

Department of Legislative Services
Maryland General Assembly
2002 Session

FISCAL NOTE

House Bill 388 (Delegates Barve and Brown)

Economic Matters

Judicial Proceedings

Corporations and Real Estate Investment Trusts

This bill makes changes to the provisions applicable to corporations and real estate investment trusts (REITs) concerning assets, powers, dissolution, signatures, stock issuance, director conduct and liability, and stockholder consent and inspection rights.

The bill is effective June 1, 2002.

Fiscal Summary

State Effect: The bill pertains almost exclusively to private sector activities and will not materially affect State finances or operations.

Local Effect: None.

Small Business Effect: Minimal. The bill would predominantly affect larger businesses.

Analysis

Bill Summary:

Corporate Assets

The bill excludes from the definition of “transfer assets,” “transfer its assets,” and “transfer of assets” transactions after which the corporation continues to: (1) own assets constituting 25% of total assets at the end of the most recently completed fiscal year; and (2) engage in a business activity that represented 25% of either income from continuing operations before taxes or revenues from continuing operations for the most recently

completed fiscal year. Failure to come within this exclusion does not create an inference that a corporation is transferring all or substantially all of its assets.

Filings with SDAT

The bill authorizes a signature on a document required or permitted to be filed with the State Department of Assessments and Taxation (SDAT) under any provision of the Maryland General Corporation Law or the Maryland REIT to be a facsimile.

Determinations

The bill adds determinations relating to assets and liabilities, book value, fair value, and authorization of a distribution to the matters that are considered *prima facie* proper if: (1) specific provisions of Maryland corporate law do not require otherwise; and (2) the determination is made in good faith in accordance with generally accepted accounting practices and principles. The bill allows determinations considered *prima facie* proper to be for the corporation separately or for the corporation and its subsidiaries on a consolidated basis.

Qualification as a REIT

The bill increases from 100 to 110 the number of persons to whom a corporation may issue shares of its stock without consideration for the purpose of qualifying the corporation as a REIT.

Articles Supplementary

The bill specifies that stock issued before the time that the articles supplementary are effective ceases to be voidable at the time that the articles supplementary become effective. In addition, a right or liability accrued by reason of the issuance of stock before the time the articles supplementary are effective is extinguished at the time the articles supplementary become effective, except to the extent that the person having the right has acted detrimentally in reliance on the right or liability.

Stock Liability

For corporations registered as investment companies under the Investment Company Act of 1940, the bill limits liability to the class of stock for which the liability is incurred, not against the corporation generally or another class or series of stock, if: (1) the corporate charter of an investment company creates one or more classes or series of stock; and (2) separate records are maintained for the series or class and its assets are held and accounted for separately. If those conditions are met, none of the investment company's liabilities generally are enforceable against the assets associated with the separated class or series.

Capital Surplus and Distributions

The bill repeals the provision requiring that a corporation's net assets that remain after a distribution, payment, or reduction of liability to be at least equal to the aggregate preferential amount payable in the event of voluntary liquidation to holders of stock having rights preferred to the rights of holders who received the distribution or payment, or whose liability was reduced.

For the meaning of "distribution," the bill includes transfers of money or other property of the corporation in respect of any of its shares. The bill repeals provisions regarding: (1) disclosure to stockholders of capital surplus; and (2) net assets of a corporation that remain after a distribution payment.

Directors and Officers

The bill includes the chief executive officer, chief operating officer, chief financial officer, and vice chairman of the board on the list of persons authorized to sign a stock certificate.

The bill includes a person, who while the director of a corporation, serves as a managing member of a limited liability company (LLC) within the meaning of a "director" entitled to the permitted indemnities for acts in the "official capacity" of a director. The bill adds service to another LLC to the list of exclusions from official capacity entitling the director to indemnification.

The bill removes the rebuttable presumption that the director did not meet the required standard for indemnification applicable for proceedings that terminate by a conviction, or a plea of *nolo contendere* or its equivalent. A corporation may obligate itself to indemnify and pay reasonable expenses in advance of the final disposition of a proceeding to the extent permitted. The bill repeals the requirement that an indemnification or advance of expenses to a director be reported to the stockholders.

Stockholder Consent and Inspection Rights

The bill authorizes: (1) stockholder consents to be given by electronic transmission; and (2) if a corporation's charter provides, a consent by stockholders having at least the minimum number of votes necessary to authorize or take action at a meeting, rather than by unanimous consent.

The bill restricts inspections to stockholders whose holdings represent shares of any class of stock entitled to cast 5% of the votes entitled to be cast in the election of directors.

Merger and Dissolution

The bill reduces the notice period, from 30 to 15 days before the articles are filed with SDAT, by which a parent corporation must give notice to all stockholders of a subsidiary corporation before a merger of the subsidiary into its parent corporation. The bill also reduces the period, from 30 to 15 days after this notice is given, during which a stockholder who desires to receive payment for stock rather than receive shares of the merged corporation. The bill removes the pre-dissolution notice requirement for employees.

Interested Stockholders

The bill allows a corporation or REIT to “opt in” to prohibitions against entering into the following business combinations with an interested stockholder for five years after the stockholder became an interested stockholder: (1) the adoption of a plan or proposal for the liquidation or dissolution of a corporation; (2) purchase or acquisition by the corporation of its own stock shares; and (3) an action or series of actions that would result in the change or conversion of voting stock shares that are not redeemable at the option of the holder.

REIT Powers

The bill authorizes a REIT to: (1) include in its declaration of trust any provision that is not inconsistent with applicable laws; (2) make guarantees; (3) invest its surplus funds, lend money when appropriate, and take and hold real and personal property for the payment of loaned or invested funds; (4) become involved in a partnership, joint venture, trust, or other enterprise; and (5) make gifts or contributions to or for the use of: (a) federal, state, or local government; or (b) a governmental or other organization for religious, charitable, scientific, civic, public welfare, literary, or educational purposes.

The bill authorizes a REIT’s board of trustees, without shareholder action and with the approval of two-thirds of its members, to amend the REIT’s declaration of trust to qualify as a REIT under the Internal Revenue Code or the Maryland REIT Law. The bill also authorizes a REIT’s board of trustees, without shareholder action and with a majority of the entire board of trustees, to amend the REIT’s declaration of trust in any respect that a corporation’s board of directors may amend the corporate charter without shareholder approval.

The bill imposes upon directors of a REIT the standard of conduct applicable to the directors of a corporation.

Current Law:

Corporate Assets

Stockholder approval is required for a transfer of all or substantially all of a corporation's assets. "Transfer assets," "transfer its assets," and "transfer of assets" mean to sell, lease, exchange, or otherwise transfer all or substantially all of the assets of a corporation. The term "substantially all of the assets of a corporation" is not defined.

Filings with SDAT

SDAT may accept documents that are filed by means of facsimile device. Such documents are subject to applicable regular and expedited filing fees.

Determinations

A determination required or permitted relating to capital, surplus, capital surplus, earned surplus, or other financial matter of a Maryland corporation is *prima facie* proper if: (1) specific provisions of Maryland corporate law do not require otherwise; and (2) the determination is made in good faith in accordance with generally accepted accounting practices and principles.

Qualification as a REIT

A corporation may issue shares of its stock to up to 100 persons without consideration for the purpose of qualifying the corporation as a REIT.

Articles Supplementary

A corporation must file articles supplementary with SDAT if under a power contained in its charter, the corporation's board of directors classifies or reclassifies any unissued stock. Articles supplementary must include: (1) a description of the stock; and (2) a statement that the stock has been classified or reclassified by the board under authority in the corporate charter.

Stock Liability

Liability among classes or series of stock is not limited for corporations registered as investment companies under the Investment Company Act of 1940.

Surplus and Distributions

A distribution means a direct or indirect transfer of money or other property, except a corporation's own shares declared or paid as a stock dividend or stock split; or (2) an incurrence or forgiveness of indebtedness by a corporation to or for the benefit of the corporation's stockholders in respect of any of its shares.

By resolution of its board of directors, a corporation may apply any part of the corporation's capital surplus to reduction of a corporate deficit or other proper corporate purpose. The application must be disclosed to stockholders in the corporation's next annual report.

A corporation's net assets that remain after a distribution, payment, or reduction of liability must be at least equal to the aggregate preferential amount payable in the event of voluntary liquidation to holders of stock having rights preferred to the rights of holders who received the distribution or payment, or whose liability was reduced.

Directors and Officers

A corporation's stock certificate must be signed by the president, a vice president, or the chairman of the board, and countersigned by the secretary, an assistant secretary, the treasurer, or an assistant treasurer.

A corporation may indemnify its directors who are made party to a proceeding by reason of service in that capacity unless: (1) the act or omission of a director was material to the matter at issue and was either: (a) committed in bad faith; or (b) the result of active or deliberate dishonesty; (2) the director received an improper personal benefit; or (3) in the case of a criminal proceeding, the director had reasonable cause to believe that the act or omission was unlawful. Indemnification may be as to judgments, penalties, fines, settlements, and reasonable expenses incurred in connection with the proceeding.

Directors entitled to indemnification include: any person who is or was a director of the corporation or a person who, while a director of the corporation is or was serving at the request of the corporation as a director, partner, trustee, employee, or agent of another corporation, partnership, joint venture, trust, other enterprise, or employee benefit plan.

Stockholder Consent and Inspection Rights

Stockholder consent to actions that could be taken at a stockholders meeting must be unanimous and written. One or more persons who together and for at least six months have at least 5% of any class of stock have inspection rights.

Merger and Dissolution

A parent corporation must give notice of a merger transaction to each of the subsidiary's minority stockholders on the date of giving notice or on a record date fixed for that purpose before the merger of the subsidiary into its parent corporation if: (1) both the parent corporation and its subsidiary are Maryland corporations; and (2) notice is not waived by all minority stockholders.

Unless otherwise allowed, a stockholder is bound by the terms of a merger transaction if: (1) the stock is listed; (2) the stock is a successor in a merger, unless certain conditions are met; (3) the stock is not entitled to be voted on the transaction or the stockholder did not own the stock on the record date to vote on the transaction; (4) the charter provided that the holders of the stock are not entitled to object; or (5) the stock is that of an open-end investment company.

At least 20 days prior to filing of articles of dissolution with SDAT, a corporation must provide notice that the dissolution has been approved to its employees and to all known creditors.

Interested Stockholders

With specified exceptions, a corporation may not engage in certain business combinations with an interested stockholder for five years following the most recent date on which the stockholder became an interested stockholder.

REIT Powers

A REIT has the power to: (1) unless otherwise provided, have perpetual existence; (2) sue and be sued; (3) transact business; (4) make contracts, incur liabilities, and borrow money; (5) lease, convey, pledge, or otherwise dispose of property; (6) issue bonds and other obligations; (7) acquire and hold real or personal property; (8) own stocks and bonds; (9) elect or appoint trustees and define their duties; (10) adopt and implement employee and officer benefit plans; (11) make and alter bylaws; (12) exercise trust powers under the law or trust documents; (13) enter certain business combinations; and (14) indemnify or advance expenses to officers, trustees, employees, and agents to the same extent as permitted for directors, officers, employees, and agents of a Maryland corporation.

Additional Information

Prior Introductions: An identical bill, HB 684, passed third reading as amended in the House during the 2001 session and received an unfavorable report from the Senate Judicial Proceedings Committee. HB 684 was the subject of a briefing before the Judicial Proceedings Committee during the 2001 interim.

Cross File: SB 123 (Senator Baker) – Judicial Proceedings.

Information Source(s): Department of Assessments and Taxation, Department of Legislative Services

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