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Correcting Incomplete Corporate Records

By D. Richard McDonald and Jeanne M. Moloney

Introduction
Attorneys conducting due diligence in preparation for corporate transactions or securities offerings often discover that their clients' corporate records are incomplete. Potential issues in such situations can range from errant formation documents to incomplete minute books and board resolutions, to improper issuance of securities, and to a whole host of other problems that can derail a transaction or offering. Although there are perhaps an infinite number of potential problems that can arise when a corporation has not properly maintained its corporate records over time, this article will focus specifically on (1) correction of incomplete formation documents and minute books and (2) approval of unauthorized or improperly authorized acts of officers and directors. No two corporate records situations will be exactly alike, and any corrective action will require creativity and individual consideration.

Compiling Materials
The first step in cleaning up an incomplete corporate record book is to compile and organize all existing documents. It is often best to start with a search of public records, as this search will yield "official" executed copies of any filed documents. When performing these searches, omit any firm designations (Corp., Inc., etc.) from the company name. Search for the name of the corporation, any prior names it may have used, and any subsidiaries it holds. A public records search in Michigan should include the following resources:

- The Department of Energy, Labor and Economic Growth (DELEG) Business Services Web Site: The DELEG's Web site (http://www.michigan.gov/dleg/) provides access to articles of incorporation, any filed amendments to the articles, and annual reports for Michigan companies. Searchers should contact the Business Services Section to obtain a certificate of good standing.
- The Secretary of State Web Site: The Michigan Secretary of State maintains UCC security interest filings. A UCC search for a Michigan corporation at https://apps.michigan.gov/UCC/Home.aspx may turn up liens that no longer exist (and should therefore be terminated), or liens for which the corporation's minutes contain no authority.

- Court Records: Court documents may provide some evidence of major contracts or major corporate acts. Searching for a company's name in all Michigan court records from the time of the corporation's inception could provide too much information to be useful. This type of search is best used to fill in specific time periods for which records are particularly lacking.

- Other Resources: Lexis and Westlaw provide access to records, but are largely focused only on public companies. Westlaw Business provides some information on private companies, and any major contracts between public and private companies may be filed as exhibits to the public company's SEC disclosure materials. Searching these and related Internet sites may provide information about material agreements or other actions that should have been approved.

Once public records have been collected, compare them to any documents the corporation currently has in its possession. All documents should be sorted, dated, and organized. Prepare a checklist of any missing documents and include amendments, restatements, and exhibits to other documents, minutes for meetings purportedly held but not recorded, contracts, leases, and securities documents. The checklist should also include proper authorization documents for the transaction being contemplated, if necessary. If the corporation stores its documents electronically, ensure that the electronic files reflect the correct, executed versions of those documents.
There are limited circumstances under which Michigan courts have found corporate actions to be void, however, as Michigan law now follows the national trend toward limiting a corporation’s liability for acts outside its express power.

Ratifying Unauthorized Corporate Acts

Any actions by a corporation’s directors or officers that require approval under its articles or bylaws or by law, but for which there is no evidence of the necessary approval, should be ratified to transform them into proper corporate acts. By definition, unauthorized (or improperly authorized) corporate actions may be either “void” or “voidable.” If such actions are void, no subsequent undertaking by the corporation or its agents can save them. There are limited circumstances under which Michigan courts have found corporate actions to be void, however, as Michigan law now follows the national trend toward limiting a corporation’s liability for acts outside its express power. Under § 271 of the MBCA, “[a]n act of a corporation..., otherwise lawful, is not invalid because the corporation was without capacity or power to do the act.” As a result, Michigan courts generally only find actions “void” that are forbidden by statute or extremely culpable. For example, “a promise or agreement requiring the performance of a criminal or tortious act” is void under Michigan caselaw. Similarly, if a corporation has obtained an agreement through “fraud in the execution” or “fraud in the factum” (whereby it was at fault in causing the other party to the agreement to be excusably ignorant of the nature of what he was agreeing to) such fraud will render an agreement void, rather than voidable.

If corporate actions are voidable (rather than void), they may be saved by ratification, which operates as retroactive approval. In general, “[v]oidable acts...are corporate acts that are within the ambit of the corporation’s power or authority but were taken absent compliance with corporate formalities.” Because most actions are merely “voidable” under Michigan law, the board (or shareholders) can legitimize most actions through ratification. If board approval is needed, the approval required for ratification comes from the directors in office at the time of ratification. If shareholder approval is needed for the particular type of action, it should likewise be obtained from shareholders with ownership interests at the time of ratification. The board or shareholders may ratify either at a meeting or by written consent. To ratify via meeting,

[ cita] all special meetings of directors and shareholders where you present a report summarizing the important transactions that lack documentation in the minute book. All relevant facts concerning these transactions should be disclosed, especially when the transactions involve the corporation and a director, an officer, or a shareholder. Then ask the shareholders and directors to adopt resolutions ratifying the actions of the directors and officers described in the report.

Otherwise, “[p]repare written consents to action that describe and ratify the important transactions. Directors or shareholders will then sign the written consents to ratify the actions.

In Michigan, consent to board action without a meeting is governed by section 525 of the MBCA, which states:

Unless prohibited by the articles of incorporation or bylaws, action required or permitted to be taken under authorization voted at a meeting of the board or a committee of the board, may be taken without a meeting if, before or after the action, all members of the board then in office or of the committee consent to the action in writing or by electronic transmission.”
NOTES


4. For a thorough discussion of the problems that can result from incomplete corporate records, see P. Hodge, O’Neal & Robert B. Thompson, O’Neal and Thompson’s Close Corporations and LLC’s § 8.2(3) (ed. 2008). A corporation’s failure to adopt bylaws, keep minutes of shareholders and directors’ meetings, maintain adequate financial and business records clearly will hinder efforts to obtain future financing. If it has no records, or it has only incomplete or inadequate records, it is certain to have difficulty borrowing from banks, placing securities privately with institutional investors, or making a public offering of securities.

5. Because the more flexible provisions of the Michigan Limited Liability Company Act do not require the same degree of record keeping and formalities as the Michigan Business Corporations Act, this article will focus solely on the issues facing corporations, and not LLCs.

6. For comprehensive ‘checklist’ of relevant documents, see Donald W. Glazer et al., Glazer and Fairchild on Legal Opinions ch. 4 (5d ed. 2008); Dorsey & Renfro, supra note 5.

7. Over the years, directors may have errantly filed documents using differing punctuation or designations, and no document filed by the corporation at issue should be overlooked. Dorsey & Renfro, supra note 5, at 806.

8. MCL 450.9513 provides the circumstances under which a secured party of record is obligated to file a termination statement for a previously filed financing statement. If any of these conditions apply to a financing statement for which the corporation is a debtor, and that financing statement has not been properly terminated and has not lapsed, contact the secured party with an authenticated demand for termination. Id. at § 2(6), (3). If the secured party does not cause the secured party of record to file a termination statement or send a termination statement to the debtor within 20 days after receipt of such demand, the debtor may file a termination statement on its own behalf. MCL 449.9509(4)(b). A termination statement filed by a debtor must indicate on its face that the debtor authorized it to be filed. Id. If a debtor files its own termination statement after the secured party’s failure to handle the matter, the debtor may also be eligible for statutory liquidated damages from the secured party, under MCL 450.9525.

9. Janover, supra note 3; Dorsey & Renfro, supra note 5.

10. For example, if a contract was executed and signed, ensure that the signed copy has been scanned, including any handwriting changes marked on the final executed copy.

11. The relevant federal law is Electronic Signatures in Global and National Commerce Act ("E-Sign"). 15 USC 7000 et. seq. E-Sign became law in the United States October 1, 2000. E-Sign effectively imposes the UETA rules on the states in interstate and international commerce and it specifically preempts different state law in that arena to the extent that state law materially departs from UETA. E-Sign does not replace state law in strictly intrastate transactions, but the history of the enforcement of the Commerce Clause of the United States Constitution suggests that the courts will apply E-Sign’s (and therefore UETA’s) principles so long as the transaction has any effect on interstate or international commerce.

12. MCL 450.1485 (2009). Keeping records in other than written form is authorized by the MBCA and thus need not be specifically mentioned in the corporation’s bylaws. Id. The books, records, or minutes may be in written form or in any other form capable of being converted into written form within a reasonable time. However, records that are kept in electronic form must be reduced to writing (e.g. by using a computer printer) upon request by any person entitled to inspect such records. Id.


14. UETA, § 3.1(1).

15. Id. at § 2.7.

16. Id. at § 2.8.

17. Id. at § 2.9.

18. Id. at § 2.10.

19. Id. at § 2.11.

20. Other key sections of UETA include:

Section 18, which leaves in the hands of state officials the decision of whether, and to what extent, to accept electronic records and signatures for required filings. Because of Section 18, any document that is required to be filed to establish, perfect, or maintain any security interest or other status (such as manually signed mortgages) should be maintained in manually-signed paper form, at least until the recording or other filing process is complete and acknowledged by the appropriate governmental authority.

Section 5, which makes it clear that no private contracting party is required to generate, accept, or deal in electronic records or signatures. This essentially means that any third party involved with a transaction could refuse to accept records other than manually-signed hardcopies. Thus, the corporation should retain the original hardcopies of any document where the other party specifically required a manually-signed hardcopy in order to exercise its rights.

21. For a thorough discussion of this issue, see Glazer et al., supra note 6, chs. 6 & 7.

22. MCL 450.1611(2) (amendment without shareholder approval), 1611(3) (amendment requiring shareholder approval), and 1614(3) (requirement with or without shareholder approval) (2009).

23. MCL 450.1431(6) (2009) ("A document, such as a certificate of amendment, is effective at the time it is endorsed [by the administrator of the Business Corporations Act] unless a subsequent effective time, not later than 90 days after the date of delivery, is set forth in the document.").


25. See MCL 450.1611(2) (amendment of articles of incorporation without shareholder approval), 1611(3) (amendment of articles of incorporation requiring shareholder approval), and 1231 (amendment of bylaws).


27. 5A William Meade Fletcher et al., Fletcher Cyclopaedia of the Law of Corporations § 2190 (Westlaw 2009) ("[S]tates may be prepared and entered at any time, even after the meeting.").

28. Id. ("[T]he mere fact that the minutes were made up informally, where they are admittedly correct, does not destroy their force.").

29. Id. at 1155-56.

30. Id. at 1154.
31. Id. at 1. 57. For example, in an unpublished opinion, the Michigan Court of Appeals found fault with the board of directors of a corporation that adopted a resolution to amend its bylaws "retroactively." The board acted to remove a provision from its bylaws restricting the sale of stock, but it found that the amendment should have been effective as of a prior date. Since no action was taken on that previous date to amend the bylaws, the court held that the amendment could not operate retroactively. Gommer v. John Carrier, No. 255713, 2005 Mich. App. LEXIS 1849 (App. 28, 2005).

32. Id. at 1159.

33. This prohibition is related to the distinction between "memorializing" and "fabricating" a transaction. For information on this related issue of backdating generally, see Jeffrey L. Kroll & Stuart D. Backinger, 63 Bus. Law. 1153 (2008).


35. The distinction between the terms "void" and "voidable" is explained in Restatement (Second) of Contracts § 7 and the comments thereafter.

36. See, e.g., Biger & Tillman, supra note 2, at 1110 ("A finding that stock is void means that it cannot be cured, whether by ratification or otherwise."); MCL 450.1271 (2009). There are enforcement exceptions to this rule for (a) a shareholder action against the corporation for injunctive relief; (b) an action on behalf of the corporation for loss or damage against a director or officer; and (c) an action by the attorney general to enjoin unauthorized transactions.

37. Id. See, e.g., Sanches v. Eagle Agility, Inc., 471 Mich. 851, 852, 684 NW2d 342 (2004) ("All contracts which are voided on an act prohibited by a statute under a penalty are void, although not expressly declared to be so."); quoting Cassius v. Pitzer, 168 Mich. 386, 390, 134 NW 482 (1912). See also Kakela v. Perry, 361 Mich. 311, 324, 105 NW2d 176 (1960) (noting that a contract that is violative of a statute is void even if the applicable statute does not so provide); Stokes v. Miller Roofing Co., 486 Mich. 660, 672, 649 NW2d 571 (2002) (quoting Bil-More Homes, Inc. v. French, 373 Mich. 695, 699, 370 NW2d 907 (1985)) (contracts by a residential builder not duly licensed as required by statute are "not only voidable but void").

Delaware law is in accord. In Solomon v. Armstrong, 38 Del. 117, 186 Atl. 227 (1936), the court held that void acts, which are either contrary to public policy or beyond the authority of the corporation, cannot be cured by ratification. Thus, for example, fraud cannot be ratified. J. R. Franklin Balcer & Jesse A. Finkelstein, The Delaware Law of Corporate & Business Organizations § 7.28 (3d ed. 1998) (citing 742 A2d 1098 (Del Ch 1999), aff’d 746 A2d 277 (Del Ch 2000); disposition reported at 74 746 A2d 277). The court noted that, as an example, "acts performed in the corporation’s interest but beyond management’s explicit authority" would be merely voidable. Id.

39. Sanders, 471 Mich. 851, 852, 684 NW2d (citing 5 Williston on Contracts § 121 (4th ed) such agreements are illegal, unenforceable, and void").

40. This type of fraud is present when a party "execute the agreement with neither knowledge nor reasonable opportunity to obtain knowledge of its character or its essential terms, as well as excusable ignorance of the contents of the writing signed." See North American Specialty Ins Co v Goellner Enter. LLC, No. 1-05-CV-856, slip op. at 8 (WD Mich. Mar. 25, 2008) (citing Bricklayer’s Pension Trust Fund-Metro Area v. Citicorp, 675 F.Supp. 1083, 1086-87 (ED Mich. 1988)). On the other hand, any agreement that is obtained through "fraud in the inducement," whereby a person knows the terms of a written instrument, but was induced to enter into the contract because of false representations made to him, is not void, but merely voidable. Id.

41. Bigger & Tillman, supra note 2, at 1115.

42. See Dory & Renfro, supra note 3, at 837 (Applying Nebraska law to explain that “[a]ny actions which should be taken or ratifications which should be made to correct minutes can usually be taken in a single comprehensive consent of the present directors and shareholders, if consents are permitted, ... at a meeting of the present directors and shareholders,” emphasis in original)). See also Janover, supra note 3, at 19 ("The acceptable procedure for retroactive approval of prior acts and deeds is to obtain unanimous written consents from the presently-constituted board of directors, and from all present shareholders if shareholder consent is required, either by joint or separate unanimous written consents.").

43. Material facts of any proposed transaction involving a conflict of interest between the corporation and a director or officer must be disclosed to the independent director, directors, shareholder, or shareholders for a valid approval, authorization, or ratification to occur. MCL 450.1545a (2009).


45. Id. See also MCL 450.1525 (board resolution by consent), §1407 (shareholder resolution by consent) (2009).

46. MCL 450.1525 (2009) and comments thereto.

47. Id. at comments. This phrase is also used in other Michigan statutes. See, e.g., the Michigan Business Corporation Act, MCL 450.151 et seq. (Filling Vacancy in Board); the Michigan Nonprofit Corporation Act, MCL 450.251 (Removal of Director or Entire Board), 2533 (Quorum; Vote Constituting Action of Board or Committee; Amendment of Bylaws), §2611 (Amendment of Articles by Incorporators; Manner of Adoption; Notice of Meeting; Vote on Proposed Amendment; Requirements; Adoption; Number of Amendments Acted Upon; at 1 Meeting; Certificate of Amendment), §2703 (Plan of Merger or Consolidation; Approval or Authorization; Voting; Notice of Meeting), §2753 (Disposition of Property and Assets of Corporation; Approval or Authorization; Fixing Terms of Conditions and Consideration; Voting; Abandonment), §2804 (Dissolution of Corporation by Action of Shareholders, Members, or Board Resolution; Approval or Authorization; Notice; Voting; Certificate), and §2815 (Renewal of Corporate Existence).


49. See, e.g., Bilt-o-Thompson Automatic Arms Corp., 64 A2d 581, 604 (Del Ch 1948).

50. Id. at § 762. See also Ammon et al., supra note 44, at §§ 6.40, 6.42.

51. Id. at § 752. See also Ammon et al., supra note 44, at § 6.42. For a comprehensive checklist of considerations and steps necessary for shareholders and directors to take action, see Lewis W. Kasich, Michigan Clearly Held Corporations $23.36 (1986), superseded by Ammon et al., supra note 44, at § 6.39.

52. See Ammon et al., supra note 44, at § 6.39.

53. “[T]his practice may not always suffice unless there is an adequate disclosure of relevant information.” Id. at § 6.42.

54. Id. at § 6.42. See, e.g., Lisa Frank, Inc v Greens, No. 2 CA-CV 2008-0120, 2009 WL 1891915 at *4 (Ariz. Ct App June 30, 2009) ("Although ... a corporation may equitably and adopt the unauthorized act of a corporate officer, ... for a ratification to be effective, the corporation must be aware of the act at ratification.").

55. Fletcher et al., supra note 48, at § 756. See also Ammon et al., supra note 44, at §§ 6.40 ("The effectiveness of [the ratification] procedure depends on the adequacy of the factual disclosure."). Kasich, supra note 51 at § 31.33 ("The practice of using blanket resolutions..."