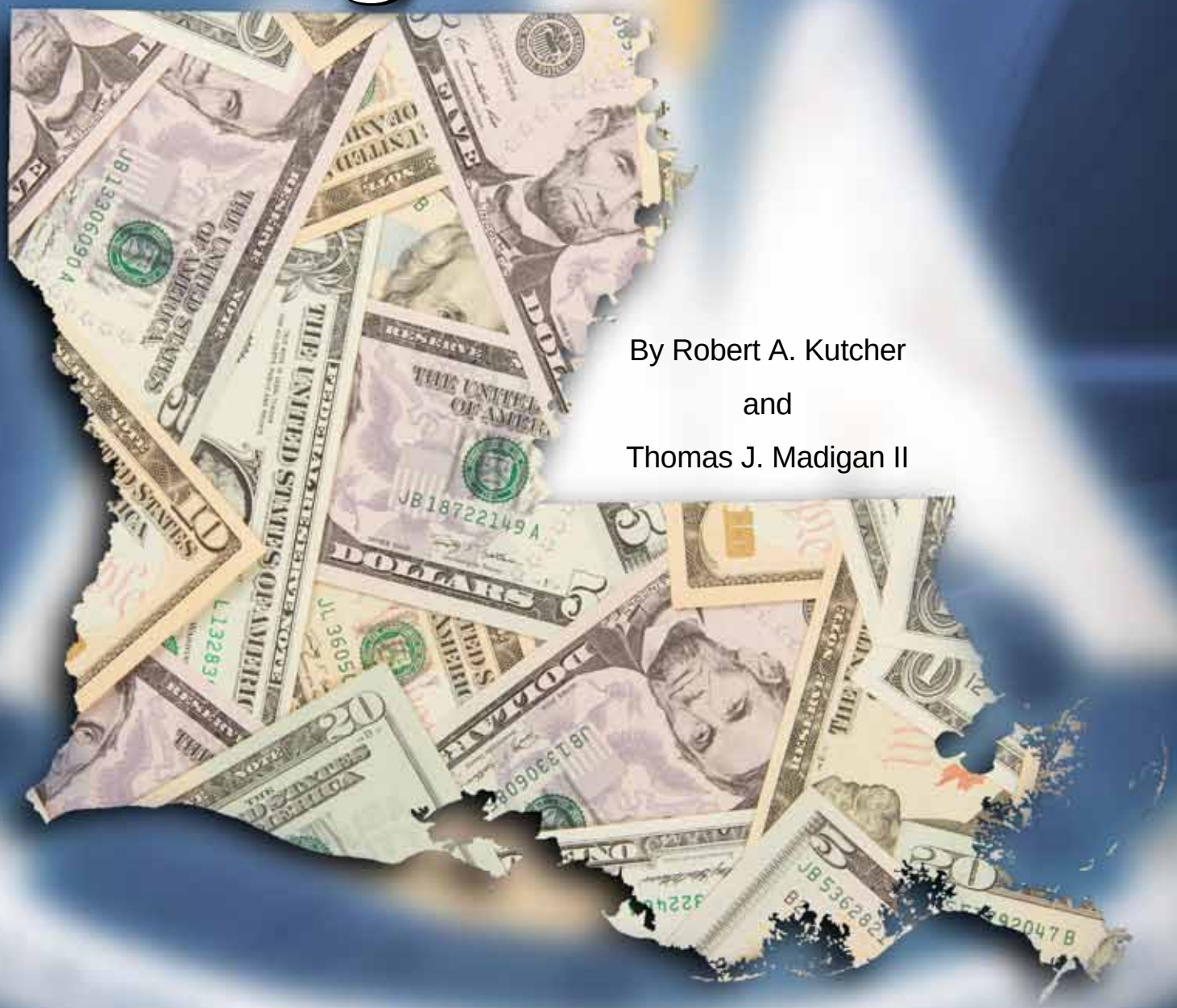
The Brand New Louisiana Business Corporation Law: *Diving Into Act 328*



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and

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In May 2014, Louisiana enacted Act 328 of the 2014 Regular Legislative Session, overhauling Louisiana's statutory business corporations law. Effective Jan. 1, 2015, a modified version of the American Bar Association's Model Business Corporations Act (MBCA) governs Louisiana corporations. Act 328 repeals Louisiana Revised Statutes sections 12:1 through 12:178 and 12:1605 through 12:1607. In its place, Act 328 enacts 12:1-101 through 12:1-1704 in a numbering system that corresponds to the MBCA. Act 328 also amends other related legislation, including Louisiana Code of Civil Procedure article 611 regarding derivative actions.

Act 328 itself provides little guidance on the impetus or purpose behind the new legislation. Practitioners and the business community may lament such an apparent overhaul without a stated purpose. One obvious purpose behind Act 328, however, is to keep pace with the rest of the country, lest Louisiana be perceived as receding into a corporate backwater without enough awareness to adopt modern model legislation. At a minimum, Act 328 will number Louisiana's corporations legislation in conformity with most other jurisdictions, making it easier to locate corresponding jurisprudence from other jurisdictions — not only for the litigator arguing *res nova* issues, but also for guidance to the transactional practitioner. In short, Act 328 puts Louisiana in, and keeps Louisiana closer to, the national discourse on corporations law, and it eschews potential misperceptions about Louisiana attitudes towards business.

Act 328 is more of a detailed re-codification than a substantive overhaul of Louisiana corporations statutes. Act 328 retains many of Louisiana's non-uniform provisions, ranging from retaining civilian terminology such as "immovable" property when it is located in Louisiana (new § 1-141) to retaining the retroactivity of corporate existence when a corporate agent acquires an immovable on behalf of a corporation not yet formed (new § 1-203 retains the substance of old § 25.1). Act 328 does, however, effect some significant changes, several of which are discussed below.

News of Act 328 certainly will raise questions, and Louisiana lawyers should be prepared. Clients will call their lawyers asking: How does this affect my business? Forward-thinking lawyers are sure to ask themselves now: How does this affect my present and future clients who are and/or deal with Louisiana corporations?

Transition

How does Act 328 affect existing corporations? This question ranks among the first substantive questions likely posed to Louisiana lawyers, particularly considering the prevalence of limited liability companies as the preferred form for newly formed companies. New § 1-1701 provides the answer: "This Chapter applies to all domestic corporations in existence on its effective date that were incorporated under the laws of this state for a purpose or purposes for which a corporation might be formed under this Chapter." Importantly, new § 1-1703 provides a savings statute, listing instances under which the repeal of a statute effected by Act 328 does not affect past actions or events, including:

► "The operation of the statute or any action taken under it, before its repeal;"

► "Any ratification, right, remedy privilege, obligation, or liability acquired, accrued, or incurred under the statute, before its repeal;"

► "Any violation of the statute, or any penalty, forfeiture, or punishment incurred because of the violation, before its repeal" (provided that, if the new statute provides a lesser penalty or punishment, then the penalty or punishment will be reduced to the new penalty or punishment if the penalty or punishment was not already imposed); and

► "Any proceeding, reorganization, or dissolution commenced under the statute before its repeal, and the proceeding, reorganization, or dissolution may be completed in accordance with the statute as if it had not been repealed."

Unanimous Governance Agreements

Not only does Act 328 tell us how to treat existing corporations, the Act potentially contains the "Endangered Species Act" for business corporations. Act 328's new § 1-732 creates "Unanimous Governance Agreements (UGAs)," which may breathe new life into business corporations as a viable alternative to limited liability companies, or at least cause lawyers and businesses to pause and consider implementing an UGA in an existing corporation before conversion. In effect, UGAs allow private corporations to behave more like limited liability companies. The term "Unanimous Governance Agreement" is non-uniform, although the concept is contained in the MBCA.

UGAs, authorized by new § 1-732, are written agreements governing the exercise of corporate powers or management that "shall be interpreted with principles of freedom of contract, subject only to the limitations of public policy." The UGA must be approved in one or more writings signed by all persons who are shareholders at the time of the UGA. The UGA is enforceable even though it is inconsistent with legislation. The UGA may eliminate or limit the board of directors. The UGA may transfer all or part of the corporate power to one or more shareholders. Further, the UGA shall not be the basis of shareholder liability, and, if the UGA limits the powers of directors, it relieves the directors from liability. The UGA designation must be noted conspicuously on the share certificates. A UGA may have an initial term of 20 years and may be renewed for an additional 20 years. It is not clear whether the original term must expire before renewal. The UGA ceases if the corporation becomes public.

Director and Officer Exculpation

Under new § 1-832, director and officer exculpation is the default rule, with four exceptions. New § 1-832 provides: "Except to the extent that the articles of incorporation limit or reject the protection against liability provided by this Section, no director or officer shall be liable to the corporation or its shareholders for money damages for any action taken, or any failure to take action, as a director or officer . . . ." This default exculpation rule contains exceptions for breach of the duty of loyalty, intentional infliction of harm on the corporation or shareholders, unlawful distributions prescribed by new § 1-833 (unlawful distributions), and intentional violation of criminal law — all of which may not be limited, although insurance may be purchased against them. Note that new § 1-833's exceptions are non-uniform as the MBCA limits its exceptions to the extent of any improper benefit received by the director. Under new § 1-202, the articles of incorporation must make an express election of exculpation, choosing whether the corporation "accepts, rejects, or limits, with a statement of limitations, the protection against liability of directors and officers" established under new § 1-832.

"Self-Dealing" Transactions n/k/a "Director's Conflicting Interest Transactions"

Act 328 changes the law regarding "self-dealing" transactions. Special provisions now apply to "director's conflicting interest transactions," which new § 1-860 defines as a transaction with the corporation to which the director is a party or a transaction with the corporation of which the director had contemporaneous knowledge and in which the director (or a related person) had a material financial interest known to the director. "Related person" and "material financial interest" are also defined terms, among several others located in new § 1-143 and new § 1-860. Material relationship is broadly defined as a relationship which "would reasonably be expected to impair the objectivity of the director's judgment."

Vote of the shareholders or "qualified directors" on a "director's conflicting interest transaction" now has much greater effect. Under the old law, such votes merely prevented the transaction from being void ab initio. Under the new law, votes by the shareholders or "qualified directors," which comply with detailed statutory procedures, now insulate the director from liability under new § 1-861 and validate the transaction by deeming it effective under new § 1-862 ("qualified director" vote) and new § 1-863 (shareholder vote). In addition to votes by the shareholders or "qualified directors," new § 861(B)(3) also retains the traditional defense to director liability when the "transaction, judged according to the circumstances at the relevant time, is established to have been fair to the corporation."

Derivative Proceedings

Act 328 also made changes regarding derivative actions. Act 328 amended Article 611 of the Louisiana Code of Civil Procedure to exempt "derivative proceedings" from the procedures contained in Articles 591 through 617 of the Louisiana Code of Civil Procedure (*i.e.*, "Chapter 5. Class and Derivative Actions"): "If a derivative action is a 'derivative proceeding' as defined in the Business Corporation Act, the action is exempt from the provisions of this Chapter other than this Subsection, and is subject instead to the provisions of the Business Corporation Act concerning derivative proceedings." New § 1-740 defines "derivative proceeding" as "a civil suit in the right of a domestic corporation or, to the extent provided in R.S. 1-747, in the right of a foreign corporation." New §§ 1-740 through 1-747, therefore, establish specialized procedures for "derivative proceedings."

Prior shareholder demand, under new § 1-742, is one important new feature applicable to derivative proceedings. Under new § 1-742, the shareholder must make a written demand on the corporation to take suitable action, and 90 days must elapse before the shareholder may file suit (unless rejected sooner or irreparable harm would result). This new "absolute" or "universal" demand requirement is a departure from prior law — both the Delaware demand-futility rule announced in *Aronson v. Lewis*, 473 A.2d 805 (Del. 1984), and Louisiana's variation on it allowing demand to be excused as futile when the majority of the directors were named as defendants.

Other features of the Act 328 procedures pertaining to "derivative proceedings" include new § 1-741's standing requirement, requiring the plaintiff to be a shareholder at the time of the action or omission complained of or later through transfer by operation of law from one who was a shareholder at the time, which is similar to the requirement contained in existing Article 615 of the Louisiana Code of Civil Procedure. Under new § 1-742.1, which is a non-uniform provision retained from Article 615, the plaintiff must specifically allege compliance with new § 1-741's standing requirement, specifically allege compliance with new § 1-742's absolute demand requirement, join the corporation and obligor as defendants, pray for relief in favor of the corporation against the obligor, and include a verification by the plaintiff or plaintiff's counsel. New §§ 1-743 and 1-744 include a stay and early dismissal procedure, allowing the corporation defendant to commence an inquiry in which the majority vote of the qualified directors (or committee appointed by them) or a court-appointed panel may determine that the maintenance of a derivative proceeding is not in the best interest of the corporation, resulting in dismissal of the proceeding. A good faith inquiry ordinarily will require a written report prepared with the assistance of independent legal counsel, according to the 2014 Official Revision Comments.

The new derivative procedures also contain, in new § 1-746, a "loser pays" provision at the conclusion of the derivative proceeding. The court may order the corporation to pay the plaintiff's expenses if the proceeding has resulted in substantial benefit to the corporation. Conversely, the court may order the plaintiff to pay the defendant's expenses if the proceeding was commenced or maintained without reasonable cause or for an improper purpose.

Holding Annual Meetings

Also of interest to litigators, new § 1-701 makes a change to the procedures enforcing

annual meeting requirements. New § 1-701 legislates that corporations must hold annual meetings, unless directors are elected by written consent in lieu of an annual meeting (see new § 1-704). While the old law allowed a shareholder to call the meeting directly when the board failed to do so, new § 1-701(D) only permits the shareholder to demand that the secretary call the meeting:

> If no annual shareholders' meeting is held for a period of eighteen months, and directors are not elected by written consent in lieu of an annual meeting during that period, any shareholder may by notice to the secretary demand that the secretary call such a meeting, to be held at the corporation's principal office or, if none in this state, at its registered office. The secretary shall call the meeting and shall provide notice of the meeting as required by R.S. 12:1-705 within thirty days after the notice to the secretary of the shareholder's demand for the meeting.

If the secretary fails or refuses to call the meeting (which must be set between 10 and 60 days after the secretary's notice) as requested by the shareholder, a mandamus proceeding under Louisiana Code of Civil Procedure article 3864 provides the remedy, as explained in 2014 Official Revision Comment (c) to new § 1-701. In addition, new § 1-703 provides for court-ordered meetings in a summary proceeding upon application by a shareholder in two circumstances: (1) an annual meeting was not held (and no written consent action in lieu thereof) within the earlier of six months after the end of the corporation's fiscal year or fifteen months after its last annual meeting, or (2) the shareholder made an unsuccessful demand under new § 1-702 and either (a) notice of the meeting was not given within 30 days after demand or (b) the notice was given but the meeting was not held in accordance with the notice.

Majority Instead of Supermajority Voting on Fundamental Issues as New Default Rule

Act 328 also lessens the supermajority required under the old law for certain fundamental transactions. Previously, a two-thirds vote was required for actions such as amendments to the articles of incorporation (old § 31(B)) and mergers (old § 112(C)(2)). New § 1-727 allows the articles to require greater quorum or voting requirements, but the default rule allows action by a majority vote. New § 1-1003(A)(3) provides for amendment of the articles by majority vote. Note also that new § 1-1005 allows amendment to the articles of incorporation in certain enumerated respects, including deleting the names and addresses of the initial directors and amending the articles to conform to the corporation's secretary of state filings with respect to its registered agent and principal office. New § 1-1104(E) permits merger (or share exchange) by majority vote, provided the board complies with detailed requirements for submitting a merger plan to the shareholders. Relatedly, new § 1-1302 generally enhances the rights of dissenting shareholders, providing for fair value appraisal rights without minority discounts, although appraisal rights are the exclusive remedy in some circumstances.

No Remote Attendance for Shareholders?

Notwithstanding its apparent progressive purpose of modernization, Act 328 did not adopt MBCA's Section 1-708, which would permit the board to implement procedures allowing shareholders to participate in shareholder meetings remotely: "Shareholders of any class or series may participate in any meeting of shareholders by means of remote communication to the extent the board of directors authorizes such participation for such class or series." Why not afford shareholders the modern convenience of participating in shareholder meetings remotely?

Dive In or Wade In?

Space limitations prevent identification of every change effected by Act 328. The text of Act 328 spans almost 300 pages. There are many other specific changes, such as the time for reserving a corporate name, issuance of shares for a promissory note, the minimum number of directors required, required officers, electronic shareholder proxies, and elimination of the higher inspection rights percentage requirement for business competitors. Louisiana lawyers should dive into the text of Act 328 to educate themselves so they may embrace the questions sure to arise in the wake of Act 328 — or at least wade in far enough to determine that the best course is a referral to those who did dive in.

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