective corporate act, the presence or approval of such greater number of shares or of such class or series thereof or such specified shareholders is required for a quorum to be present or to approve the adopted resolutions, as applicable, except that the presence or approval of shares of any class or series of which no shares are then outstanding, or of any person that is no longer a shareholder, is not required;
 - (b) The approval of adopted resolutions ratifying the election of a director requires the affirmative vote of the majority of shares present at the meeting and entitled to vote on the election of such director, except that if the articles of incorporation or bylaws of the corporation then in effect or in effect at the time of the defective election require or required a greater number of shares to elect such director, the affirmative vote of such greater number of shares is required to ratify the election of such director; and
 - (c) In the event of a failure of authorization resulting from failure to comply with the provisions of ORS 60.835, the ratification of the defective corporate act requires the shareholder vote set forth in ORS 60.835(3), regardless of whether such vote would have otherwise been required.
- (6) If notice of the adopted resolutions was not required to be, and was not in fact, given in accordance with subsection (5) of this section, prompt notice of the board of directors' adoption of the adopted resolutions must be given to all holders of valid shares and putative shares, whether voting or nonvoting, as of the date the adopted resolutions were adopted by the board of directors, not later than 60 days after the date of such adoption, as established by the board of directors, at the address of such holder as it appears or most recently appeared, as appropriate, on the records of the corporation. The notice must also be given to the holders of record of valid shares and putative shares, whether voting or nonvoting, as of the time of the defective corporate act, other than holders whose identities or addresses cannot be determined from the records of the corporation. The notice must contain a copy of the adopted resolutions and a statement that any claim that the defective corporate act or putative shares ratified under this section is void or voidable due to the identified failure of authorization, or any claim that the circuit court should declare in its discretion that a ratification in accordance with this section is not effective or is effective only on certain conditions, must be brought within 120 days after the validation effective time. Solely for purposes of subsections (5) and (6) of this section, notice to holders of putative shares, and notice to holders of valid shares and putative shares as of the time of the defective corporate

act, constitutes notice to holders of valid shares for purposes of ORS 60.034, 60.214 and 60.217.

(7) If the defective corporate act ratified pursuant to this section would have required under any other section of this chapter the filing of a document with the Secretary of State in accordance with ORS 60.004, then, whether or not a document was previously filed in respect of the defective corporate act and in lieu of filing the document otherwise required by this chapter, the corporation must file a certificate of validation in accordance with ORS 60.004. The certificate of validation must set forth:

(a) The adopted resolutions, the date the board of directors adopted the adopted resolutions, the date the shareholders approved the adopted resolutions if applicable, and a statement that the adopted resolutions were duly adopted and approved in accordance with this section;

(b) If a document was previously filed under ORS 60.004 in respect of the defective corporate act, the chapter and date of filing of such prior document and any articles of correction thereto filed in accordance with ORS 60.014; and

(c) Any other provisions required under any other section of this chapter to be included in the document that otherwise would have been required to be filed pursuant to this chapter with respect to such defective corporate act.

(8) From and after the validation effective time, unless otherwise determined in an action brought pursuant to ORS 60.973:

(a) Each defective corporate act set forth in the adopted resolutions is no longer void or voidable as a result of a failure of authorization identified in the adopted resolutions and such effect is retroactive to the time of the defective corporate act; and

(b) Each share or fraction of a share of putative shares issued or purportedly issued pursuant to a defective corporate act that is identified in the adopted resolutions is no longer void or voidable as a result of a failure of authorization identified in the adopted resolutions and is deemed to be an identical share or fraction of a share of outstanding shares as of the time it was purportedly issued.

(9) Ratification under this section or validation under ORS 60.973 is not the exclusive means of ratifying or validating any act or transaction taken by or on behalf of the corporation, including any defective corporate act, or any issuance of shares, including any putative shares, and the absence or failure of ratification in accordance with either this section or validation under ORS 60.973 shall not, of itself, affect the validity or effectiveness of any act or transaction or the issuance of any shares properly ratified under common law or otherwise, nor shall it create a presumption that any such act or transaction is or was a defective corporate act or that such shares are void or voidable.

ORS § 60.973. Proceedings regarding validity of defective corporate acts and putative shares [New ORS statute section added]

(1) Subject to subsection (6) of this section, upon application by a corporation, any successor entity to the corporation, any member of the corporation's board of directors, any record or beneficial holder of valid shares or putative shares of the corporation, any record or beneficial holder of valid or putative shares of the corporation as of the time of a defective corporate act ratified pursuant to ORS 60.972 or any other person claiming to be substantially and adversely affected by a ratification pursuant to ORS 60.972, the circuit court of the county where the corporation's principal office is located, or, if the principal office is not in this state, where the registered office of the corporation is or was last located, may:

- (a) Determine the validity and effectiveness of any defective corporate act ratified pursuant to ORS 60.972;
- (b) Determine the validity and effectiveness of the ratification of any defective corporate act pursuant to ORS 60.972;
- (c) Determine the validity and effectiveness of any defective corporate act not ratified or not ratified effectively pursuant to ORS 60.972;
- (d) Determine the validity and effectiveness of any corporate act or transaction and any shares, rights or options to acquire shares; and
- (e) Modify or waive any of the procedures set forth in ORS 60.972 to ratify a defective corporate act.

(2) In connection with an action under this section, the circuit court may:

- (a) Declare that a ratification in accordance with and pursuant to ORS 60.972 is not effective or shall be effective only at a time or upon conditions established by the circuit court;
- (b) Validate and declare effective any defective corporate act or putative shares and impose conditions upon such validation by the circuit court;
- (c) Require measures to remedy or avoid harm to any person substantially and adversely affected by a ratification pursuant to ORS 60.972 or from any order of the circuit court pursuant to this section, excluding any harm that would have resulted if the defective corporate act had been valid when approved or effectuated;
- (d) Order the Secretary of State to accept an instrument for filing with an effective time specified by the circuit court, which effective time may be prior or subsequent to the time of such order, provided that the filing date of such instrument shall be determined in accordance with ORS 60.017(2);
- (e) Approve a stock ledger for the corporation that includes any shares ratified or validated in accordance with this section or with ORS 60.972;
- (f) Declare that putative shares are valid shares or require a corporation to issue and deliver valid shares in place of any putative shares;
- (g) Order that a meeting of holders of valid shares or putative shares be held and exercise the powers provided to the circuit court under ORS 60.207 with respect to such a meeting;

(h) Declare that a defective corporate act validated by the circuit court shall be effective as of the time of the defective corporate act or at such other time as the circuit court shall determine;

(i) Declare that putative shares validated by the circuit court shall be deemed to be identical valid shares or fraction of valid shares as of the time originally issued or purportedly issued or at such other time as the Court determines; and

(j) Make any other orders regarding such matters as it deems proper under the circumstances.

(3) Upon an application under subsection (1) of this section by an applicant other than the corporation, service of process upon the registered agent of the corporation shall be deemed to be service upon the corporation, and no other party need be joined for the circuit court to adjudicate the matter, unless otherwise required by the circuit court. Upon application under subsection (1) of this section by the corporation, the circuit court may, in its discretion, require that notice of the action be provided to other persons, and the circuit court may permit other persons to intervene in the action.

(4) In connection with the resolution of matters pursuant to subsections (1) and (2) of this section, the circuit court may consider the following:

(a) Whether the defective corporate act was originally approved or effectuated with the belief that the approval or effectuation complied with the provisions of this chapter and the articles of incorporation or bylaws of the corporation;

(b) Whether the corporation and board of directors has treated the defective corporate act as a valid act or transaction and whether any person has acted in reliance on the public record that such defective corporate act was valid;

(c) Whether any person will be or was harmed by the ratification or validation of the defective corporate act, excluding any harm that would have resulted if the defective corporate act had been valid when initially approved or effectuated;

(d) Whether any person will be harmed by the failure to ratify or validate the defective corporate act; and

(e) Any other factors or considerations the circuit court deems just and equitable.

(5) The circuit court of the county where a corporation's principal office is located when the application under this section is initially filed, or, if the principal office is not in this state, where the registered office of the corporation is or was last located, is vested with exclusive jurisdiction to hear and determine all actions brought under this section.

(6) Notwithstanding any other provision of this section, no action may be brought more than 120 days after the validation effective time asserting that (a) a defective corporate act or putative shares ratified in accordance with ORS 60.972 is void or voidable due to a failure of authorization identified in the adopted resolutions or (b) the circuit court should declare in its discretion that a ratification in accordance with ORS 60.972 is not effective or is effective only on certain conditions, except that this subsection shall not apply to an action asserting that a ratification was not accomplished in accordance with ORS 60.972 or to any person to whom notice of the ratification was required to have been given pursuant to ORS 60.972(5) or (8), but to whom such notice was not given.

Substantially similar changes are proposed to the Oregon Professional Corporation Act.

DRAFT