What You Need to Know About Nebraska's New Model Business Corporation Act

by Amber N. Preston[1]

The body of Nebraska statutory law governing corporations is scheduled to change significantly on January 1, 2017.[2] While these changes were adopted by the Legislature over two years ago, their effective date was delayed until January 1, 2017, to provide the Legislature time to address various concerns raised by practitioners. This article provides a brief overview of Nebraska statutory corporate law as it exists today and summarizes the key changes which become effective in 2017.

Background

Nebraska adopted the Business Corporation Act (the "Current Act") in 1995.[3] The Current Act is based on the Model Business Corporation Act ("MBCA") as approved and promulgated by the Committee of Corporate Law of the Section of Business Law of American Bar Association (the "ABA"). The MBCA is designed as a free-standing general corporation statute that can be adopted in its entirety by individual states.[4] The first ABA model act was promulgated in 1950 and substantially rewritten in 1984.[5] Currently, at least 32 states have adopted all or substantially all of the MBCA, and two other states have a model act based on the 1969 ABA model act.[6]

Since adopting the Current Act in 1995, Nebraska has implemented very few of the ABA's changes to the MBCA.[7] With a few notable exceptions,[8] the Nebraska Model Business Corporation Act (the "Revised Act") largely tracks the language of the MBCA. This consistency enables practitioners to consult the MBCA's commentary, as well as the case law from other states which have adopted the MBCA, to fill gaps and otherwise interpret and apply the corresponding Nebraska provisions.

The Nebraska Model Business Corporation Act

In 2014, the Nebraska Legislature adopted the Revised Act,[9] which repealed and replaced the Current Act in its entirety. In 2015, however, the Legislature, at the request of the Nebraska State Bar Association, delayed the operative date of the new Revised Act in order to address a number of issues raised by practitioners and others. Several amendments were proposed, the most significant of which were to preserve the grandfathering of preemptive rights for shareholders of corporations formed before 1996;[10] to clarify that directors may be elected by less than unanimous consent (as such is inconsistent with cumulative voting provisions);[11] and to confirm that dissenters' rights are not available for shareholders of banks, bank holding companies, and other financial institutions.[12] The Legislature eventually passed L.B. 794 to address these and other concerns.

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This article by no means purports to be an exhaustive analysis of the differences between the Current Act and the Revised Act.[13] Rather, what follows is a brief overview of the most significant changes adopted in the Revised Act, organized into sections addressing those changes impacting shareholders, directors, and officers, respectively, and a section covering miscellaneous changes.

A. Impacts on the Shareholders

The changes in the Revised Act which will most significantly impact shareholders are the allowance of electronic notices, the revision of the default rules governing special meetings and written consent in lieu thereof, the modification of various default shareholder approval thresholds, and the addition of a receivership remedy in cases of management deadlock.

1. Electronic Notices

The Revised Act broadens the methods by which notices and other communications may be sent to include electronic means such as email. Electronic communications are subject to several unique requirements. First, the recipient must have consented to receive notices by such electronic means.[14] Second, the recipient may revoke consent at any time and will be deemed to have revoked consent where either (a) the corporation is unable to deliver two consecutive electronic transmissions or (b) the secretary or assistant secretary of the corporation becomes aware of the recipient's inability to receive electronic transmissions.[15] Finally, once consent is obtained, and provided there has been no revocation or deemed revocation of the same, an electronic transmission is considered received regardless of whether the recipient is aware of its receipt. For example, the ABA suggests in its Commentary to the MBCA that an electronic transmission would be received by a recipient notwithstanding the fact that it is blocked by the recipient's electronic filters or firewalls, reasoning that a recipient who consents to receipt of notices by electronic means is responsible for any filters or firewalls blocking the recipient's access to them.[16]

While these new provisions certainly have the potential to reduce the time and cost associated with delivery of such notices, it should be stressed that the only permissible method of obtaining a shareholder's consent to electronic transmission of notice is by writing in advance—neither the corporation's articles nor its bylaws can authorize or require electronic transmission of notices.[17]

2. Shareholder Meetings

The Revised Act includes a number of changes which will affect the shareholders' ability to call and participate in meetings. First, the Revised Act permits a corporation to vary the voting threshold required for shareholders to call a special meeting. While Current Act and the Revised Act both provide that a special shareholder meeting may be called by the holders of at least 10% of the votes entitled to be cast at that meeting, the Current Act does not permit variance from this 10% threshold.[18] The Revised Act, however, permits a corporation to either reduce this threshold below 10% or to increase it up to 25%; provided, in all cases, that the corporation includes this provision in its articles of incorporation.[19]

Second, the Revised Act also allows a corporation to vary the percentage of shareholders required to approve an action by written consent in lieu of a meeting. Under the Current Act, shareholder consent in lieu of a meeting can only be accomplished by *unanimous written consent*.[20] The Revised Act permits a corporation to reduce this threshold below unanimity, provided the corporation makes an appropriate provision in its articles of incorporation and the threshold is the same as would be required to authorize the transaction at a meeting of the shareholders.[21] Further, if an action is taken by less than unanimous written consent of shareholders, the corporation must give nonconsenting shareholders written notice of the action *not more than 10 days* after a sufficient number of written consents have been delivered to the corporation or such later date that the tabulation of consents is completed.[22]

Third, the Revised Act permits remote participation by shareholders in annual and special meetings. Under the Current Act, a shareholder meeting must be held at the place stated in the bylaws or, if the bylaws are silent, at the corporation's principal office.[23] Thus, the Current Act does not expressly authorize anything other than a physical meeting of shareholders. Given the advances in technology which have made remote participation increasingly available and desirable, the Revised Act includes a provision clarifying and reinforcing the use of remote communication to conduct a meeting without a quorum physically present. Under the Revised Act, shareholders may participate in meetings "by means of remote communication to the extent the Board of Directors authorizes such participation" and such participation will be subject to the board's guidelines and procedures.[24] A shareholder participating remotely may vote at the meeting only if the corporation has both implemented reasonable measures to verify the shareholder's right to vote and provided the shareholder with a reasonable opportunity to participate in the meeting.[25] Remote participation may include telephone conferences or Internet communications. Note that the Revised Act still does not permit entirely virtual meetings—those meetings in which no one is physically present at the designated location—rather, it permits only "hybrid shareholder meeting" approval, meaning that a physical location is designated for the meeting, virtual participation is permitted, and each shareholder may decide whether and how to participate.

3. Shareholder Approval

The Revised Act includes a number of changes related

to the shareholder approval thresholds required for certain corporation actions. First, the Revised Act adds a new subsection describing when the corporation must have shareholder approval prior to issuing shares for consideration other than cash. In cases where the proposed issuance for non-cash consideration comprises more than 20% of the voting power of all shares outstanding—as calculated before the proposed transaction—the corporation, prior to the issuance, must obtain shareholder approval at a meeting at which a quorum consisting of at least a majority of the votes entitled to be cast on the matter is present.[26] For example, if ABC Corporation has 2 million shares of voting common stock issued and outstanding and proposes to issue 400,000 shares of common stock in exchange for a business owned by XYZ Corporation, then no shareholder approval is required (400,000 ÷ 2,000,000 = 20%). On the other hand, if 400,001 shares are issued, then shareholder approval would be required prior to the issuance. This change was largely motivated by and modeled after the NYSE and NASDAQ Marketplace Rules and will afford shareholders an additional layer of protection.[27]

Second, the Revised Act eliminates the heightened shareholder approval threshold where a corporation proposes an amendment to its articles of incorporation which would create dissenters' rights. Under the Current Act, such an amendment would require a two-thirds majority of the votes entitled to be cast.[28] The Revised Act reduces this threshold to a majority.[29]

Third, the Revised Act reduces the default shareholder approval threshold required for a proposed merger. Under the Current Act, a plan of merger must be approved by *a majority of all votes entitled be cast* on the plan unless the articles of incorporation or board of directors requires a greater vote.[30] Under the Revised Act, a plan of merger must be approved by *a majority vote at a meeting at which a quorum consisting of at least a majority entitled to be cast is present* unless the articles of incorporation or board of directors requires a greater vote.[31] To illustrate the impact of this change, assume that ABC Corporation has 10,000 shares of common stock outstanding and proposes to merge with XYZ Corporation. Under the Current Act, the proposed transaction would require the favorable vote of at least 5,001 ABC shares (which represents 100% of the required quorum) to move forward. Under the Revised Act, at least 5,001 ABC shares must be present to establish a quorum, but, assuming only this minimum number were present at the meeting, only 2,501 of these shares would be required to approve the merger.

Finally, the Revised Act changes the default rule with respect to the shareholder approval threshold for the proposed sale of all or substantially all of the corporation's assets. Under the Current Act, such a sale must be approved by two-thirds of the shares entitled to vote unless the articles of incorporation or board of directors established a higher threshold.[32] Under the Revised Act, however, the same transaction would only require majority approval by shareholders at a meeting for which a quorum consisting of at least a majority of the votes entitled to be cast is present.[33] Using the example above, if ABC Corporation decided to pursue an asset sale rather than a merger, the Current Act would require the favorable vote of at least 6,667 shares. However, Revised Act would require only the favorable vote by a majority of the shares at meeting for which a quorum is present—an approval threshold which could be as low as 2,501 shares if only the minimum number required to establish a quorum—5,001—were present at the meeting.

4. Deadlock

The Revised Act creates a new statutory remedy for shareholders faced with a management deadlock. Under both Acts, shareholders have the option to file a petition for judicial dissolution for, among other things, a deadlock among the directors in the management of the corporation's affairs.[34] This remedy, however, carries significant risk for a shareholder: the corporation may elect to purchase the petitioning shareholder's shares and, after a hearing to determine the fair value of the shares, the court will order the purchase the petitioning shareholder's shares and the matter resolved.[35]

The Revised Act affords shareholders confronted by management deadlock with an alternative to this rather high-stakes proposition: the shareholder may petition the court to appoint a custodian without also requesting dissolution and thereby triggering its attendant buyout option. Section 21-283(d) provides that a "court may appoint one or more persons to be custodians, or, if the corporation is insolvent, to be receivers, of and for a corporation in a proceeding by a shareholder when it is established that . . . the directors are deadlocked in the management of the corporate affairs, the shareholders are unable to break the deadlock, and irreparable injury to the corporation is threatened or being suffered."[36] This remedy is also available in cases where "the directors or those in control of the corporation are acting fraudulently and irreparable injury to the corporation is threatened or being suffered."[37] In either case, the court may appoint an individual or corporation as a custodian or receiver and such person may exercise all the powers of the corporation, through or in place of its board of directors, to the extent necessary to manage the business and affairs of the corporation.[38]

B. Impacts on the Corporation's Board of Directors

The Revised Act includes several changes which will significantly impact directors: the expansion of the definition of conflicting interest transactions, the creation of a safe harbor for a director's pursuit of certain corporate opportunities, and the grant to directors of the ability to delegate to officers the grant of certain awards.

1. Expanded Definition of Conflict of Interest

The Revised Act expands the definition of "related persons" for the purpose of determining whether a transaction constitutes a conflict of interest. A director's conflicting interest transaction is a transaction with the corporation: (i) to which the director is a party; (ii) respecting which the director had knowledge and a material financial interest known to the director; or (iii) respecting which the director knew that a related person was a party or had a material financial interest.[39] Under the Current Act, "related person" is defined as (a) the spouse, or a parent or sibling thereof, of the director; (b) a child, grandchild, sibling, parent, or spouse of any thereof, of the director; or (c) an individual having the same home as the director.[40] The Revised Act added the following relatives to the definition: stepchild, stepparent, stepsibling, half-sibling, aunt, uncle, niece or nephew, or spouse of any thereof.[41] Thus, the analysis of whether a proposed transaction involves a conflicting interest must be broadened accordingly.

The Revised Act also adopts a definition of "material financial interest," which is a financial interest in a transaction that "would reasonably be expected to impair the objectivity of the director's judgment when participating in action on the authorization of the transaction."[42] This standard is intended to be objective, rather than subjective.[43]

2. Business Opportunities

Recognizing that corporations neither need nor desire to pursue all available business opportunities presented to them, the Revised Act creates a safe harbor under which directors may pursue certain of the corporation's business opportunities.[44] Any director who pursues a corporation's business opportunity risks compromising his or her fiduciary duty of loyalty. The Revised Act allows a director to mitigate this risk in certain circumstances. Under Section 21-2124, a director may pursue a corporate opportunity if (a) the director brings it to the corporation's attention *before* incurring any legal obligation with respect to such opportunity and (b) qualified directors, shareholders, or both are afforded the option to disclaim the opportunity.[45] The shareholders and directors can delay the decision to disclaim any interest or attach conditions to such disclaimers. It is imperative that this process be completed before the director takes advantage of the opportunity; otherwise, the director may not be afforded protection under this safe harbor. However, this safe harbor is not the only means by which a director may pursue a corporate opportunity without compromising his or her fiduciary obligations: any other legal basis for the director's action remains intact and the director's failure to qualify an opportunity under this safe harbor should not result in any negative inferences.[46]

3. Ability to Delegate Awards of Rights, Options, and Warrants

The Current Act authorizes the board of directors to determine the terms upon which rights, options, or warrants are issued.[47] The Revised Act grants the board of directors the ability to delegate to corporate officers the authority to select recipients of rights, options, and warrants and the number and terms of such rights, options, or warrants.[48] For corporations with stock option plans, the board of directors may authorize one or more officers to (a) designate the recipients of stock options (or other equity compensation awards) and (b) determine, within amounts and restrictions set by the board of directors, the number of options and other terms.[49] An officer delegated this authority may not award himself or herself any options.[50]

C. Impacts on the Corporation's Officers

The Revised Act clarifies that corporate officers have an affirmative duty to report material violations of the law and other material breaches of fiduciary obligations.[51] This duty includes the requirement that an officer inform, as appropriate, his or her superior officers, another person within the corporation, the board of directors, or a board committee of any (a) actual or probable material violation of law involving the corporation or (b) material breach of duty to the corporation by an officer, employee, or agent of the corporation that the officer believes has occurred or is likely to occur.[52] It should be noted that the officer's compliance with this provision will be analyzed under a "subject belief" standard rather than objective knowledge standard;[53] that is, the fundamental inquiry is whether the officer should have concluded that the misconduct was occurring.[54]

D. Miscellaneous Changes

This final section highlights several of the more significant miscellaneous changes adopted in the Revised Act.

1. Use of Outside Facts in Articles of Incorporation

The Revised Act provides that the articles of incorporation may now be dependent upon facts objectively ascertainable outside the document itself.[55] The Current Act is silent on this issue, leaving tenuous the common practice of describing the terms of preferred shares by reference to market benchmarks. For instance, a certificate of designation may describe the applicable interest rate by reference to federal funds or securities market prices. Such a designation is expressly permitted under the Revised Act provided the corporation follows the informational, filing, and other requirements set forth in Section 21-203(k).

2. Domestication

The Revised Act provides for the domestication of foreign corporations in Nebraska and for Nebraska corporations to become domesticated in other jurisdictions. In either case, the board of directors initiates the process by preparing a plan of domestication. The plan should include the following: (a) the proposed new jurisdiction; (b) the terms and conditions of the domestication; (c) the manner of reclassifying shares following domestication; and (d) amendments, if any, to the articles of incorporation to become effective upon domestication.[56] The board of directors then submits the plan to the shareholders, and a majority is required to approve the plan, unless the articles of incorporation designate a higher approval threshold.[57] If the plan is approved, the board of directors must have articles of surrender prepared and filed with the Nebraska Secretary of State.[58] The articles of surrender should include the corporation's name, a statement that the corporation intends to domesticate elsewhere, a statement that domestication has been properly approved, and the prospective jurisdiction of domestication.[59]

3. Sale of "Substantially All" Assets

Most, if not all, states' corporate statutes contain certain exceptions to the directors' broad discretion in managing the affairs of a corporation. Chief among these exceptions is the directors' inability to effect a sale of all or nearly all of the corporation's assets without first obtaining shareholder approval. The Current Act relies on the nearly ubiquitous "all or substantially all" standard in assessing whether shareholder approval is required[60] and, in cases where this standard has been satisfied, requires that the sale first be approved by a vote of two-thirds of all votes entitled to be cast on the transaction.[61]

The Revised Act establishes a new standard for such transactions—shareholder approval is required "if the disposition would leave the corporation without a significant continuing business activity"[62]—and provides a two-pronged analysis for determining whether a significant continuing business activity remains. A corporation "will conclusively be deemed to have retained a significant continuing business activity" if the corporation retains a business activity that represents both (a) at least 25% of the total assets at the end of the most recently completed fiscal year and (b) 25% of either income from continuing operations for that fiscal year (before taxes) or revenues from continuing operations for that fiscal year (in each case of the corporation and its subsidiaries on a consolidated basis).[63] The "all or substantially all" standard of the Current Act has been the subject of varying case law interpretations, but the Revised Act's new standard—whether a corporation has retained significant continuing business activities—presents a more objective test.[64]

Conclusion

Beginning January 1, 2017,[65] Nebraska's body of statutory law governing corporations will change substantially. The Revised Act further aligns Nebraska law with the ABA's MBCA and the significant number of states which have adopted it. This consistency promises to afford Nebraska prac-

titioners greater certainty as the MBCA's provisions continue to be interpreted and applied in courts throughout the country.

Endnotes

1 I would like to thank my colleague and mentor, Dennis J. Fogland, a partner at Baird Holm LLP, for all of his insight and research in connection with Nebraska's adoption of the updated version of the Model Business Corporation Act, as well as my personal editor, Stephen Q. Preston, for his assistance.

2 *See* L.B. 749, 103rd Leg. Sess. (Neb. 2014); L.B. 157, 104th Leg. Sess. (Neb. 2015); and L.B. 794, 104th Leg. Sess. (Neb. 2016) L.B. 749 adopted the ABA's current Model Business Corporation Act and repealed the Current Act (defined below). L.B. 157 delayed the operative date from January 1, 2016 to January 1, 2017. L.B. 794 amended the Revised Act (defined below), as passed in 2014, to incorporate amendments prior to the operative date.

3 The Business Corporation Act, NEB. REV. STAT. §§ 21-2001 - 21-20,197, which will be repealed in its entirety on December 31, 2016, is referred to in this Article simply as the "Current Act" and citations to the same in these endnotes will not designate it as "repealed".

4 *See* Introduction to the MODEL BUS. CORP. ACT (2013).

5 *Id*.

6 *Id*.

7 *See* L.B. 749 – Introducer's Statement of Intent.

8 The most significant of these exceptions have been reconciled by the amendatory legislation referenced below.

9 The Nebraska Model Business Corporation Act, NEB. REV. STAT. §§ 21-201 - 21-2,232 and Section 11 and 14 (Effective January 1, 2017) is referred to in this Article simply as the "Revised Act" and citations to the same in these endnotes will not designate its effective date.

10 Historically, shareholders of Nebraska corporations incorporated before January 1, 1996, have had preemptive rights if the applicable articles of incorporation are silent. Conversely, shareholders of Nebraska corporations incorporated after such date do not have preemptive rights unless expressly provided for in the articles of incorporation. In 2014, when the Revised Act was originally adopted, it did not include a grandfathering provision for corporations incorporated prior to January 1, 1996. In 2016, the Legislature amended the newly adopted Section 21-250 of the Revised Act to grandfather these rights for corporations formed before 1996.

11 NEB. REV. STAT. § 21-253 (striking in 2016, the final clause in subsection (a): "except that directors may not be elected by less than unanimous consent").

12 NEB. REV. STAT. § 21-2,172(d) (subsection (d) essentially mirrors the prior provision provided in NEB. REV. STAT. § 21-20,138(3).

13 I would also like to thank Hannah K. Fischer and AriAnna Goldstein, my colleagues at Baird Holm LLP, for all of their work on a 227-page Memorandum comparing the Revised Act to the Current Act. A copy of such Memorandum is available at www.nebar.com/?page=CLEMaterials.

14 NEB. REV. STAT. § 21-215.

15 *Id*. at subsection (f).

16 *See* Commentary to MODEL BUS. CORP. ACT §1.41 (2013).

17 While shareholder consent in writing is required for electronic notice, Neb. Rev. Stat. § 21-215(l) allows a corporation's articles or bylaws to "authorize or require" delivery of notices of *meetings of directors* by electronic transmission.

18 NEB. REV. STAT. § 21-2052(1)(b).

19 NEB. REV. STAT. § 21-254(a).

20 NEB. REV. STAT. § 21-2054.

21 NEB. REV. STAT. § 21-256(b). The Revised Act continues to require that directors must be elected by unanimous written consent. *Id*.

22 NEB. REV. STAT. § 21-256(e).

23 NEB. REV. STAT. § 21-2051.

24 NEB. REV. STAT. § 21-261(a).

25 NEB. REV. STAT. § 21-261(b).

26 NEB. REV. STAT. § 21-242(f).

27 *See* Commentary to MODEL BUS. CORP. ACT §6.21 (2013).

28 NEB. REV. STAT. § 21-20,118(5).

29 NEB. REV. STAT. § 21-2,152.

30 NEB. REV. STAT. § 21-20,130(5).

31 NEB. REV. STAT. § 21-2,164(5).

32 NEB. REV. STAT. § 21-20,136.

33 NEB. REV. STAT. § 21-2,170.

34 NEB. REV. STAT. §21-20,162 (Repealed); Compare to NEB. REV. STAT. §21-21,197.

35 Id.

36 NEB. REV. STAT. § 21-283.

37 NEB. REV. STAT. § 21-283(a)(1).

38 NEB. REV. STAT. § 21-283(d)(1).

39 NEB. REV. STAT. § 21-2,120(1).

40 NEB. REV. STAT. § 21-20,112(3).

41 NEB. REV. STAT. § 21-2,120(5).

42 NEB. REV. STAT. § 21-2,120(4).

43 *See*, Commentary to MODEL BUS. CORP. ACT. § 8.60 (2013).

44 No statutory definition of business opportunity exists; however, courts have interpreted "corporate opportunity," which could impact interpretations of business opportunity. *See*, Commentary to MODEL BUS. CORP. ACT. § 8.70 (2013).

45 *Id*.

46 *Id*.

47 NEB. REV. STAT. § 21-2043.

48 NEB. REV. STAT. § 21-245(c).

49 *Id*.

50 *Id*.

51 NEB. REV. STAT. § 21-2,107(b). The ABA's commentary to the corresponding MBCA provision reflects that this is not a "new" duty; rather, it has long been recognized at common law and is encompassed within a director's broader duties to act in good faith and with reasonable care. *See* MODEL BUS. CORP. ACT § 8.42 (2013).

52 *Id*.

53 *Id*. The use of "material" modifying laws denotes both qualitative and quantitative standards.

54 *Id*.

55 NEB. REV. STAT. §§ 21-203(k) & 21-220(d).

56 NEB. REV. STAT. § 21-2,127.

57 NEB. REV. STAT. § 21-2,128.

58 NEB. REV. STAT. § 21-2,130.

59 *Id*.

60 NEB. REV. STAT. § 21-20,136.

61 *Id*.

62 NEB. REV. STAT. § 21-2,170(a).

63 *Id*.

64 Commentary to the MODEL BUS. CORP. ACT § 12.02 (2013).

65 Like the Current Act, the Revised Act includes a saving clause which provides that any proceeding, reorganization, or dissolution commenced prior to January 1, 2017, may be completed in accordance with the Current Act as if it had not been repealed. *See* NEB. REV. STAT. § 21-2,232.