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PROPOSALS FOR REFORM

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MICHIGAN CLOSE CORPORATION LAW:

PROPOSALS FOR REFORM

George J. Siedel*

A close corporation is a corporation whose shares are not traded publicly. Close corporations play a vital role in the American economy, as "the vast majority of business corporations are closely-held."¹ Some close corporations are large, well-established businesses in both the manufacturing (for example, Steelcase, The Stroh Brewery) and service (Domino's Pizza) sectors. Most close corporations, however, are relatively small enterprises,² although they have a major impact on employment, sales, and new product development.³

Given their importance, state law should be designed to recognize and accommodate the special needs of close corporations, thus serving to spur, rather than impede, business growth. This is often a difficult goal because a close corporation combines certain characteristics of both the partnership and the publicly-held corporation. Shareholders in a close corporation, like general partners, need flexibility in order to meet their particular business and personal needs. For example, shareholders may operate the business under a shareholders' agreement which is similar to a partnership agreement, restrict transferability of shares, and, in certain circumstances, elect to be taxed like a partnership. However, as in a public corporation, the liability of shareholders in a close corporation is limited to their investment in the business.

In dealing with the unique features of a close corporation, state corporation laws appear in two distinct formats. Some states have what are called integrated statutes, where the close corporation provisions are found in a separate chapter in the business corporation statute. Most states, however, do not use the integrated approach; instead close corporation provisions are spread throughout the business corporation statute. An example of a non-integrated statute, the Michigan corporation law contains (in the words of a leading authority on close corporations) "numerous well-drafted provisions designed to cope with close corporation problems...."⁴

On June 26, 1982,⁵ the American Bar Association's Committee on Corporate Laws adopted the Model Statutory Close Corporation Supplement (the "Supplement") which uses the integrated format. An introductory comment to a preliminary draft of the Supplement states that: "The main purpose of the Supplement is to provide model legislation for those states that wish to enact special provisions that incorporate the best available ideas on the special needs of close corporation shareholders and that at the same time provide basic statutory protection to the shareholders even in situations where they are not represented by experienced corporate counsel."⁶ Section 2(a) of the Supplement provides that a state's general corporation law also applies to close corporations, to the extent that it is not inconsistent with the Supplement.

The purpose of this article is twofold. First, an overview of Michigan close corporation law will be provided. Because Michigan does not use the integrated approach, close corporation provisions are often difficult to locate and might be overlooked in practice. Second, the article will discuss features in Michigan close corporation law that might be improved in light of the Supplement

I. MICHIGAN CLOSE CORPORATION LAW

The Michigan Business Corporation Act (the "Act") provides that it "shall be liberally construed and applied to promote its underlying purposes and policies which include [giving] special recognition to the legitimate needs of close corporations."⁷ Although most of the close corporation provisions are available to all corporations, they are especially significant for smaller corporations with a limited number of shareholders.

A. Forming the Corporation

The procedure for establishing a corporation under the Act is not complicated. Only one person is needed to act as incorporator.⁸ Under the Act's definition of "person," partnerships, corporations, and other entities,⁹ as well as individuals, may create a corporation by executing and filing the articles of incorporation.¹⁰

The articles of incorporation and the bylaws, along with shareholder voting and control agreements,¹¹ furnish the chief mechanisms for adapting the corporate form to the specific needs of a close corporation.¹² Although the

articles of incorporation need contain only a minimal number of mandatory provisions,¹³ they may specify optional provisions so long as these provisions are consistent with the Act and other state laws governing the management or powers of the corporation, the directors, and the shareholders. Optional provisions in the articles often include variations in voting power such as greater than majority and class voting requirements, control agreements (for example, limitations on board discretion over dividend policy), share transfer restrictions, authorization of action without a shareholder meeting, and preemptive rights. Additionally, the incorporators or the shareholders may choose to place provisions which are usually in the bylaws in the articles instead, thereby restricting amendment.¹⁴

The bylaws are useful as a planning device in that a close corporation may tailor them (for example, the provisions dealing with duties and powers of the officers) to the skills and personalities of the shareholders who participate in the business.¹⁵ In Michigan the bylaws, like the articles, may be used to regulate and limit board discretion.¹⁶ The bylaws may prescribe that only the shareholders may alter or repeal bylaws made by them.¹⁷ Bylaw provisions may also be used to vary voting power. A Michigan court may, however, invalidate a bylaw on the ground that it is unreasonable.¹⁸

B. Financial Structure

Under the Act, authorized shares may be divided into classes and any class of shares may be further divided into and issued in series, with the articles authorizing the board to set the terms of each series.¹⁹ Although perhaps used more by public corporations, this power may be valuable to small corporations. For example, the articles may authorize a single class of preferred stock and allow the board to establish various series within that class carrying different dividend rates to ensure availability of capital as market conditions change.²⁰

The Michigan Act is novel in permitting both future services and future payment to be adequate consideration for current issuance of shares.²¹ The Act also allows considerable flexibility in permitting a corporation's redemption of its own shares--an important consideration in close corporations, where redemption provides an alternative to buy-sell agreements.²²

C. Shareholder Rights

The key to close corporation planning is the relationship between shareholder rights and corporate governance. The Michigan Act validates a number of devices often used by close corporations to meet the needs of its shareholders. First, provision is made for informal shareholder action. Close corporations, especially family-operated corporations, frequently ignore operational formalities. To insure the validity of such informal arrangements, non-unanimous shareholder action may be taken without a meeting, prior notice, or a vote - if written consents to the action are obtained from shareholders.²³ The consents must set forth the action taken and they must be signed by a sufficient number of shareholders to exceed the minimum number of votes that would be necessary to authorize the action at a meeting at which all the voting shares are present. Even without such a provision in the articles, unanimous written consent without a meeting or prior notice is permitted by the Act.²⁴

Second, several provisions relate to shareholder meetings. Attendance at a shareholder meeting constitutes waiver of notice unless the shareholder attends only to object, at the outset of the meeting, to the conduct of business.²⁵ A requirement of lesser or greater than majority shareholder attendance to constitute a quorum may be imposed by the articles or bylaws.²⁶ The articles may also impose a greater than majority voting requirement for any action.²⁷ If so, an amendment to the articles to change or delete the super-majority requirement must itself be adopted by no less than the vote required by the provision to be amended.²⁸ If the incorporators or shareholders so desire, the articles may provide for cumulative voting in the election of directors; the Act's presumption, however, is against cumulative voting.²⁹

Third, the Act has a liberal provision for voting agreements between two or more shareholders.³⁰ Among other things, voting agreements generally may commit the parties to vote their shares for specified persons as directors, or to vote as a majority of the shares in the agreement pool may decide or as an arbitrator may direct in the event of a disagreement.³¹ Voting agreements may also give certain shareholders voting power which is disproportionate to their actual holdings of voting shares, a device which may be needed in a close corporation in which key shareholders own relatively little voting stock.

Unlike many jurisdictions,³² Michigan does not limit the duration of voting agreements. Although voting agreements are probably specifically enforceable, it would be wise to assure compliance by means of irrevocable proxies executed pursuant to the Act, as a court may not imply the existence of irrevocable proxies should a controversy arise.³³

The flexibility of voting agreements generally makes their use preferable to the more cumbersome and rigid voting trust device. If used, a voting trust may be created for a term of 10 years, renewable within 12 months before its expiration.³⁴ A principle drawback of the voting trust is that upon expiration of the 10-year period, the voting trust is not binding on any shareholder who refuses to consent to an extension.

Fourth, the Act validates shareholder control agreements³⁵ - perhaps the single most important provision specifically drafted for close corporations. The Act permits a corporation to operate without a board of directors in what amounts to an incorporated partnership. Coupled with the rules for establishing the role of the board of directors,³⁶ the Act also assures the validity of agreements which substantially limit the discretion of the board to manage the corporation. Control agreements may be used to designate the officers of the corporation, name other key employees, fix salaries, and specify conditions under which dividends may be paid.³⁷

Unlike simple voting agreements, shareholder control agreements must either be adopted by all the incorporators and placed in the original articles or authorized by all shareholders in an amendment to the articles.³⁸ Control agreements terminate automatically if the close corporation's shares are listed on a national exchange or regularly quoted in an over-the-counter market.³⁹ Termination is also automatic if shares are transferred to a person who takes delivery without notice of the control agreement; existence of a control agreement must be conspicuously noted on the face of all corporate share certificates.⁴⁰ To the extent the control agreement limits the discretion of the directors, the directors' usual liability is imposed instead on the shareholders.⁴¹ In drafting control agreements, the corporation's attorney may wish to include a remedial provision to take effect when any occurrence terminating the control agreement takes place.⁴²

Fifth, a shareholder agreement, the articles, or the bylaws may impose restrictions on the transfer of shares.⁴³ Such restrictions should be noted

on the stock certificates.⁴⁴ The Act expressly validates the most common forms of transfer restrictions: (a) first option to the corporation or other holders; (b) buy-out obligations; (c) consent requirements; (d) prohibitions on transfers to designated persons or classes of persons; and (e) restraints for the purpose of preserving S corporation status.⁴⁵

Finally, close corporation shareholders may prefer to establish preemptive rights as a means of protecting their proportional holdings and voting power. Preemptive rights may be established in the articles or by a shareholder agreement under the Michigan Act.⁴⁶

D. Management Structure

As noted above, elimination of the board is one of the control devices available under the Act. If the board of directors is not eliminated, the Act provides that the board may consist of one or more members.⁴⁷ The classification of directors, another control device permitted by the Act, allows the election of directors to terms of a maximum of three years.⁴⁸ The Act sets no minimum size for a classified board; a classified board may consist of two or three members with one director in each class. Yet another permissible control device is a provision in the articles that one or more directors shall be elected exclusively by the shareholders of one class or series.⁴⁹

The Michigan Act presumes that a majority of the directors currently in office constitutes a quorum for transaction of business and that a majority vote of members present at a meeting having a quorum present is sufficient for approval of an action.⁵⁰ These rules may be changed in the articles or by-laws, increasing or decreasing quorum requirements, and increasing (but not decreasing) the number of votes required to approve an action. Unless the articles or bylaws provide otherwise, the board may act without a meeting if the directors give unanimous written consent.⁵¹

Theoretically, a close corporation might operate with a single individual holding all of the required officer positions. Practically, a corporation must have two officers, since the Act requires two official signatures on stock certificates,⁵² and banks will normally require two signatures in executing documents.⁵³

If the board's power to elect officers is removed (or if there is no board), arrangements for election of officers should be covered in the shareholder control agreement in order to assure the validity of election procedures.⁵⁴

E. Amendment to Articles; Fundamental Changes

The chapter in the Michigan Act on amending the articles of incorporation is useful because many of the control devices employed by close corporations may be contained in the articles. Shareholders may vote as a class on a proposed amendment, even when they hold nonvoting stock, if the amendment would have an adverse effect on the class.⁵⁵ Class voting may also be used as a protective device written into the articles of incorporation.⁵⁶

A holder of "adversely affected" shares who does not vote for an amendment may dissent and demand payment for the shares if the amendment: (a) materially alters or abolishes a preferential right, or (b) creates, alters or abolishes a material provision or right in respect of the redemption of such shares.⁵⁷ Thus, the category of amendments which triggers this right is more narrowly defined than the category entitling holders to a class vote.⁵⁸ A dissenting shareholder is entitled to receive payment no greater than the amount payable on redemption of the shares or liquidation of the corporation, whichever is less.⁵⁹

Although mergers, consolidations, and sales of assets outside the usual course of business may normally be approved by simple majority of the outstanding shares,⁶⁰ the articles may require a higher vote -- an important protection for minority shareholders. And even when a simple majority can approve such a fundamental change, the appraisal remedy is available to dissenting shareholders.⁶¹ A typical effect of the appraisal right is to force a compromise between the majority who desire a fundamental change in the corporation and dissenters who refuse to be forced into a position different from that bargained for when the stock was purchased.

F. Dissolution and Alternative Remedies

Dissolution may occur voluntarily or by court order. Voluntary dissolution often results when conditions set forth in the articles of incorporation are met.⁶² The value of allowing dissolution at will or upon the occurrence of a specified event can be great for close corporations.

Shareholders' or directors' deaths, retirement, and deadlocks will cause considerable difficulty for close corporations; yet standards for judicial intervention in many states are so stringent that courts will seldom grant a remedy. Even when the relevant standard is met, a petition for judicial dissolution or other remedy may result in lengthy proceedings, and the legal fees may be beyond the company's financial capability. Advance agreement on dissolution-causing events can avoid these problems, although these advantages must be weighed against other potential problems, such as potential abuse of the device by shareholders.⁶³ The Michigan Act is quite valuable to a close corporation wishing to operate as a quasi-partnership, because an individual shareholder may be able to rely on an agreement specifying the conditions triggering dissolution as a deterrent to directors or controlling shareholders acting against the minority shareholder's interest.

Further protection from deadlock and oppression is afforded by the Michigan Act's lenient standard for dissolution by court order.⁶⁴ A court is empowered to dissolve the enterprise even though the deadlocked corporation is operating at a profit.⁶⁵ Furthermore, if the directors or shareholders are so divided that they have been unable to elect successors to directors whose terms have expired, dissolution may be ordered. This is a major departure from the approach used elsewhere in which courts have refused to intervene and dissolve the corporation unless insolvency is imminent.

The Act also provides that a court may use equitable remedies in the event a shareholder can show that "the acts of the directors or those in control of the corporation are illegal, fraudulent or wilfully unfair and oppressive to the corporation or to such shareholder."⁶⁶ In such a situation, the court may decree either dissolution of the corporation or utilize less drastic remedies, including changes in the articles or bylaws, cancellation of or injunction against a resolution or other act of the corporation, and prohibition or direction of an act of the corporation or other parties.⁶⁷ The court may also direct that the corporation or the individuals responsible for the wrongful acts purchase shares at a fair price.⁶⁸

Although dissolution is still considered to be a drastic remedy, equitable remedies provided by statute give the courts great flexibility in fashioning relief appropriate to the particular situation. Previously, courts were reluctant to intervene except to dissolve, considering dissolution to be

an extreme remedy to be used only as a last resort.⁶⁹ Under the Act, other equitable relief may be used when the circumstances warrant a remedy short of dissolution.⁷⁰ For example, in Moore v. Carney⁷¹ the corporation was ordered to purchase the plaintiff's stock interests, thereby preventing dissolution. This decision follows the spirit of the statute in its alternative resolution of a conflict in which the court formerly would have intervened only to order dissolution. In Barnett v. International Tennis Corp.,⁷² however, the court ignored the alternative relief made expressly available by statute. The court determined that the situation was not so grave as to warrant dissolution and refused to grant relief.

II. LAW REFORM

Michigan close corporation law, on the whole, compares very favorably with the Supplement.⁷³ There is, however, room for improvement in six areas.

A. Transfer of Shares in Breach of Transfer Restrictions

Section 10 of the Supplement requires that all stock certificates carry a notice which states:

The rights of shareholders in a statutory close corporation may differ materially from the rights of shareholders in other corporations. Copies of the articles of incorporation and bylaws, shareholders' agreements, or other documents, which may restrict transfers and affect voting and other rights, may be obtained by a shareholder on written request to the corporation.

Section 13 of the Supplement provides that attempted transfers in violation of restrictions which are binding on transferees shall be ineffective. If a transfer in violation of a restriction not binding on a transferee (due either to lack of notice or invalidity of the restriction in question) is attempted, the corporation has the option, upon notice given within 30 days of presentment of the shares for registration, to purchase the shares from the transferee at the same price and terms agreed to by the transferee.

Michigan corporation law does not contain the remedies available in the Supplement, although if transfer restrictions are violated the corporation might have the power to rescind a transfer or remaining shareholders might have a cause of action for damages against the transferor. It is unlikely, however, that even these remedies would be available in cases where the

transfer restriction is held invalid, a situation in which the Supplement provides the thirty-day option to acquire the shares.

B. Bylaws

Section 22 of the Supplement provides that "[a] statutory close corporation need not adopt bylaws if provisions required by law to be continued in bylaws are contained in either articles of incorporation or a shareholder agreement"⁷⁴ The Supplement forgoes a bylaw requirement in an attempt to recognize the fact that many close corporations choose to operate in a manner similar to that of a partnership. Furthermore, the Supplement recognizes that "business corporation statutes universally require that a corporation adopt bylaws."⁷⁵ However, the commentators note that the statutes specify very few provisions that must be included in the bylaws.⁷⁶

Whether Michigan requires bylaws is unclear. The Act provides that "[t]he articles of incorporation may contain any provision not inconsistent with this act or any other statute of this state ... including any provision which under this act is required or permitted to be set forth in the bylaws."⁷⁷ The Act allows provisions otherwise required to be included in the bylaws also to be included in the articles of incorporation. However, it does clearly state that the articles of incorporation may serve as a substitute for bylaws.⁷⁸

The Act should be amended to provide that bylaws are not required. As the comment to section 22 of the Supplement suggests, in a close corporation where investors are active in the business, a shareholders' agreement often includes the information normally contained in the bylaws. Requiring bylaws involves unnecessary duplication and a formalism that may be burdensome in close corporations, which are typically operated on a more informal basis than larger companies.⁷⁹

C. Annual Meeting

Section 23 of the Supplement authorizes a close corporation to establish a date at which an annual meeting may be held, by way of articles of incorporation, bylaws, or shareholder agreements as authorized by section 20.⁸⁰ If no annual meeting date is so established, the date shall be the first business day after May 31.⁸¹ However, unless a contrary provision is made in the articles of incorporation, no annual meeting need be held unless a

written request is delivered to the corporation by a shareholder, thirty or more days prior to the established meeting date.⁸²

The Michigan statute provides: "An annual meeting of shareholders for election of directors and for such other business as may come before the meeting shall be held at a time as provided in the bylaws, unless such action is taken by written consent as provided in section 407."⁸³ If the corporation elects to operate without a board of directors, there would be little reason to hold an annual meeting unless "other business" arises which requires an annual meeting. Additionally, Michigan allows a corporation to take action without a meeting, provided that written consent of a sufficient number of shareholders to authorize such action is obtained.⁸⁴

The Act's "requirement" of an annual meeting provides that "[f]ailure to hold the annual meeting at the designated time ... does not affect otherwise valid corporate acts or work a forfeiture or give cause for dissolution ..."⁸⁵ Therefore, there is no immediate penalty for failure to hold an annual meeting. The Act does provide that the circuit court may summarily order that a meeting be held upon the application of a shareholder. The prerequisites for compelling a shareholder's meeting under the Act are the passage of ninety days after the date designated for the annual meeting, or fifteen months after organization of the corporation or the holding of the last annual meeting.⁸⁶

It appears that Michigan does not require an annual meeting, unless a shareholder wishes to compel one. However, in failing to make clear that an annual meeting is not necessary, Michigan law does not expressly recognize the special situation of close corporations, i.e., often operating as incorporated partnerships. Rather, one must "read around" the statute to reach the result expressly authorized by the Supplement. Despite statutory provisions to the contrary, the failure to hold meetings could be raised in an attempt to pierce the corporate veil. The Supplement reduces unnecessary corporate formality without endangering the separate identity of the corporation.

D. Shareholder Sale Option at Death

Sections 14 through 17 of the Supplement authorize a compulsory buy-out upon the death of a shareholder. If the articles of incorporation so provide, an executor or administrator is given the right to require the corporation either to redeem all (but not less than all) of the decedent's shares, or be

dissolved.⁸⁷ The buy-out provisions authorized by section 14 can be modified by two-thirds vote of all shares,⁸⁸ and a shareholder who votes against alteration of buy-out rights has the right to obtain the fair value of his shares.⁸⁹ Sections 15 through 17 set forth in detail the procedure by which the buy-out option is exercised.

Michigan law includes no provision analogous to sections 14 through 17 of the Supplement. However, a Michigan close corporation is free to adopt a buy-out provision similar to that provided in the Supplement.⁹⁰

The difference between the Supplement on the one hand, and the Michigan statute on the other, is the specific tailoring of the Supplement to the assumed needs of a "typical" close corporation. The Supplement establishes a procedure which may be adopted by the incorporators through reference in the articles of incorporation.⁹¹ Additionally, the Supplement's procedure is easily modified to fit the needs of a particular close corporation. The articles of incorporation need only state that sections 14 through 17 of the Supplement have been adopted with changes as specified in the articles.⁹² Michigan, however, requires that the incorporators draft and adopt a buy-out provision. While the procedure specified in the Supplement would be valid in Michigan, it is clearly more difficult for a close corporation to provide for such a buy-out. In Michigan detailed language must be drafted and formally adopted.

Given the importance of liquidity for the shares of a decedent and the potential for litigation resulting from liquidity problems, the Supplement is preferable. It provides both protection to shareholders who have no buy-out agreement and the basis for an agreement when one is desirable. Incorporators and their attorneys must recognize, however, that business and personal considerations, such as tax implications,⁹³ vary among close corporations. Consequently, wholesale adoption of a statutory buy-out provision should never supplant careful negotiation and planning when a business is formed.

E. Limited Liability

Section 25 of the Supplement states: "The failure of a statutory close corporation to observe the usual corporate formalities or requirements relating to the exercise of its corporate powers or the management of its business and affairs shall not be grounds for imposing personal liability on

the shareholders for liabilities of the corporation."⁹⁴ The comment to this section notes that its purpose is to make certain that, even if the shareholders elect to operate the close corporation like a partnership, it is still a legally constituted corporation with the limited liability attendant to such entities.⁹⁵

Michigan has no provision similar to section 25. On one hand, it can be argued that such a provision is unnecessary because Michigan does not provide for statutory close corporations and a close corporation that adheres to the requirements of the Act presumably would not be in danger of having its corporate veil pierced. On the other hand, a Michigan corporation may operate without a board of directors (or might be subject to a management agreement which limits the board's discretion) and may elect to give shareholders the right to dissolve the corporation at will or upon the occurrence of specified events. While these features should not cause a court to pierce the corporate veil, a provision similar to section 25 would certainly do no harm.

F. Execution of Documents

Section 24 of the Supplement permits a person who holds more than one office in a statutory close corporation to execute, acknowledge, or verify any instrument in more than one capacity. Such authority is given even if the instrument is required by law to be officially signed by two or more different corporate officers.⁹⁶ This section is particularly useful in helping one-person corporations avoid filing formalities.

Although the Michigan Act permits one person to hold two or more offices, unlike the Supplement it does not allow a person to execute documents in more than one official capacity.⁹⁷ The Act also requires two official signatures when stock certificates are issued⁹⁸ and the articles may similarly require dual signatures.⁹⁹ Such an approach is unduly restrictive in close corporations where, as is often the case, there is only one shareholder or officer.

III. CONCLUSION

Four questions are especially relevant in evaluating a close corporation law:¹⁰⁰ (1) Is the law flexible in allowing corporations to vary usual corporate rules to meet special needs of shareholders? (2) Does the law minimize legal formalities? (3) Are minority shareholders protected from

oppression? (4) Should close corporation provisions be adopted in a separate chapter or included among the provisions of the general corporation act?

In Michigan, the first three questions can be answered affirmatively, especially when Michigan close corporation law is compared with the Supplement or with the law in states that have adopted the integrated format, such as Delaware.¹⁰¹ Michigan law can be improved, however, by adoption of the recommendations discussed in this article:

1. Remedies available when stock is transferred in violation of share transfer restrictions should be specified.
2. The Act state should state clearly that bylaws and annual meetings are not required.
3. Buy-out provisions that may be elected at the option of the corporation should be indicated in the Act.
4. The Act should include a limited liability provision applicable to all corporations.
5. One person should be permitted to execute documents in more than one official capacity.

Even if Michigan law is substantively sound, however, should Michigan adopt the integrated approach? On the surface, the integrated approach with its concentration on close corporations contained in one chapter is appealing because it appears to be easier to use. In fact, however, the opposite is true for the reason that provisions in a general corporation act may also apply to close corporations. Consequently, the integrated approach requires constant comparison of general corporation provisions with provisions in the close corporation chapter. The drafters of the Supplement recognized this problem:

One of the chief criticisms leveled at the existing integrated close corporation statutes is that they are so cumbersome lawyers are afraid to use them. To a large extent, the statutory framework for close corporations will inevitably be somewhat complex because the provisions must be drafted around the existing corporate statutes and case law.¹⁰²

In terms of complexity, then, the statutory format of the Michigan Act is preferable to the other approaches. However, one question remains. Is the

complexity of the integrated approach justified by the need for special statutory provisions relating only to close corporations? The preceding analysis indicates that, while selected close corporation provisions are at times beneficial, there is no reason why they cannot be incorporated into a general corporation act.

NOTES

- * Professor of Business Law, The University of Michigan, School of Business Administration. This article has been adapted, with permission, from Siedel, Close Corporation Law: Michigan, Delaware and the Model Act, 11 DEL. J. CORP. L. 383 (1986). Copies of this article may be obtained without charge from Dr. Edwin Miller, Division of Research, School of Business Administration, The University of Michigan, Ann Arbor, MI 48109. I am indebted to Thomas M. Skelly, Jane P. Wilson and M. Scott Wilson for their valuable research assistance. I also wish to thank Charles W. Borgsdorf and Paul A. Ward, both of whom practice corporation law in Michigan, for their review of the Delaware Journal manuscript and suggestions. This research was supported by a grant from the Independent Business Research Office of Michigan.
1. H. HENN & J. ALEXANDER, LAWS OF CORPORATIONS AND OTHER BUSINESS ENT. §257, at 695 (1983).
 2. Id.
 3. "Small business now employs about half of our private work force contributes 42 percent of sales and generates about 30 percent of the gross national product.... And small firms may produce close to 24 times more innovations per research and development dollar than large firms." America's Independents, MANAGEMENT FOCUS, Sept.-Oct. 1984, at 5.
 4. 1 F. O'NEAL, CLOSE CORPORATIONS §1.14b (2d ed. Supp. 1985).
 5. See Report of the Committee on Corporate Laws; Change in the Model Business Corporation Act, 38 BUS. LAW. 1031 (1983).
 6. Report of ABA Committee on Corporate Law, Proposed Statutory Close Corporation Supplement to the Model Business Corporation Act, 37 BUS. LAW. 269, 271 (1981) [hereinafter cited as ABA Report].
 7. Mich. Comp. Laws Ann. §450.1103 (West 1973)(Mich. Stat. Ann. §21.200(103)(Callaghan 1983)).
 8. Id. §450.1201 (Mich. Stat. Ann. §21.200(201)(Callaghan 1983)).
 9. Id. §450.1108(2) (Mich. Stat. Ann. §21.200(108)(Callaghan 1983)).
 10. Id. §450.1201 (Mich. Stat. Ann. §21.200(201)(Callaghan 1983)).
 11. Id. §§450.1461, 450.1463 (Mich. Stat. Ann. §§21.200(461), 21.200(463)(Callaghan 1983)).
 12. Although the term "close corporation" is defined in a variety of ways by various commentators and authorities, for purposes of discussing the Michigan Act a relatively simple and broad definition will suffice: "'close corporation' means a corporation whose shares are not generally traded in the securities markets." 1 F. O'NEAL, CLOSE CORPORATIONS §1.02 (2d ed. 1971); see also Mich. Comp. Laws Ann. §450.1463 (West 1973) (Mich. Stat. Ann. §21.200(463)(Callaghan 1983)).

13. The mandatory provisions are: corporate name, corporate purposes, number of authorized shares, division of shares into classes and series, address of the corporation's initial registered office, name of the corporation's initial resident agent, and the names and addresses of the incorporators. Mich. Comp. Laws Ann. §450.1202 (West 1973)(Mich. Stat. Ann. §21.200 (202)(Callaghan 1983)).
14. Most matters of internal management and operation, however, should be covered in the bylaws, as these matters might have to be amended quickly. 1 F. O'NEAL, CLOSE CORPORATIONS §3.79 (2d ed. 1971).
15. 1 F. O'NEAL, CLOSE CORPORATIONS §3.73 (2d ed. 1971).
16. Mich. Comp. Laws Ann. §450.1231 (West 1973)(Mich. Stat. Ann. §21.200(231)(Callaghan 1983)).
17. Id.
18. See Dozier v. Automobile Club of Michigan, 69 Mich. App. 114, 244 N.W.2d 376 (1976).
19. Mich. Comp. Laws Ann. §§450.1301, 450.1302 (West 1973)(Mich. Stat. Ann. §§21.200(301), 21.200(302) (Callaghan 1983)).
20. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §3.03 (1979).
21. Mich. Comp. Laws Ann. §450.1315 (West 1973)(Mich. Stat. Ann. §21.200(315)(Callaghan 1983)). A 1984 revision of the Model Business Corporation Act now permits an arrangement wherein the corporation may place shares issued for a contract for future services or a promissory note in escrow until the services are performed or the note is paid. Rev. Model Business Corp. Act §6.21(e)(1985).
22. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §3.14 (1979).
23. Mich. Comp. Laws Ann. §450.1407(1) (West 1973)(Mich. Stat. Ann. §21.200(407)(1) (Callaghan 1983)).
24. Id. §450.1407(3) (Mich. Stat. Ann. §21.200(407)(3) (Callaghan 1983)).
25. Id. §450.1404(3) (Mich Stat. Ann. §21.200(404)(3) (Callaghan 1983)).
26. Id. §450.1415(1) (Mich. Stat. Ann. §21.200(415)(1) (Callaghan 1983)). This section also provides that, once quorum requirements have been met, a meeting may continue despite the withdrawal of enough shareholders to leave less than a quorum.
27. Id. §450.1455 (Mich. Stat. Ann. §21.200(455)(Callaghan 1983)).
28. Id.
29. Id. §450.1451 (Mich. Stat. Ann. §21.200 (451)(Callaghan 1983)).
30. Id. §450.1461 (Mich. Stat. Ann. §21.200(461)(Callaghan 1983)).

31. 1 F. O'NEAL, CLOSE CORPORATIONS §5.12 (2d ed. 1971).
32. See, e.g., Del. Code Ann. tit. 8, §218(c)(1983).
33. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §4.14 (1979). Proxies are valid for three years unless they provide otherwise. Mich. Comp. Laws Ann. §450.1421 (West 1973)(Mich. Stat. Ann. §21.200(421)(Callaghan 1983)).
34. Mich. Comp. Laws Ann. §§450.1466, 450.1468 (West 1973)(Mich. Stat. Ann. §§21.200(466), 21.200(468)(Callaghan 1983)).
35. Id. §450.1463 (Mich. Stat. Ann. §21.200(463)(Callaghan 1983)).
36. Id. §450.1501 (Mich. Stat. Ann. §21.200(501)(Callaghan Supp. 1985)).
37. 1 F. O'NEAL, CLOSE CORPORATIONS §5.02 (2d ed. 1971).
38. Mich. Comp. Laws Ann. §450.1463(1) (West Supp. 1985)(Mich. Stat. Ann. §21.200(463)(1)(Callaghan 1983)).
39. Id. §450.1463(2)(b)(Mich. Stat. Ann. §21.200(463)(2)(b)(Callaghan 1983)).
40. Id. §450.1463(2)(a),(4)(Mich. Stat. Ann. §21.200(463)(2)(a),(4)(Callaghan 1983)).
41. Id. §450.1463(3) (Mich. Stat. Ann. §21.200(463)(3)(Callaghan 1983)). Under Michigan law, the corporate director is charged with a duty of good faith and with a duty of diligence, care and skill which an ordinarily prudent person would exercise under similar circumstances in a like position. See Mich. Comp. Laws Ann. §450.1541. In the event an agreement is used these duties are transferred to the shareholders in their capacity as shareholders.
42. Compare with Del. Code Ann. tit. 8, §348 (1983)(describing a 30 day grace period during which the terminating occurrence might be reversed or corrected without a loss of close corporation status).
43. Mich. Comp. Laws Ann. §450.1472(1) (West 1973)(Mich. Stat. Ann. §21.200(472)(1)(Callaghan 1983)).
44. Id. §450.1472(2)(Mich. Stat. Ann. §21.200(472)(2)(Callaghan 1983)).
45. Id. §450.1473 (Mich. Stat. Ann. §21.200(473)(Callaghan 1983)).
46. Id. §450.1481(1) (Mich. Stat. Ann. §21.200(481)(1)(Callaghan 1983)).
47. Id. §450.1505(1) (Mich. Stat. Ann. §21.200(505)(1) (Callaghan (1983))).
48. Id. §450.1506(1) (Mich. Stat. Ann. §21.200(506)(1)(Callaghan (1983))).
49. Id. §450.1506(2) (Mich. Stat. Ann. §21.200(506)(2)(Callaghan 1983)).

50. Id. §450.1523 (Mich. Stat. Ann. §21.200(523)(Callaghan 1983)).
51. Id. §450.1525 (Mich. Stat. Ann. §21.200(525)(Callaghan 1983)).
52. Id. §450.1331 (Mich. Stat. Ann. §21.200(331)(Callaghan 1983)).
53. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §5.07 (1979).
54. Id.
55. Mich. Comp. Laws Ann. §450.1615(1) (West 1973)(Mich. Stat. Ann. §21.200(615)(1)(Callaghan 1983)).
56. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §6.05 (1979).
57. Mich. Comp. Laws Ann. §450.1621 (West 1973)(Mich. Stat. Ann. §21.200(621)(Callaghan 1983)).
58. Id. §450.1615 (Mich. Stat. Ann. §21.200(615)(Callaghan 1983)).
59. Id. §450.1621(2) (Mich. Stat. Ann. §21.200(621)(2)(Callaghan 1983)).
60. Id. §§450.1703(2), 450.1753(4) (Mich. Stat. Ann. §§21.200(703)(2), 21.200(753)(4)(Callaghan 1983)).
61. Id. §450.1768(1) (Mich. Stat. Ann. §21.200 (768)(1)(Callaghan 1983)).
The procedure for appraisal is covered by Mich. Comp. Laws Ann. §§450.1761-771 (West 1973)(Mich. Stat. Ann. §§21.200(761-771)(Callaghan 1983)).
62. Id. §450.1805 (Mich. Stat. Ann. §21.200(805)(Callaghan 1983)).
63. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §8.03 (1979).
64. Mich. Comp. Laws Ann. §450.1823 (West 1973) (Mich. Stat. Ann. §21.200(823)(Callaghan 1983)).
65. Cf. Salvador v. Connor, 87 Mich. App. 664, 276 N.W.2d 458 (1978)(leave to appeal denied, 406 Mich. 966 (1979)).
66. Mich. Comp. Laws Ann. §450.1825 (West 1973) (Mich. Stat. Ann. §21.200(825)(Callaghan 1983)).
67. Id.
68. Id.
69. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §8.06 (1979); see also Stott Realty v. Orloff, 262 Mich. 375, 247 N.W. 698 (1933).
70. S. SIEGEL, MICHIGAN BUSINESS CORPORATIONS §8.06 (1979).

71. CA No. 203-179 R (Wayne County Cir. Ct., May 23, 1975), aff'd on other grounds 84 Mich. App. 399, 269 N.W.2d 614 (1978).
72. 80 Mich. App. 396, 263 N.W.2d 908 (1978).
73. Siedel, Close Corporation Law: Michigan, Delaware and the Model Act, 11 DEL. J. CORP. L. 383 (1986).
74. Model Stat. Close Corp. Supp. §22.
75. Id. §22, official comment.
76. Id.
77. Mich. Comp. Laws § 450.1209 (West 1973) (Mich. Stat. Ann. §21.200(209) (Callaghan 1983)).
78. Id. § 450.1231 (Mich. Stat. Ann. §21.200(231)(Callaghan 1983)) provides:
The initial bylaws of a corporation shall be adopted by its incorporators, its shareholders or its board. The shareholders or the board may amend or repeal the bylaws or adopt new bylaws unless power to do so is reserved exclusively to the shareholders by the articles of incorporation. The shareholders may prescribe in the bylaws that any bylaw made by them shall not be altered or repealed by the board. The bylaws may contain any provision for the regulation and management of the affairs of the corporation not inconsistent with law or the articles of incorporation.
This language may be interpreted to serve as identification of the parties charged with the authority to adopt initial bylaws rather than to operate as a requirement that bylaws be adopted. It might be argued that there is little difference between the express power to adopt and repeal bylaws and the power never to adopt bylaws at all.
79. See Model Stat. Close Corp. Supp. § 22. Because the Act is not integrated, the proposed amendment would apply to all corporations. It is unlikely, however, that large, publicly-held corporations would elect to operate without bylaws.
80. Id. §23(a).
81. Id.
82. Id. § 23(2).
83. Mich. Comp. Laws § 450.1402 (West 1973) (Mich. Stat. Ann. §21.200(402) (Callaghan 1983)). Under Section 407, the articles of incorporation may provide for action to be taken without a meeting, if there is written consent setting forth the action to be taken and signed by the requisite number of shareholders. Id. §21.200(407).
84. Id. § 405.1407 (Mich. Stat. Ann. § 21.200(407)(Callaghan 1983)).
85. Id. § 405.1402 (Mich. Stat. Ann. §21.200(402)(Callaghan 1983)).

86. Id. Although a federal court in *Studebaker Corp. v. Allied Products Corp.*, 256 F.Supp. 173, 189 (W.D. Mich. 1966), concluded that, under Michigan law, an annual meeting is implicitly required, the case was decided prior to the promulgation of the Business Corporation Act. Therefore, the court did not have the opportunity to address the rights and responsibilities of close corporations under the present Michigan law. Additionally, the court's conclusion may be considered dictum.
87. Id. § 14(a).
88. Id. § 14(c).
89. Id. § 14(d).
90. Mich. Comp. Laws § 450.1473 (West 1973)(Mich. Stat. Ann. § 21.200(473) (Callaghan 1983)).
91. Model Stat. Close Corp. Supp. § 14.
92. Id. § 14, official comment.
93. Id. § 14.
94. Id. § 25.
95. Id., official comment.
96. Id. § 24.
97. Mich. Comp. Laws § 450.1531(2) (West 1973)(Mich. Stat. Ann. § 21.200(531)(2)(Callaghan 1983)).
98. Id. § 450.1331 (Mich. Stat. Ann. § 21.200(331)(Callaghan 1983)) (facsimile signatures are allowed).
99. Id. §§ 450.1201, .1231 (Mich. Stat. Ann. §§ 21.200(201), (231)(Callaghan 1983)).
100. These questions were derived from the guiding principles used in drafting the Model Stat. Close Corp. Supp., ABA Report, supra note 6, at 271.
101. See Siedel, supra note 73.
102. ABA Report, supra note 6, at 271.