/* Part 3 of 8 of the Model Act continues. */

would have been required to be sent to nonvoting shareholders in notice of meeting at which the proposed action would have been submitted to the shareholders for action.

Official Comment

2. Revocation of Consent Action by unanimous written consent is effective only when the last shareholder has signed the appropriate written consent and all consents have been delivered to the secretary of the corporation. Before that time, any shareholder may withdraw his consent simply by advising the secretary of that fact. Cf. Calumet Industries, Inc. v. MacClure, 464 F.Supp. 19 (N.D.Ill.1978). The withdrawal of a single consent, of course, destroys the unanimous written consent required by this section. If a shareholder seeks to withdraw his consent after all shareholders have signed written consents and filed them with the secretary of the corporation, the corporation may treat the attempted withdrawal as too late or give it effect, thereby requiring the matter to be presented at a shareholders' meeting.

7.05 Notice of Meeting

(a) A corporation shall notify shareholders of the date, time, and place of each annual and special shareholders' meeting no fewer than 10 nor more than 60 days before the meeting date. Unless this Act or the articles of incorporation require otherwise, the corporation is required to give notice only to shareholders entitled to vote at the meeting.

(b) Unless this Act or the articles of incorporation require otherwise, notice of an annual meeting need not include a description of the purpose or purposes for which the meeting is called.

(c) Notice of a special meeting must include a description of the purpose or purposes for which the meeting is called.

(d) If not otherwise fixed under section 7.03 or 7.07, the record date for determining shareholders entitled to notice of and to vote at an annual or special shareholders' meeting is the day before the first notice is delivered to shareholders.

(e) Unless the bylaws require otherwise, if an annual or special shareholders' meeting is adjourned to a different date, time, or place, notice need not be given of the new date, time, or place if the new date, time, or place is announced at the meeting before adjournment. If a new record date for the adjourned meeting is or must be fixed under section 7.07, however, notice of the adjourned meeting must be given under this section to persons who are shareholders as of the new record date.

7.06 Waiver of Notice

(a) A shareholder may waive any notice required by this Act, the articles of incorporation, or bylaws before or after the date and time stated in the notice. The waiver must be in writing, be signed by the shareholder entitled to the notice, and be delivered to the corporation for inclusion in the minutes or filing with the corporate records.

(b) A shareholder's attendance at a meeting:

(1) waives objection to lack of notice or defective notice of the meeting, unless the shareholder at the beginning of the meeting objects to holding the meeting or transacting business at the meeting;

(2) waives objection to consideration of a particular matter at the meeting that is not within the purpose or purposes described in the meeting notice, unless the shareholder objects to considering the matter when it is presented.

7.07 Record Date

(a) The bylaws may fix or provide the manner of fixing the record date for one or more voting groups in order to determine the shareholders entitled to notice of a shareholders' meeting, to demand a special meeting, to vote, or to take any other action. If the bylaws do not fix or provide for fixing a record date, the board of directors of the corporation may fix a future date as the record date.

(b) A record date fixed under this section may not be more than 70 days before the meeting or action requiring a determination of shareholders.

(c) A determination of shareholders entitled to notice of or to vote at a shareholders' meeting is effective for any adjournment of the meeting unless the board of directors fixes a new record date, which it must do if the meeting is adjourned to a date more than 120 days after the date fixed for the original meeting.

(d) If a court orders a meeting adjourned to a date more than 120 days after the date fixed for the original meeting, it may provide that the original record date continues in effect or it may fix a new record date.

Subchapter B

Voting

7.20 Shareholders' List for Meeting

(a) After fixing a record date for a meeting, a corporation shall prepare an alphabetical list of the names of all its shareholders who are entitled to notice of a shareholders' meeting. The list

must be arranged by voting group (and within each voting group by class or series of shares) and show the address of and number of shares held by each shareholder.

(b) The shareholders' list must be available for inspection by any shareholder, beginning two business days after notice of the meeting is given for which the list was prepared and continuing through the meeting, at the corporation's principal office or at a place identified in the meeting notice in the city where the meeting will be held. A shareholder, his agent, or attorney is entitled on written demand to inspect and, subject to the requirements of section 16.02(c), to copy the list, during regular business hours and at his expense, during the period it is available for inspection.

(c) The corporation shall make the shareholders' list available at the meeting, and any shareholder, his agent, or attorney is entitled to inspect the list at any time during the meeting or any adjournment.

(d) If the corporation refuses to allow a shareholder, his agent, or attorney to inspect the shareholders' list before or at the meeting (or copy the list as permitted by subsection (b)), the [name or describe court of the county where a corporation's principal office (or, if none in this state, its registered office) is located, on application of the shareholder, may summarily order the inspection or copying at the corporation's expense and may postpone the meeting for which the list was prepared until the inspection or copying is complete.

(e) Refusal or failure to prepare or make available the shareholders' list does not affect the validity of action taken at the meeting.

Official Comment

5. The Right to Obtain a Copy of the List

Section 7.20(b) permits shareholders to "inspect" the list without limitation, but permits the shareholder to "copy" the list only if the shareholder complies with the requirement of section 16.02(c), that the demand be "made in good faith and for a proper purpose." The right to copy the list includes, if reasonable, the right to receive a copy of the list upon payment of a reasonable charge. See sections 16.03(b) and (c). The distinction between inspection" and "copying" set forth in section 7.20(b) reflects an accommodation between competing considerations of permitting shareholders access to the list before a meeting and possible misuse of the list.

6. Relationship to Right to Inspect Corporate Records Generally
Section 7.20 creates a right of shareholders to inspect a list of shareholders in advance of and at a meeting that is independent of the rights of shareholders to inspect corporate records under chapter 16A. A shareholder may obtain the right to inspect the

list of shareholders as provided in chapter 16A without regard to the provisions relating to the pendency of a meeting in section 7.20, and similarly the limitations of chapter 16A are not applicable to the right of inspection created by section 7.20 except to the extent the shareholder seeks to copy the list in advance of the meeting. The right to inspect under chapter 16A is also broader in the sense that in some circumstances the shareholder may be entitled to receive copies of the documents he may inspect. See section 16.03.

7.21 Voting Entitlement of Shares

(a) Except as provided in subsections (b)and (c) or unless the articles of incorporation provide otherwise, each outstanding share, regardless of class, is entitled to one vote on each matter voted on at a shareholders' meeting. Only shares are entitled to vote.

(b) Absent special circumstances, the shares of a corporation are not entitled to vote if they are owned, directly or indirectly, by a second corporation, domestic or foreign, and the first corporation owns, directly or indirectly, a majority of the shares entitled to vote for directors of the second corporation.

/* The code starts with a new concept, that prevents corporations from interlocking. */

(c) Subsection (b) does not limit the power of a corporation to vote any shares, including its own shares, held by it in a fiduciary capacity.

(d) Redeemable shares are not entitled to vote after notice of redemption is mailed to the holders and a sum sufficient to redeem the shares has been deposited with a bank, trust company, or other financial institution under an irrevocable obligation to pay the holders the redemption price on surrender of the shares.

Official Comment

Section 7.21 deals with the entitlement of shareholders to vote, while section 7.22 deals with voting by proxy and section 7.24 establishes rules for the corporation's acceptance or rejection of proxy votes.

1. Voting Power of Shares

Section 7.21(a provides that each outstanding share, regardless of class, is entitled to one vote per share unless otherwise provided in the articles of incorporation. See section 6.01 and its Official Comment. The articles of incorporation may provide for multiple or fractional votes per share and may provide that some classes of shares are nonvoting on some or all matters, or that some classes have multiple or fractional votes per share while other classes have a single vote per share or different multiple or fractional votes per share, or that some classes

constitute one or more separate voting groups and are entitled to vote separately on the matter.

The articles of incorporation may also authorize the board of directors to create classes or series of shares with preferential rights, which may be voting or nonvoting in whole or in part. See section 6.02 and its Official Comment.

Fractional or multiple votes per share, or nonvoting shares, are often used in the planning of business ventures, particularly closely held ventures, when the contributions of participants vary in kind or quality. It is possible through these devices, for example, to give persons with relatively small financial contributions a relatively large voting power within the corporation.

The power to vary or condition voting power is also often used to give increased protection to financial interests in the corporation. It is customary, for example, to make classes of shares with preferential rights nonvoting, but the power to vote may be granted to those classes if distributions are omitted for a specified period. This conditional right to vote may permit the class of shares with preferential rights to vote separately as a voting group to elect one or more directors or to vote with the shares having general voting rights in the election of the directors.

In order to reflect the possibility that shares may have multiple or fractional votes per share, all provisions relating to quorums, voting, and similar matters in the Model Act are phrased in terms of "votes" rather than "shares."

2. Voting Power of Nonshareholders

Under the last sentence of section 7.21(a), the power to vote cannot be granted generally to nonshareholders. The statutes of some states permit bondholders to be given the power to vote under certain specified circumstances; this option is not available under the Model Act. But creditors may in effect be given the power to vote, e.g., by creating a special class of redeemable voting shares for them, by creating a voting trust at the time the credit is extended with power in the creditors to name the voting trustees, by registering the shares in the name of the creditors as pledgees with power to vote, or by granting the creditors a revocable or irrevocable proxy to vote some or all of the outstanding shares. See the Official Comment to section 7.22.

3. Circular Holdings

Section 7.21(b) prohibits the voting of shares held by a domestic or foreign corporation that is itself a majority-owned subsidiary of the corporation issuing the shares, The purpose of this prohibition is to prevent management from using a corporate investment to perpetuate itself in power. Similar public policy

considerations may be present in situations where the issuing corporation owns a large but not a majority interest in the corporation voting the shares. The inclusion of section 7.21(b) is not intended to affect the possible application of common law principles that may invalidate circular holding situations not within its literal prohibition. As to the possible existence of these common law principles, see, e.g., Cleveland Trust Co. v. Eaton, 11 Ohio Misc. 151, 229 N.E.2d 850 (1967), rev'd on the basis of statutory amendment, 21 Ohio St.2d 129, 256 N.E.2d 198 (1970). The phrase "absent special circumstances" is included to enable a court to permit the voting of shares where it deems that the purpose of the section is not violated.

4. Shares Held in a Fiduciary Capacity

Section 7.21(c) makes the prohibition against voting of circularly-owned shares of section 7.21(b) inapplicable to shares held in a fiduciary capacity. Compare Del.Gen.Corp.Law 160(c). The Ohio statute involved in the Eaton case authorized a bank to vote its own shares that were held by it in a fiduciary capacity. A state may grant or prohibit such voting by another statute; section 7.21(c) provides only that such voting is not prohibited by the Model Act. .

7.22 Proxies

(a) A shareholder may vote his shares in person or by proxy.

(b) A shareholder may appoint a proxy to vote or otherwise act for him by signing an appointment form, either personally or by his attorney-in-fact.

(c) An appointment of a proxy is effective when received by the secretary or other officer or agent authorized to tabulate votes. An appointment is valid for 11 months unless a longer period is expressly provided in the appointment form.

(d) An appointment of a proxy is revocable by the shareholder unless the appointment form conspicuously states that it is irrevocable and the appointment is coupled with an interest. Appointments coupled with an interest include the appointment of:

(1) a pledgee;

(2) a person who purchased or agreed to purchase the shares;

(3) a creditor of the corporation who extended it credit under terms requiring the appointment;

(4) an employee of the corporation whose employment contract requires the appointment; or

(5) a party to a voting agreement created under section 7.31.

(e) The death or incapacity of the shareholder appointing a proxy does not affect the right of the corporation to accept the proxy's authority unless notice of the death or incapacity is received by the secretary or other officer or agent authorized to tabulate votes before the proxy exercises his authority under the appointment.

(f) An appointment made irrevocable under subsection (d) is revoked when the interest with which it is coupled is extinguished.

(g) A transferee for value of shares subject to an irrevocable appointment may revoke the appointment if he did not know of its existence when he acquired the shares and the existence of the irrevocable appointment was not noted conspicuously on the certificate representing the shares or on the information statement for shares without certificates.

(h) Subject to section 7.24 and to any express limitation on the proxy's authority appearing on the face of the appointment form, a corporation is entitled to accept the proxy's vote or other action as that of the shareholder making the appointment.

Official Comment.

I. Nomenclature

The word "proxy" is often used ambiguously, sometimes referring to the grant of authority to vote, sometimes to the document granting the authority, and sometimes to the person to whom the authority is granted. In the revised Model Act the word "proxy" is used only in the last sense; the term "appointment form" is used to describe the document appointing the proxy; and the word "appointment" is used to describe the grant of authority to vote.

7.23 Shares Held by Nominees

(a) A corporation may establish a procedure by which the beneficial owner of shares that are registered in the name of a nominee is recognized by the corporation as the shareholder. The extent of this recognition may be determined in the procedure.

(b) The procedure may set forth:

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

(2) the rights or privileges that the corporation recognizes in a beneficial owner;

(3) the manner in which the procedure is selected by the nominee;

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

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

(6) other aspects of the rights and duties created.

7.24 Corporation's Acceptance of Votes

(a) If the name signed on a vote, consent, waiver, or proxy appointment corresponds to the name of a shareholder, the corporation if acting in good faith is entitled to accept the vote, consent, waiver, or proxy appointment and give it effect as the act of the shareholder.

(b) If the name signed on a vote, consent, waiver, or proxy appointment does not correspond to the name of its shareholder, the corporation if acting in good faith is nevertheless entitled to accept the vote, consent, waiver, or proxy appointment and give it effect as the act of the shareholder if:

(1) the shareholder is an entity and the name signed purports to be that of an officer or agent of the entity;

(2) the name signed purports to be that of an administrator, executor, guardian, or conservator representing the shareholder and, if the corporation requests, evidence of fiduciary status acceptable to the corporation has been presented with respect to the vote, consent, waiver, or proxy appointment;

(3) the name signed purports to be that of a receiver or trustee in bankruptcy of the shareholder and, if the corporation requests, evidence of this status acceptable to the corporation has been presented with respect to the vote, consent, waiver, or proxy appointment;

(4) the name signed purports to be that of a pledgee, beneficial owner, or attorney-in-fact of the shareholder and, if the corporation requests, evidence acceptable to the corporation of the signatory's authority to sign for the shareholder has been presented with respect to the vote, consent, waiver, or proxy appointment;

(5) two or more persons are the shareholder as cotenants or fiduciaries and the name signed purports to be the name of at least one of the coowners and the person signing appears to be acting on behalf of all the coowners.

(c) The corporation is entitled to reject a vote, consent, waiver, or proxy appointment if the secretary or other officer or agent authorized to tabulate votes, acting in good faith, has reasonable basis for doubt about the validity of the signature on it or about the signatory's authority to sign for the shareholder.

(d) The corporation and its officer or agent who accepts or rejects a vote, consent, waiver, or proxy appointment in good

faith and in accordance with the standards of this section are not liable in damages to the shareholder for the consequences of the acceptance or rejection.

(e) Corporate action based on the acceptance or rejection of a vote, consent, waiver, or proxy appointment under this section is valid unless a court of competent jurisdiction determines otherwise.

/* An interesting statement that appears to be unnecessary. Corporate actions are usually effective unless a court says otherwise. */

7.25 Quorum and Voting Requirements for Voting Groups

(a) Shares entitled to vote as a separate voting group may take action on a matter at a meeting only if a quorum of those shares exists with respect to that matter. Unless the articles of incorporation or this Act provide otherwise, a majority of the votes entitled to be cast on the matter by the voting group constitutes a quorum of that voting group for action on that matter.

(b) Once a share is represented for any purpose at a meeting, it is deemed present for quorum purposes for the remainder of the meeting and for any adjournment of that meeting unless a new record date is or must be set for that adjourned meeting.

(c) If a quorum exists, action on a matter (other than the election of directors) by a voting group is approved if the votes cast within the voting group favoring the action exceed the votes cast opposing the action, unless the articles of incorporation or this Act require a greater number of affirmative votes.

(d) An amendment of articles of incorporation adding, changing, or deleting a quorum or voting requirement for a voting group greater than specified in subsection (a) or (c) is governed by section 7.27.

(e) The election of directors is governed by section 7.28.

Official Comment

3. Quorum Requirements for Action by Voting Group

Section 7.25(b) retains the common law view that once a share is present at a meeting, it is deemed present for quorum purposes throughout the meeting. Thus, a voting group may continue to act despite the withdrawal of persons having the power to vote one or more shares in an effort "to break the quorum." In this respect, a meeting of shareholders is governed by a different rule than a meeting of directors, where a sufficient number of directors must be present to constitute a quorum at the time action is taken. See section 8.24 and its Official Comment.

Once a share is present at a meeting it is also deemed to be present at any adjourned meeting unless a new record date is or must be set for that adjourned meeting. See section 7.07. If a new record date is set, new notice must be given to holders of shares of a voting group and a quorum must be established from within the holders of shares of that voting group on the new record date.

The shares owned by a shareholder who comes to the meeting to object on grounds of lack of notice may be counted toward the presence of a quorum. Similarly, the holdings of a shareholder who attends a meeting solely for purposes of raising the objection that a quorum is not present is counted toward the presence of a quorum. Attendance at a meeting, however, does not constitute a waiver of other objections to the meeting such as the lack of notice. Such waivers are governed by section 7.06 (b).

As used in sections 7.25 and 7.26, "represented at the meeting" means the physical presence of the shareholder (whether in person or by his written authorization) in the meeting room after the meeting has been called to order or the presiding officer has commenced consideration of the business of the meeting, and before the final adjournment of the meeting.

4. Voting Requirements for Approval by Voting Group

Section 7.25(c) provides that an action (other than the election of directors, which is governed by section 7.28) is approved by a voting group at a meeting at which a quorum is present if the votes cast in favor of the action exceed the votes cast opposing the action. This section changes the traditional rule appearing in earlier versions of the Model Act and many state statutes that an action is approved at a meeting at which a quorum is present if it receives the affirmative vote `of a majority of the shares represented at that meeting." The traditional rule in effect treated abstentions as negative votes; the Revised Model Act treats them truly as abstentions.

5. Modification of Standard Requirements

The articles of incorporation may increase the quorum and voting requirements to any extent desired up to and including unanimity upon compliance with section 7.27 . . . The articles may also decrease the quorum requirement as desired. Earlier versions of the Model Act limited the power to reduce the quorum to a minimum of one-third; this restriction, was eliminated from the Revised Model Act because it was thought to be unreasonably confining in certain situations, such as where a class of shares with preferential rights is given a limited right to vote that may be exercisable only rarely.

7.26 Action by Single and Multiple Voting Groups

(a) If the articles of incorporation or this Act provide for voting by a single voting group on a matter, action on that matter is taken when voted upon by that voting group as provided in section 7.25.

(b) If the articles of incorporation or this Act provide for voting by two or more voting groups on a matter, action on that matter is taken only when voted upon by each of those voting groups counted separately as provided in section 7.25. Action may be taken by one voting group on a matter even though no action is taken by another voting group entitled to vote on the matter.

Official Comment

Section 7.26(a) provides that when a matter is to be voted upon by a single voting group, action is taken when the voting group votes upon the action as provided in section 7.25. In most instances the single voting group will consist of all the shares of the class or classes entitled to vote by the articles of incorporation; voting by two or more voting groups as contemplated by section 7.26(b) is the exceptional case.

Section 7.26(b) basically requires that if more than one voting group is entitled to vote on a matter, favorable action on a matter is taken only when it is voted upon favorably by each voting group, counted separately. Implicit in this section are the concepts that

(1) different quorum and voting requirements may be applicable to different matters considered at a single meeting and

(2) different quorum and voting requirements may be applicable to different voting groups voting on the same matter. See the Official Comment to section 7.25. Thus, each group entitled to vote must independently meet the quorum and voting requirements established by section 7.25.

2. Participation of Shares in Multiple Voting Groups

As described in section 7.26(b), if voting by multiple voting groups is required, the votes of members of each voting group must be separately tabulated. Normally, each class or series of shares will participate in only a single voting group. But since holders of shares entitled by the articles of incorporation to vote generally on a matter are always entitled to vote in the voting group consisting of the general voting shares, in some instances classes or series of shares may be entitled to be counted simultaneously in two voting groups. This will occur whenever a class or series of shares entitled to vote generally on a matter under the articles of incorporation is affected by the matter in a way that gives rise to the right to have its vote counted separately as an independent voting group under the Act. For example, assume that corporation Y has outstanding one class of general voting shares without preferential rights ("common shares"), 500 shares issued, and one class of shares with

preferential rights ("preferred shares"), 100 shares issued, that also have full voting rights under the articles of incorporation, i.e., the preferred may vote for election of directors and on all other matters on which common may vote. The preferred and the common therefore are part of the general voting group. The directors propose to amend the articles of incorporation to change the preferential dividend rights of the preferred from cumulative to noncumulative. All shares are present at the meeting and they divide as follows on the proposal to adopt the amendment:

Yes - Common 230

- Preferred 80

No - Common 270

- Preferred 20

Both the preferred and the common are entitled to vote on the amendment to the articles of incorporation since they are part of a general voting group pursuant to the articles. But the vote of the preferred is also entitled to be counted separately on the proposal by section 10.04(a)(4) of the Model Act. The result is that the proposal passes by a vote of 310 to 290 in the voting group consisting of the shares entitled to vote generally and 80 to 20 in the voting group consisting solely of the preferred shares:

(a) First voting group

Yes: Common 230

Preferred80

310

No: Common 270

Preferred 20

290

(b) Second voting group (preferred)

Yes: Preferred 80

No: Preferred 20

In this situation, in the absence of a special quorum requirement, a meeting could approve the proposal to amend the articles of incorporation if-and only if-a quorum of each voting group is present, i.e., at least 51 shares of preferred and 301 shares of common and preferred were represented at the meeting. .

7.27 Greater Quorum or Voting Requirements

(a) The articles of incorporation may provide for a greater quorum or voting requirement for shareholders (or voting groups of shareholders) than is provided for by this Act.

(b) An amendment to the articles of incorporation that adds, changes, or deletes a greater quorum or voting requirement must meet the same quorum requirement and be adopted by the same vote and voting groups required to take action under the quorum and voting requirements then in effect or proposed to be adopted, whichever is greater.

Official Comment

Section 7.27(a) permits the articles of incorporation to increase the quorum or voting requirements for approval of an action by shareholders up to any desired amount including unanimity. These provisions may relate to ordinary or routine actions by the general voting group . . . or to one or more other voting groups or to actions for which the Model Act provides a greater voting requirement-for example, changes of a fundamental nature in the corporation like certain amendments to articles of incorporation (section 10.03) . .

A provision that increases the requirement for approval of an ordinary matter or a fundamental change is usually referred to as a "supermajority" provision.

Section 7.27(b) requires any amendment of the articles of incorporation that adds, modifies, or repeals any supermajority provision to be approved by the greater of the proposed quorum and vote requirement or by the quorum and vote required by the articles before their amendment. Thus, a supermajority provision that requires an 80 percent affirmative vote of all eligible votes of a voting group present at the meeting may not be removed from the articles of incorporation or reduced in any way except by an 80 percent affirmative vote. If the 80 percent requirement is coupled with a quorum requirement for a voting group that shares representing two-thirds of the total votes must be present in person or by proxy, both the 80 percent voting requirement and the two-thirds quorum requirement are immune from reduction except at a meeting of the voting group at which the two-thirds quorum requirement is met and the reduction is approved by an 80 percent affirmative vote. If the proposal is to increase the 80 percent voting requirement to 90 percent, that proposal must be approved by a 90 percent affirmative vote at a meeting of the voting group at which the two thirds quorum requirement is met; if the proposal is to increase the two thirds quorum requirement to three-fourths without changing the 80 percent voting requirement, that proposal must be approved by an 80 percent affirmative vote at a meeting of the voting group at which a three-fourths quorum requirement is met.

7.28 Voting for Directors; Cumulative Voting

(a) Unless otherwise provided in the articles of incorporation, directors are elected by a plurality of the votes cast by the shares entitled to vote in the election at a meeting at which a quorum is present.

(b) Shareholders do not have a right to cumulate their votes for directors unless the articles of incorporation so provide.

(c) A statement included in the articles of incorporation that "[all] [a designated voting group of] shareholders are entitled to cumulate their votes for directors" (or words of similar import) means that the shareholders designated are entitled to multiply the number of votes they are entitled to cast by the number of directors for whom they are entitled to vote and cast the product for a single candidate or distribute the product among two or more candidates.

(d) Shares otherwise entitled to vote cumulatively may not be voted cumulatively at a particular meeting unless:

(1) the meeting notice or proxy statement accompanying the notice states conspicuously that cumulative voting is authorized; or

(2) a shareholder who has the right to cumulate his votes gives notice to the corporation not less than 48 hours before the time set for the meeting of his intent to cumulate his votes during the meeting, and if one shareholder gives this notice all other shareholders in the same voting group participating in the election are entitled to cumulate their votes without giving further notice.

Subchapter C

Voting Trusts and Agreements

7.30 Voting Trusts

(a) One or more shareholders may create a voting trust, conferring on a trustee the right to vote or otherwise act for them, by signing an agreement setting out the provisions of the trust (which may include anything consistent with its purpose) and transferring their shares to the trustee. When a voting trust agreement is signed, the trustee shall prepare a list of the names and addresses of all owners of beneficial interests in the trust, together with the number and class of shares each transferred to the trust, and deliver copies of the list and agreement to the corporation's principal office.

(b) A voting trust becomes effective on the date the first shares subject to the trust are registered in the trustee's name. A voting trust is valid for not more than 10 years after its effective date unless extended under subsection (c).

(c) All or some of the parties to a voting trust may extend it for additional terms of not more than 10 years each by signing an extension agreement and obtaining the voting trustee's written consent to the extension. An extension is valid for 10 years from the date the first shareholder signs the extension agreement. The voting trustee must deliver copies of the extension agreement and list of beneficial owners to the corporation's principal office. An extension agreement binds only those parties signing it.

7.31 Voting Agreements

(a) Two or more shareholders may provide for the manner in which they will vote their shares by signing an agreement for that purpose. A voting agreement created under this section is not subject to the provisions of section 7.30.

(b) A voting agreement created under this section is specifically enforceable.

Official Comment

Section 7.31(a) explicitly recognizes agreements among two or more shareholders as to the voting of shares and makes clear that these agreements are not subject to the rules relating to a voting trust. These agreements are often referred to as "pooling agreements." The only formal requirements are that they be in writing and signed by all the participating shareholders; in other respects their validity is to be judged as any other contract. They are not subject to the 1-year limitation applicable to voting trusts.

Section 7.31(b) provides that voting agreements may be specifically enforceable. A voting agreement may provide its own enforcement mechanism, as by the appointment of a proxy to vote all shares subject to the agreement; the appointment may be made irrevocable under section 7.22. If no enforcement mechanism is provided, a court may order specific enforcement of the agreement and order the votes cast as the agreement contemplates. This section recognizes that damages are not likely to be an appropriate remedy for breach of a voting agreement, and also avoids the result reached in Ringling Bros. Barnum & Bailey Combined Shows v. Ringling, 53 A.2d 441 (Del.1947), where the court held that the appropriate remedy to enforce a pooling agreement was to refuse to permit any voting of the breaching party's shares.

[Old] Subchapter D

Derivative Proceedings

7.40 Procedure in Derivative Proceedings

(a) A person may not commence a proceeding in the right of a domestic or foreign corporation unless he was a shareholder of

the corporation when the transaction complained of occurred or unless he became a shareholder through transfer by operation of law from one who was a shareholder at that time.

(b) A complaint in a proceeding brought in the right of a corporation must be verified and allege with particularity the demand made, if any, to obtain action by the board of directors and either that the demand was refused or ignored or why he did not make the demand. Whether or not a demand for action was made, if the corporation commences an investigation of the charges made in the demand or complaint, the court may stay any proceeding until the investigation is completed.

(c) A proceeding commenced under this section may not be discontinued or settled without the court's approval. If the court determines that a proposed discontinuance or settlement will substantially affect the interest of the corporation's shareholders or a class of shareholders, the court shall direct that notice be given the shareholders affected.

(d) On termination of the proceeding the court may require the plaintiff to pay any defendant's reasonable expenses (including counsel fees) incurred in defending the proceeding if it finds that the proceeding was commenced without reasonable cause.

(e) For purposes of this section, "shareholder" includes a beneficial owner whose shares are held in a voting trust or held by a nominee on his behalf.

Official Comment

f. There Need Be No Prior Notice to or Demand on Shareholders

Rule 23.1 of the Federal Rules of Civil Procedure requires that, in addition to a demand on the board of directors, a demand be made on shareholders "if necessary." The statutes of a number of states, including California and New York, require demands only on boards of directors.

Although a demand on shareholders seems generally consistent with the broad doctrine of requiring exhaustion of all internal avenues of relief before commencement of suit, the board of directors, not the shareholders, is charged with governance of the corporation, including the commencement and management of litigation. Further, to require a demand on shareholders would virtually require the plaintiff to engage in a preliminary proxy contest and, in the case of publicly held corporations, would greatly increase the costs of filing all derivative suits, discouraging even legitimate cases.

For these reasons, it was concluded that the requirement of a demand on shareholders would add uncertainty, expense, and delay without commensurately improving the prospects of resolving the substantive issues.

h. Plaintiffs Are Not Required to Post Bond as Security for Expenses

Earlier versions of the Model Act and the statutes of many states required a plaintiff to give security for reasonable expenses, including attorneys' fees, if his holdings of shares did not reach a specified size or value-five percent of the outstanding shares or a value of $25,000 in the earlier version of the Model Act. This requirement has been deleted. The security for expenses requirement, to the extent it was based on the size or value of the plaintiff's holdings rather than on the apparent good faith of his claim, was subject to criticism that it unreasonably discriminated against small shareholders.

The basic policy question with respect to the requirement of a bond for small shareholders is how far to go in protecting the corporation and its officers and directors from suits. The choice is between making the right to sue widely available, without obstacles except in obviously baseless cases, or imposing obstacles in the way of the small shareholder without imposing a similar obstacle in the way of the large shareholder. Moreover, no bond requirement exists for class actions, anti-trust cases, or individual actions for personal injury, all of which involve the corporation in substantial expense of defending against suit.

Several states have concluded on the basis of these considerations that the bond requirement for small plaintiffs should be repealed or not adopted. . .

[New] Subchapter D

Derivative Proceedings

7.40 Subchapter Definitions

In this subchapter:

(1) "Derivative proceeding" means a civil suit in the right of a domestic corporation or, to the extent provided in section 7.47, in the right of a foreign corporation.

(2) "Shareholder" includes a beneficial owner whose shares are held in a voting trust or held by a nominee on the beneficial owner's behalf.

Official Comment

The definition of "derivative proceeding" makes it clear that the subchapter applies to foreign corporations only to the extent provided in section 7.47. Section 7.47 provides that the law of the jurisdiction of incorporation governs except for sections 7. 43 (stay of proceedings), 7.45 (discontinuance or settlement) and 7.46 (payment of expenses). See the Official Comment to section 7.47.

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 (dissenters' rights) and section 16.02(f) (inspection of records by a shareholder). In the context of subchapter D, 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 which includes persons with the right to vote or dispose of the shares even though they have no economic interest in them.

7.41 Standing

A shareholder may not commence or maintain a derivative proceeding unless the shareholder:

(1) was a shareholder of the corporation at the time of the act or omission complained of or became a shareholder through transfer by operation of law from one who was a shareholder at that time; and

(2) fairly and adequately represents the interests of the corporation in enforcing the right of the corporation.

Official Comment.

Section 7.41 requires the plaintiff to be a shareholder and therefore does not permit creditors or holders of options, warrants, or conversion rights to commence a derivative proceeding.

Section 7.41(2) follows the requirement of Federal Rule of Civil Procedure 23.1 with the exception that the plaintiff must fairly and adequately represent the interests of the corporation rather than shareholders similarly situated as provided in the rule. The clarity of the rule's language in this regard has been questioned by the courts. See Nolen v. Shaw-Walker Company, 449 F.2d 506, 508 n. 4 (6th Cir.1971). Furthermore, it is believed that the reference to the corporation in section 7.41(2) more properly reflects the nature of the derivative suit.

The introductory language of section 7.41 refers both to the commencement and maintenance of the proceeding to make it clear that the proceeding should be dismissed if, after commencement, the plaintiff ceases to be a shareholder or a fair and adequate representative. The latter would occur, for example, if the plaintiff were using the proceeding for personal advantage. If a plaintiff no longer has standing, courts have in a number of instances provided an opportunity for one or more other shareholders to intervene.

7.42 Demand

No shareholder may commence a derivative proceeding until:

(1) a written demand has been made upon the corporation to take suitable action; and

(2) 90 days have expired from the date the demand was made unless the shareholder has earlier been notified that the demand has been rejected by the corporation or unless irreparable injury to the corporation would result by waiting for the expiration of the 90 day period.

Official Comment

Section 7.42 requires a written demand on the corporation in all cases. The demand must be made at least 90 days before commencement of suit unless irreparable injury to the corporation would result. This approach has been adopted for two reasons. First, even though no director may be independent, the demand will give the board of directors the opportunity to reexamine the act complained of in the light of a potential lawsuit and take corrective action. Secondly, the provision eliminates the time and expense of the litigants and the court involved in litigating the question whether demand is required. It is believed that requiring a demand in all cases does not impose an onerous burden since a relatively short waiting period of 90 days is provided and this period may be shortened if irreparable injury to the corporation would result by waiting for the expiration of the 90 day period. Moreover, the cases in which demand is excused are relatively rare. Many plaintiffs' counsel as a matter of practice make a demand in all cases rather than litigate the issue whether demand is excused.

1. Form of Demand

Section 7.42 specifies only that the demand shall be in writing. The demand should, however, set forth the facts concerning share ownership and be sufficiently specific to apprise the corporation of the action sought to be taken and the grounds for that action so that the demand can be evaluated. See Allison v. General Motors Corp., 604 F.Supp. 1106, 1117 (D. Del.1985). Detailed pleading is not required since the corporation can contact the shareholder for clarification if there are any questions. In keeping with the spirit of this section, the specificity of the demand should not become a new source of dilatory motions.

2. Upon Whom Demand Should Be Made

Section 7.42 states that demand shall be made upon the corporation. Reference is not made specifically to the board of directors as in previous section 7.40(b) since there may be instances, such as a decision to sue a third party for an injury to the corporation, in which the taking of, or refusal to take, action would fall within the authority of an officer of the corporation. Nevertheless, it is expected that in most cases the

board of directors will be the appropriate body to review the demand.

To ensure that the demand reaches the appropriate person for review, it should be addressed to the board of directors, chief executive officer or corporate secretary of the corporation at its principal office.

3. The 90 Day Period.

Two exceptions are provided to the 90 day waiting period. The first exception is the situation where the shareholder has been notified of the rejection of the demand prior to the end of the 90 days. The second exception is where irreparable injury to the corporation would otherwise result if the commencement of the proceeding is delayed for the 90 day period. The standard to be applied is intended to be the same as that governing the entry of a preliminary injunction. Compare Gimbel v. Signal Cos., 316 A. 2d 599 (Del. Ch.1974) with Gelco Corp. v. Coniston Partners, 811 F.2d 414 (8th Cir.1987). Other factors may also be considered such as the possible expiration of the statute of limitations although this would depend on the period of time during which the shareholder was aware of the grounds for the proceeding.

It should be noted that the shareholder bringing suit does not necessarily have to be the person making the demand. Only one demand need be made in order for the corporation to consider whether to take corrective action.

4. Response by the Corporation

There is no obligation on the part of the corporation to respond to the demand. However, if the corporation, after receiving the demand, decides to institute litigation or, after a derivative proceeding has commenced, decides to assume control of the litigation, the shareholder's right to commence or control the proceeding ends unless it can be shown that the corporation will not adequately pursue the matter. .

7.43 Stay of Proceedings

If the corporation commences an inquiry into the allegations made in the demand or complaint, the court may stay any derivative proceeding for such period as the court deems appropriate.

Official Comment

Section 7.43 provides that if the corporation undertakes an inquiry, the court may in its discretion stay the proceeding for such period as the court deems appropriate. This might occur where the complaint is filed 90 days after demand but the inquiry into the matters raised by the demand has not been completed or where a demand has not been investigated but the corporation commences the inquiry after the complaint has been filed. In either case, it is expected that the court will monitor the

course of the inquiry to ensure that it is proceeding expeditiously and in good faith.

7.44 Dismissal

(a) A derivative proceeding shall be dismissed by the court on motion by the corporation if one of the groups specified in subsections (b) or (f) has determined in good faith after conducting a reasonable inquiry upon which its conclusions are based that the maintenance of the derivative proceeding is not in the best interests of the corporation.

(b) Unless a panel is appointed pursuant to subsection (f), the determination in subsection (a) shall be made by:

(1) a majority vote of independent directors present at a meeting of the board of directors if the independent directors constitute a quorum; or

/* It is important to note that the Model Business Corporation Act provides that derivative suits are subject to dismissal if the corporation has a truly independent review of the case and determines that it is not in the bests interests of the corporation. Note that this does not mean that the test is not whether it is meritorious or not. */