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With wider recognition of the special problems experienced by participants in closely held enterprises, it is the author's thesis that business corporation acts, specifically, the Wyoming Business Corporation Act, should be revised to meet such problems. Focusing upon the major areas of corporate activity that generate difficulties for the close corporation, Professor Carney analyzes the manner in which more flexiable corporation laws have alleviated these difficulties. The author advocates changes to the Wyoming Business Corporation Act that are more in keeping with the unique character of the Wyoming corporation.

CLOSE CORPORATIONS AND THE WYOMING BUSINESS CORPORATION ACT: TIME FOR A CHANGE?

*William J. Carney**

INTRODUCTION

It has been sixteen years since Wyoming adopted its present Business Corporation Act.[1] At that time the Wyoming State Bar undertook, at considerable effort, a review of the then current state of the law in order to recommend a modern corporation statute which would meet the needs of Wyoming business.[2] While the Bar's recommendations centered around the then current version of the Model Business Corporation Act,[3] the Bar Committee also reviewed other leading cor-

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1. Wyoming Business Corporation Act. 1961 Wyo. Sess. Laws ch. 95, § 1 *et seq.* (codified as WYO. STAT. § 17-36.1 *et seq.* (1965)).
2. The history of this effort is outlined in Rudolph, *The New Wyoming Business Corporation Act*, 15 WYO. L.J. 185, 185-86 (1961).
3. At the time of the Bar's consideration of these revisions, the version of the Act most commonly in use was the 1953 revision, printed in 1957, ABA-ALI MODEL BUS. CORP. ACT (1957). By the time of enactment, a 1959 revision had been adopted by the American Bar Association, but was not printed until 1960, and was not generally available until 1961. ABA-ALI-MODEL BUS. CORP. ACT. ANN. (1960).

poration statutes and adopted some of the most modern solutions to the problems of the closely held corporation.[4] The Act as adopted represented an exemplary effort by the State Bar to keep abreast of rapid changes in corporation law. It was unfortunate that the American Bar Association came out with a revised version of the Model Business Corporation Act only slightly after the effort was completed,[5] and that some of the reforms of that act were not included in the Wyoming Act.[6]

No major substantive amendments have been made to the Wyoming Act since that time. In the last sixteen years, however, corporation law has continued to change rapidly. Perhaps the most important change was the adoption of a second edition of the Model Business Corporation Act in 1968, which contained major changes affecting the closely held corporation.[7] These Model Act changes followed closely on the heels of the major overhaul of the Delaware General Corporation law in 1967 and incorporated many of the Delaware innovations.[8] Both acts represented a massive effort by corporation law experts and scholars to draft corporation acts which were truly "enabling" acts and which would provide maximum flexibility for the corporate entity. Delaware dealt expressly with close corporations, and has essentially authorized the incorporated partnership, eliminating many of the technical objections which courts have raised in the past to such entities.[9]

This article will focus on the problems of the closely held corporation, and review the changes in modern corpora-

4. The provisions on share transfer restrictions, in Section 17-36.32 of the Wyoming Statutes (1965), were patterned after the Texas provisions. Rudolph, *supra* note 2, at 195, n. 73.
5. ABA-ALI MODEL BUS. CORP. ACT (1957).
6. *See* the discussion of removal of directors *infra* text at notes 182-188.
7. ABA-ALI MODEL BUS. CORP. ACT ANN. (2nd ed. 1971). A pamphlet edition preceded this. A discussion of the Model Act provision can be found in Scriggins, *Developments in State Corporation Law—1969*, 25 BUS. LAW. 1691, 1701-02 (1970) and Scott, *Changes in the Model Business Corporation Act* 24 BUS. LAW 291 (1968).
8. Delaware General Corporation Law, DEL. CODE ANN. tit. 8, § 398 *et seq.* (1974). *Compare* the present Model Act treatment of indemnification of officers and directors *with* that of the Delaware statute. *See* text *infra* at notes 167-77.
9. DEL. CODE ANN., tit. 8, §§ 341-356 (1974).

tion law as they affect such corporations.[10] This author's predilection is for a modern corporation act, particularly one governing closely held enterprises, which is essentially an enabling statute, giving participants maximum flexibility to arrange their affairs by agreement, as in a partnership. Problems of unfairness are best dealt with in equity, rather than with rigid and formal rules ill-suited to the needs of many businesses. State corporation laws have come under considerable criticism for being too "liberal" in recent years, but these criticisms are directed primarily at the way in which these laws deal with the publicly held corporation.[11] Professor Cary has charged that, with Delaware leading, there has been a race downward in morality in corporate standards.[12] Ralph Nader has suggested federal chartering as a solution to the abuses which he and his organization perceive in the publicly held corporation.[13] Congressional hearings have even been held on the subject.[14]

Whatever the outcome of such debates, they should have little effect on Wyoming corporate law. The vast majority of Wyoming corporations are closely held, and in view of the scarcity of Wyoming Supreme Court decisions in the area, there is little likelihood that Wyoming will ever be a popular jurisdiction with giant publicly held corporations. The question which Wyoming lawyers and lawmakers must continually address is whether Wyoming's business corporation law adequately serves the needs of closely held businesses. This article will review major areas of difficulty in the present Wyoming Act, and attempt to point out some of the major

10. There is no universal agreement on the size limit of a closely held corporation. Delaware's Act uses a 30 shareholder limit (DEL. CODE ANN. tit. 8, § 342(a) (1974)). California's new act uses ten (CAL. CORP. CODE § 158 (a) (West Supp. 1977). Wyoming's provisions permitting certain restrictions on the transfer of shares are subject to a proviso that the corporation have no more than 20 shareholders. WYO. STAT. § 17-36.32(c)-(d) (1965). Professor O'Neal discusses the variety of tests and definitions in 1 O'NEAL, CLOSE CORPORATIONS ch. 1 (2d ed. 1971).

11. The most ambitious recent attack is by NADER, GREEN & SELIGMAN, CONSTITUTIONALIZING THE CORPORATION: THE CASE FOR THE FEDERAL CHARTERING OF GIANT CORPORATIONS (1976).

12. Cary, *Federalism and Corporate Law: Reflections upon Delaware*, 83 YALE L.J. 663 (1974).

13. NADER, GREEN & SELIGMAN, *supra* note 11.

14. *Hearings Before the Comm. on Commerce, on Corporate Rights and Responsibilities*, 94th Cong. 2d Sess. (June 15-17, 21-23 (1976)).

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trends of modern legislation dealing with the closely held corporation.[15]

ORGANIZATION AND CAPITALIZATION

Generally the requirements of Wyoming law concerning creation of the corporation are simple and modern, and should cause little difficulty.[16]

Payment of Minimum Capital

Section 49 of the Act requires that consideration of the value of at least $500 shall be paid into the corporation before it transacts business.[17] This requirement is reinforced by a provision that articles of incorporation shall contain a similar statement.[18] At the time of adoption of the Wyoming Act, the drafters omitted a provision of the Model Act which limited the liability of directors in such cases to the deficiency below such paid-in capital.[19] Elimination of this provision limiting liability of directors may create the inference that the drafters intended to impose unlimited liability upon directors who begin business without such minimum capital,

15. No attempt is made here to define the close corporation. Generally it is regarded as a corporation which has few shareholders, no general market for its stock, and participation in management by a significant proportion of its shareholders. Frequently it is operated informally, and restrictions are imposed on entry of new participants in the enterprise. *See* O'NEAL, *supra* note 10.
16. WYO. STAT. §§ 17-36.45 and 36.48 (1965). Correspondence with the office of the Secretary of State indicates the most common error relates to compliance with Section 17-36.46(5) of the Wyoming Statutes (1965), where the initial board of directors will be less than three members.
17. WYO. STAT. § 17-36.49 (1965) provides:

    A corporation shall not transact any business or incur any indebtedness, except such as shall be incidental to its organization or to obtaining subscriptions to or payment for its shares, until there has been paid in for the issuance of shares considerations of the value of at least five hundred dollars.
18. Section 17-36.46(g) of the Wyoming Business Corporation Act requires articles of incorporation to set forth: "A statement that the corporation will not commence business until consideration of the value of at least five hundred dollars has been received for the issuance of shares."
19. Section 43(e) of the Model Act provided:

    If a corporation shall commence business before it has received at least $1,000 [*the minimum required paid-in capital*] as consideration for the issuance of shares, the directors who assent thereto shall be jointly and severally liable to the corporation for such part of $1,000 as shall not have been received before commencing business, but such liability shall be terminated when the corporation has actually received $1,000 as consideration for the issuance of shares. 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 43 (e) (1960).

a drastic result in view of the insignificant amount required by the Act. The current version of the Model Act contains no minimum capital requirement,[20] a more realistic approach to the problem. Surely there are very few corporations where $500 represents significant capital in today's economy, and it seems unrealistic to pick any arbitrary amount as providing significant protection for creditors of the enterprise. The common law approach of "piercing the corporate veil" where a corporation is grossly undercapitalized, and holding the participants in the enterprise liable as principals seems far more equitable.[21] Creditors have been doing business with closely held corporations of limited capital for a sufficiently long time to realize that incorporation is no guarantee of substantial capital.[22]

Consideration for Shares

It is not unusual for the closely held corporation to be owned by persons performing two separate functions—entrepreneurs, who promote and organize the entity, and capitalists, who provide substantial funds to finance the business. Even where the parties agree that the contributions of the entrepreneurial group are equal to those of the capitalists, corporation statutes such as Wyoming's still impose roadblocks to the accomplishment of equal ownership. Wyoming's statute prohibits the payment for shares with either promissory notes or future services.[23] In this respect Wyoming's Act is similar to the provisions of both the Model[24] and Delaware[25] Acts. Thus the standard rule of nearly all jurisdic-

20. ABA-ALI MODEL BUS. CORP. ACT ANN. (2d ed. 1971).
21. *See, e.g.*, Arnold v. Phillips, 117 F.2d 497 (5th Cir. 1941); Minton v. Cavaney, 56 Cal.2d 576, 364 P.2d 473, 15 Cal. Rptr. 641 (1961). *Cf.* Walkovszky v. Carlton, 18 N.Y.2d 414, 223 N.E. 2d 6, 276 N.Y.S.2d 585 (1966).
22. *See, e.g.*, Bing Crosby Minute Maid Corp. v. Eaton, 46 Cal. 2d 484, 297 P.2d 5 (1956).
23. The Wyoming Business Corporation Act provides in part: "Neither promissory notes nor future services shall constitute payment or part payment, for shares of a corporation." WYO. STAT. § 17-36.16 (1965).
24. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 19 (2d ed. 1971).
25. DEL. CODE ANN. tit. 8, § 152 (1974). FOLK, THE DELAWARE GENERAL CORPORATION LAW: A COMMENTARY AND ANALYSIS (1972), states at 117: "Since § 152 explicitly says that subscriptions may be paid by 'labor done,' only past services are valid consideration for the issuance of fully paid, nonassessable stock."

Also *see* Folk's statement that "Delaware follows the majority rule that a promissory note or a promise to lend money to the corporation in the future given in payment for fully paid, nonassessable stock does not constitute 'money paid' or 'property actually acquired' within the statute and is therefore unlawful consideration." FOLK, *supra*, at 119.

tions prohibits the issue of stock for such consideration. The problem has not loomed large for experienced corporate counsel, who have solved it through the use of low-par or no-par shares, which make it possible for the entrepreneur to receive a substantial portion of the equity interest in the corporation for nominal consideration, such as one dollar, or the like. Where the shares are of higher par value, it may be necessary for the capitalist to purchase all of the shares originally issued, and then transfer an appropriate number to the entrepreneur in consideration of his promissory note or promise of future services.

These statutes were designed to preclude the types of fraud which took place largely in the 19th century, when great issues were offered to the public in companies where the promoters had taken vast amounts of stock for nothing, or for worthless assets. Such frauds are better dealt with today under the securities laws.[26] The theories which were created to deal with the watered stock problem at an earlier time, though ingenious, were artificial, and are hardly suited to conditions a century later.[27]

The problems of watered stock exist only for those corporate promoters represented by counsel inexperienced in corporate affairs, who fail to appreciate the need for low-par shares, or who fail to warn their clients adequately. Quite aside from whether creditors are defrauded, the transaction between promoters may legitimately contemplate the issuance of shares to promoters in consideration of promissory notes or future services. The prospective chief officer of the corporation may demand some present compensation for the risk he takes in leaving a secure position, and the capitalist may agree to give this person a present claim against the assets which he is contributing to the corporation. A mod-

26. Securities Act of 1933, 15 U.S.C. § 77 *et seq.* (1970); Wyoming Uniform Securities Act, WYO. STAT. § 17-117.1 *et seq.* (1965).
27. *See* Hospes v. Northwestern Mfg. & Car Co., 48 Minn. 174, 50 N.W. 1117 (1892), rejecting the theory stated by Mr. Justice Story in Wood v. Drummer, 30 F.Cas. 435 (C.C.D. Me. 1824) (No. 17, 944), that the stated capital of a corporation is a fund held in trust for the benefit of the creditors of a corporation, and inventing a theory that the holders of watered or bonus shares have misrepresented the condition of the corporation to its creditors, regardless of whether creditors actually relied on the stated capital.

ern corporate statute which attempts to allow the parties to the corporation to contract in any manner which is not fraudulent should not specify permissible and forbidden types of consideration.[28] A misrepresentation theory, which protects against actual frauds on creditors, should provide sufficient protection to outsiders.[29]

Further, the initial promoters are generally held to be fiduciaries with respect to their dealings with the corporation, and this duty is widely held to run for the length of the process by which the corporation is capitalized, so subsequent shareholders can complain in the corporation's name should the promoters' transactions with the corporation turn out to be so unfair as to constitute constructive fraud.[30] With ample remedies available to protect shareholders and creditors from actual fraud, there is little justification for corporate rules which operate primarily as a trap for the unwary, readily avoidable by more experienced practitioners and promoters.[31]

SHAREHOLDERS

Shareholders in the closely held corporation generally consider it important to control the identity of the participants, much as in a partnership.

Shareholder's Preemptive Rights

The Wyoming Act recognizes the doctrine of preemptive rights[32] and incorporates the language of the Model Act of the time.[33] The Act merely recognizes the rights which have

28. No such restrictions appear in partnership law, which allows participants to arrange their shares by contract. Even in the limited partnership, the only restriction is disclosure of the capital contributions of the participants in the certificate of limited partnership. Uniform Limited Partnership Act, WYO. STAT. § 17-265(a)(i)(F) (Supp. 1976).
29. Hospes v. Northwestern Mfg. and Car Co., *supra* note 27; Tuttle v. Rohrer, 23 Wyo. 305, 149 P. 857 (1915).
30. *See* San Juan Uranium Corp. v. Wolfe, 241 F.2d 121 (10th Cir. 1957) and Old Dominion Copper Mining & Smelting Co., 203 Mass. 159, 89 N.E. 193 (1909). But *see* Old Dominion Copper Mining & Smelting Co. v. Lewisohn, 210 U.S. 206 (1907).
31. *See* Herwitz, *Allocation of Stock Between Services and Capital in the Organization of a Close Corporation*, 75 HARV. L. REV. 1098 (1962).
32. WYO. STAT. § 17-36.23 (1965).
33. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 24 (1st ed. 1960).

existed at common law since early in the 19th century.[34] The only alteration which it makes in such rights is to provide that they may be limited or denied in two ways. They may be limited or denied in the articles of incorporation, or, absent that, by two-thirds vote of the shareholders entitled to vote thereon, authorizing the issue and sale of shares to officers or employees of the corporation or its subsidiaries.[35]

While the doctrine of preemptive rights is universally recognized, it is by no means simple in its application.[36] Historically the right to vote was thought to be the predominant right of the shareholders protected by the doctrine.[37] However, over time courts also have begun to focus on the economic aspects of preemptive rights.[38] Once preemptive rights are regarded as protecting both the voting rights and equity interests, confusion results when the capital structure of a corporation grows more complex.[39]

In addition to being of somewhat uncertain application with respect to the kind of rights protected, the doctrine is replete with exceptions, which have been made necessary by the awkward rigidity of its approach to what is basically an equitable problem.[40] For example, an exception exists for

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34. Gray v. Portland Bank, 3 Mass. 364, 3 Am. Dec. 156 (1807) was the first American case relating to preemptive rights.

35. WYO. STAT. § 17-36.23 (1965).

36. 11 FLETCHER, CYCLOPEDIA CORPORATIONS § 5135 (perm. ed. 1971).

37. *See* CARY, CASES AND MATERIALS ON CORPORATION 1133 (4th Ed. unabr. 1969). An effective argument that this should be the only basis for preemptive rights appears in Frey, *Shareholders' Preemptive Rights.* 38 YALE L.J. 563 (1929).

38. This seems to be the basis of the opinion of Justice Sewall in Gray v. Portland Bank, *supra* note 34, at 378, where he discussed the prospect that the subsequent stockholders would benefit from the expenditures made from the first subscription to develop the bank. Indeed, there is little if any discussion of voting rights in the case.

39. *See* discussion in Frey, *supra* note 37. *See also* N.Y. BUS. CORP. LAW § 622 (McKinney 1963), recognizing preemptive rights with respect to both voting and equity interests. Note that where separate classes of shares exist with voting and equity interests, and new shares are to be issued diluting the rights of both classes, the statute is unable to resolve the conflict over the appropriate allocation. It simply leaves the matter to the discretion of the board of directors. *See* N.Y. BUS. CORP. LAW § 622(d) (McKinney 1963).

40. 11 FLETCHER, *supra* note 36, § 5135.1, before treating the various exceptions, discusses the importance of the fiduciary duty of directors in issuing shares. For a case discussing the complexities and dealing simply with the fiduciary problems, *see* Ross Transport, Inc. v. Crothers, 185 Md. 573, 45 A.2d 267 (1946).

shares which are part of the original issue or authorization.[41] But this exception did not anticipate that practices would change so it would become customary to authorize far more shares than were originally intended to be issued. In response, the doctrine has been limited by some courts to the shares originally contemplated to be issued.[42] Similarly, courts have carved out exceptions where circumstances have changed since the original plan to issue shares.[43] Other exceptions have developed in other jurisdictions for such transactions as mergers, acquisitions of assets which cannot be purchased for cash, sales of treasury shares (presumably not applicable in Wyoming because of the statute) as well as for employee plans, which are recognized in Wyoming.[44]

In the end, one can only state that the doctrine is complex, confusing, sometimes inconsistent, and subject to severe limitations by a court of equity whenever it sees unfairness.[45] Under these circumstances, it seems likely that many counsel do not fully consider all of the ramifications of preemptive rights when they omit their mention in drafting articles of incorporation. Indeed, in view of the absence of Wyoming case law on the subject, it is probably impossible to do so. Thus the existence of preemptive rights, beneficial as they may be in the close corporation, creates considerable

41. Ross Transport, Inc. v. Crothers, *supra* note 40; Yasik v. Wachtel, 25 Del. Ch. 247, 17 A.2d 309 (1941) and Dunlay v. Avenue M Garage and Repair Co., 253 N.Y. 174, 170 N.E. 917, 919 (1930); 11 FLETCHER, *supra* note 36, § 5136.1, at 179-80; BALLANTINE, CORPORATIONS § 135, at 421 n. 34; 2 HORNSTEIN, CORPORATION LAW AND PRACTICE § 523, at 148 (1959).

42. In *Dunlay v. Avenue M Garage and Repair Co.*, the Court made this distinction and stated:

> The issued stock may be related to the unissued stock as stock for immediate use to stock for future expansion. In such cases the preemptive right might not be denied. It has been too loosley stated that 'a corporation may use its original unissued authorized capital stock for any legitimate or lawful purpose it sees fit.' [Citation omitted] If the issue of the unissued original shares, whenever authorized, is reasonably necessary to raise money to be used in the business of the corporation rather than the expansion of such business beyond the original limits, the original shareholders have no right to count on obtaining and keeping their proportionate part of the original stock.

Dunlay v. Avenue M Garage and Repair Co., *supra* note 41, at 919.

43. Ross Transport, Inc. v. Crothers, *supra* note 40, at 271.

44. Compare N.Y. BUS. CORP. LAW § 622(e) (McKinney 1963).

45. Katzowitz v. Sidler, 24 N.Y.2d 512, 249 N.E.2d 319, 301 N.Y.S.2d 470 (1969); Gord v. Iowana Farms Milk Co., 245 Iowa 1, 60 N.W.2d 820 (1953); Bennett v. Breuil Petroleum Corp., 34 Del. Ch. 6, 99 A.2d 236, 239 (1953); Steven v. Hale-Haas Corp., 249 Wis. 205, 23 N.W. 620, 630-31 (1946); 11 FLETCHER, *supra* note 36, § 5135.1, at 173-174.

uncertainty and confusion. Perhaps for these reasons the current Model Act denies preemptive rights unless they are provided in the articles of incorporation.[46] Another explanation may be that the drafters were focusing more on the publicly held corporation, where such rights are awkward and often inadvertently violated.[47]

As an alternative, the Model Act provides for the existence of preemptive rights except to the extent denied in the articles (a provision much like the present Wyoming Act), or to the extent denied by the Model Act itself.[48] The alternative provisions in Section 26A of the current Model Act provide that no preemptive rights shall exist with respect to shares sold to officers, directors or employees, unless otherwise provided in the corporate articles, which does not significantly change existing Wyoming law.[49] The current Model Act also provides a broad exception for shares issued for consideration other than cash.[50] Perhaps the most significant change in the Model Act is to resolve doubts whether preemptive rights are based on voting rights or economic interests in the corporation. The Model Act alternative section provides that preemptive rights exist only with respect to shares having voting rights,[51] and for such shareholders, only with respect to stock in the same class—not of other classes which may dilute the economic interest of those shareholders.[52]

If such a restrictive approach were to be taken in Wyoming, it might be well to add a provision such as that of North Carolina, which reaffirms the shareholders' right of action

46. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 26 (2d ed. 1971).

47. The comments to the present version of the Model Act indicate heavy reliance on the equitable principles discussed above. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 26A, ¶ 2 (2d ed. 1971). They also contain a discussion of the complexity of the doctrine and the growth and complexity of capital structures of publicly held corporations, which make the doctrine less advisable. These reasons seem less applicable in a state such as Wyoming, where the act will be used predominantly for closely held enterprises.

48. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 26A (2d ed. 1971).

49. *Compare* 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 26A(a)(1) (2d ed. 1971) *with* WYO. STAT. § 17-36.23 (1965). In view of the fact that the officers will often be all or most of the shareholders in a closely held business, such a provision may unduly frustrate preemptive rights.

50. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 26A(a)(2) (2d ed. 1971).

51. ABA-ALI MODEL BUS. CORP. ACT. § 26A(d) (2d ed. 1971).

52. ABA-ALI MODEL BUS. CORP. ACT. § 26A(c) (2d ed. 1971).

for breach of fiduciary duty in the issue of shares.[53] This author's view is in accord with that of Professor O'Neal, who regards the existence of preemptive rights for closely held corporations as essential.[54] If this view is accepted, the current basic approach of the Wyoming Act should be preserved, to provide for preemptive rights unless denied in the articles of incorporation. In view of the confusion, the nature of the rights could well be spelled out in the Act itself, taking into consideration the rules provided in the current Model Act, the New York Act and others.

Share Transfer Restrictions

Shareholders in the closely held corporation are frequently concerned that new participants not be admitted by their fellow shareholders. To protect themselves they frequently attempt to impose a variety of restrictions on the transfer of shares. Wyoming has one of the most modern statutes regulating such restrictions.[55] Its source was the Texas statute, and it deals with most of the commonly used forms of restraints.[56] While in many jurisdictions there is doubt about what constitutes a reasonable restraint on alienation,[57] Wyoming's Act appears to resolve most of those doubts. For example, consent restraints appear to be pre-

53. *See* N.C. GEN. STAT. § 55-56(e) (1975) which provides:

> The issuance of shares that are not subject to preemptive rights shall not impair any remedy which any shareholder may have for a breach of fiduciary duties on the part of the board of directors with respect thereto. The remedy may include the granting of such preemptive rights or the cancellation of such a number of shares or the compulsory allowance by the corporation of such amount of money damages as the court may order.

54. *O'Neal, Molding the Corporate Form to Particular Business Practices: Optional Charter Clauses*, 10 VAN L. REV. 1, 41 (1956).
55. WYO. STAT. § 17-36.32 (1965).
56. Rudolph, *supra* note 2, at 194-95, n. 73. *See* TEX. BUS. AND COMM. CODE ANN. tit. 3A, § 2.22 (Vernon 1968).
57. A century ago such restraints were often questioned as unreasonable restraints on alienation. Morris v. Hussong Dyeing Mach. Co., 81 N.J.Eq. 256, 86 A. 1026 (1913); *In re* Klaus, 67 Wis. 401, 29 N.W. 582 (1886); Feckheimer v. National Exchange Bank of Norfolk, 79 Va. 80 (1884); 12 FLETCHER, *supra* note 36, § 5452. Since that time, the general rule has been modified in most jurisdictions so "what the law condemns is, not a restriction on transfer . . . but an effective prohibition against transferability itself." Allen v. Biltmore Tissue Corp., 2 N.Y.2d 534, 542, 141 N.E.2d 812, 816, 161 N.Y.S.2d 418, 423 (1957); and *see* 1 HORNSTEIN, *supra* note 41, § 194, at 256 (1959); 2 O'NEAL, *supra* note 10, ch. 71; and O'Neal and Smith, *The Close Corporation and the Colorado Lawyer*, 39 U. COLO. L. REV. 299 (1967). The latter article attempts to delineate standards of reasonableness. *Id.* at 302-03.

sumptively reasonable, even where, as in the two shareholder corporation, a veto power in either shareholder may effectively amount to a prohibition of transfers.[58] In other jurisdictions the validity of such consent restraints is at least questionable.[59]

Although Wyoming's basic approach in this area has been to allow the shareholders in the closely held corporation virtually as much freedom as partners, who have a veto power over the admission of new members,[60] the Act, unlike the partnership act, fails to provide a set of rules governing the relationship in the absence of specific agreement. The risk for shareholders is that they will fail to utilize the broad powers granted by Section 32, and will thus allow a shareholder to sell to a stranger whose presence will not benefit the enterprise. An alternative which Wyoming might consider is a prohibition on stock transfers in closely held corporations, absent shareholder consent, unless otherwise provided in the articles of incorporation. Maryland has taken such an approach.[61] California's new close corporation provisions go nearly as far to keep the shareholder group within the ten shareholders allowed by the act.[62]

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58. WYO. STAT. § 17-36.32(d) (1965).
59. Rafe v. Hindin, 29 App. Div.2d 481, 288 N.Y.S.2d 662 (1968), invalidated a consent restraint in a two-shareholder corporation, on the theory that it gave an effective veto power to each shareholder.
60. Uniform Partnership Act, WYO. STAT. § 17-212(g) (1965), provides that "No person can become a member of partnership without the consent of all the partners." The withdrawal of a partner from carrying on the partnership business dissolves the partnership under Section 17-223 of the Wyoming Statutes (1965), thus emphasizing the importance of the relationship.
61. MD. CORP. & ASS'N. CODE ANN. § 101(a) (Supp. 1969). The Maryland Legislature "has embodied the position . . . that the partnership and the close corporation are functionally equivalent . . . [and] has done so in a simple clear directive that stock of a close corporation may not be transferred, without the consent of all of the stockholders. . . ." Bradley, *Stock Transfer Restrictions and Buy-Sell Agreements*, 1969 U. ILL. L.F. 139, 151 (1969).
62. The California Act provides that a close corporation may have no more than ten shareholders. CAL. CORP. CODE § 158(a) (1977). The act requires all certificates to carry the following legend:

    This corporation is a close corporation. The number of holders of record of its shares of all classes cannot exceed [a number not in excess of 10]. Any attempted voluntary inter vivos transfer which would violate this requirement is void. Refer to the articles, bylaws and any agreements on file with the secretary of the corporation for further restrictions. CAL. CORP. CODE § 418(c) (Supp. 1977).

    The placing of such a legend on a certificate voids any transfer which would result in a violation of the numerical limitation. CAL. CORP. CODE § 418(d) (Supp. 1977).

Provisions which presume a personal relationship among the shareholders in the closely held corporation, and restrict transfer unless shareholders consciously alter this relationship, suggest the need for separate treatment of closely held corporations in a statute which otherwise treats shares as freely transferable personal property.

Cumulative Voting

Share ownership is the most important way of allocating control. Cumulative voting is an important supplement, especially for minority shareholders. Presently the Wyoming Act mandates cumulative voting.[63] It is not the purpose of this article to make a value judgment about the desirability of such a provision. Cumulative voting was required in a number of state constitutions adopted between 1870 and 1900, with only one state adopting such a constitutional provision since that date.[64] The current Model Act permits but does not require cumulative voting,[65] as does the Delaware Act.[66] Philosophically, the question boils down to whether representation of minority groups on the board of directors is so essential to the protection of their rights that it demands reduction in the freedom of choice generally available to incorporators and shareholders in structuring their own business and control relationships. The general thrust of modern corporation statutes has clearly been to allow greater freedom to the members of a business enterprise in structuring these relationships. At the same time, this tendency has been balanced to some extent by increasingly stringent standards of fiduciary duty towards minority shareholders.[67]

63. WYO. STAT. § 17-36.30 (1965).
64. Ten states now require cumulative voting in their constitutions—Arizona, Idaho, Illinois, Kentucky, Missouri, Montana, Nebraska, North Dakota, South Dakota and West Virginia. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 33 and § 3.03, at 691 (2d ed. 1971). The specific citations to constitutional provisions are found in 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 31, ¶ 4, § 2.01, at 522 (1960). Other states also make cumulative voting mandatory by statute. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 33 ¶ 4, § 3.03(2), at 691 (2d ed. 1971).
65. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 33 (2d ed. 1971).
66. DEL. CODE ANN. tit. 8 § 214 (1974).
67. Federal corporation law has to a large extent been responsible for this development. Expanded regulation of proxy solicitations under Section 14 of the Securities Exchange Act of 1934, 15 U.S.C. § 78 (1970), and heightened duties of disclosure of material inside information by corporations under Section 10(b) of that act and rule 10b-5, have been at the heart of

Given the present legislative decision in favor of protection of minority rights through mandatory cumulative voting, several problems are created by the silence of the statute in other respects. The problem of removal of directors is treated elsewhere in this article.[68] Classification of directors requires extension of their terms beyond one year if one wishes to stagger terms so the tenure of directors will overlap. Continuity on a board of directors may benefit the enterprise through the growing experience and knowledge of the board over time. The Wyoming Act is presently somewhat ambiguous on length of term of directors[69] and silent on whether directors may be classified and their terms staggered. The case law in such situations is divided, lending to confusion for the attorney attempting to give his clients the maximum freedom of action in planning a business enterprise.[70] Commentary contemporary with the adoption of the Wyoming Act indicates that classification of directors may be permissible, but the matter could certainly be clarified, if the legislature so desired.[71] The justification given by the commentator in question is based on provisions of Section 30, which were taken directly from the Model Act. The difficulty with this analysis is that the Model Act left cumulative voting as an option, and language in other related sections

much of this movement. *See* Schoenbaum v. Firstbrook, 405 F.2d 200, *rev'd en banc* 405 F.2d 215 (2d Cir. 1968), *cert. denied* 395 U.S. 906 (1969) 1; S.E.C. v. Texas Gulf Sulphur Co., 401 F.2d 833 (2d Cir. 1968).

68. *See* text *infra* at notes 179-89.
69. The last two sentences of Section 34 of the Wyoming Business Corporation Act provide that "At the first annual meeting of shareholders and at each annual meeting thereafter the shareholders shall elect directors to hold office until the next succeeding annual meeting. Each director shall hold office for the term for which he is elected and until his successor shall have been elected and qualified." WYO. STAT. § 17-36.34 (1965).

    The implication of the first sentence is that a director holds office from one annual meeting to the next. It is at least arguable that the second sentence negates that, since it states not that the director shall hold office until the next annual meeting, but that he shall hold office for the term for which he is elected.
70. Wolfson v. Avery, 6 Ill.2d 78, 126 N.E.2d 701 (1955), held under a provision of the Illinois Constitution substantially similar to the language of the Wyoming Business Corporation Act that classification of a board of directors was invalid since it diminished the proportional representation on the board which was required by the constitution. On the other hand in Janney v. Philadelphia Transportation Co., 387 Pa. 282, 128 A.2d 76 (1956) an opposite result was reached on slightly different language.
71. Rudolph, *supra* note 2, at 191 n. 46, citing as authority the provisions of section 30 of the Act that every shareholder shall have the right to vote for "as many persons as there are directors to be elected and for whose election he has a right to vote." This may mean that different classes of shares may have the right to elect a certain number of directors.

of the Act was left broad and general enough to accommodate either legislative decision.[72] Staggered terms for directors also represent an important defensive device for the publicly held corporation facing the threat of a takeover, since a new majority shareholder may find that with staggered terms it will be several years before control of the board can be obtained.[73]

The other question is whether shares and directors can be classified so holders of separate classes of stock select a designated number of directors.[74] Share classification for this purpose can be used either to enhance or frustrate minority interests, and merits specific consideration and treatment in a corporation law.[75] Allowing classification of directors within reasonable limits would be consistent with both protection of minority interests and allowing contractual flexibility in the close corporation. For example, as long as there are no fewer than three directors in each class, minority interests receive as much protection as is presently required by the Act, which requires no more than three directors.

Director Vacancies

Section 35 of the Wyoming Act states that "any vacancy occurring in the Board of Directors *may* be filled by the affirmative vote of the majority of the remaining directors though less than a quorum of the Board of Directors."[76] More flexibility, consistent with the contract theory of corporation law rather than the concession theory, could be granted by allowing modification of this rule in either the articles of incorporation or the bylaws of the corporation.[77]

72. 1 ABA-ALI MODEL BUS. CORP. ACT § 31 (1960).
73. If the old management still retains enough stock to be able to elect some directors through cumulative voting, minority control may be stretched out even further. Whether the new majority shareholder can remove existing directors without cause is discussed in the text, *infra* at notes 187-89.
74. *See* the views of Rudolph, *supra* note 2, at 191.
75. For example, a 10% investor can be assured board representation by giving him a class of stock entitled to elect one out of three board members. On the other hand, with two shareholders holding 70% and 30% of the common stock, (26% is enough stock to elect ⅓ of the board, given cumulative voting) the majority shareholder could frustrate cumulative voting by creating 3 classes of stock, each electing one director, if the majority shareholder holds a proportionate interest in each class.
76. WYO. STAT. § 17-36.35 (1965).
77. *See* the discussion of these theories in O'Neal, *supra* note 54, at 20-21.

The difficulty with the present requirement is well illustrated in *Gearing v. Kelly*,[78] where two shareholder groups each held equal amounts of shares and each elected two directors. When one of the plaintiff's directors resigned, a board meeting was attended by the resigning director and the two opposition directors, who accepted her resignation and elected an ally of theirs to replace her, thus shifting power to one side. Problems like this are readily avoidable if attorneys can tailor their bylaws to solve the problem. In the close corporation there is no reason why contracts, bylaws and articles of incorporation should not allow replacement of a director by the persons who elected that director, the shareholders, or a class of shareholders.

SHAREHOLDER MEETINGS AND VOTING

For the shareholder, once the questions of ownership of shares and their voting rights are determined, the focus shifts to the exercise of those voting rights. Here the emphasis of close corporation law shifts from questions of fairness to those of convenience and recognition of the informal manner in which many such corporations operate.

Notice of Meetings

Few changes of consequence have occurred in the provisions relating to notice of shareholders' meetings in modern statutes. Wyoming requires written notice of both regular and special meetings, and where the meeting is a special one, the purpose of the meeting must be set out.[79] If there is a deficiency in delivery of the notice, it can be waived, but only in writing.[80] The language of the Act implies that mere oral waiver or attendance at and participation in the meeting is not sufficient to constitute a waiver. The Model Act is unchanged in this respect. This should be contrasted with the provisions of the Delaware Act, which state that, in addition to written waivers, attendance at a meeting constitutes a waiver of notice unless the person attends the meeting es-

78. 11 N.Y.2d 201, 182 N.E.2d 391 (1962).
79. WYO. STAT. § 17-36.26 (1965).
80. WYO. STAT. § 17-36.120 (1965).

pecially for the purpose of objecting to the meeting as not having been lawfully convened.[81] This provision recognizes the informality which often governs the conduct of the close corporation, where a secretary may fail to give written notice, because all of the shareholders, who are also directors, have been present at a meeting of the board in which they mutually agreed on the time and place of a shareholders' meeting. In such cases the strict requirements of the statute become little more than a trap for the participants in the enterprise.

Shareholder Meetings

The provisions of the Wyoming Act concerning the time and place of shareholder meetings are unusually rigid when compared with modern statutes. Section 25 of the Act requires shareholder meetings, whether regular or special, to be held at such place as is designated in the by-laws.[82] For annual meetings, the time must also be set in the by-laws.[83] The Model Act at the time contained similar provisions.[84] With the amendment of the Model Act in 1969,[85] these meetings may either be held at the place stated in the by-laws, or fixed in accordance with the by-laws, which allows the meeting to be held at various places selected by the directors, if the by-laws so provide.[86] In a society as mobile as ours, such flexibility seems desirable for both close and public corporations.

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81. DEL. CODE ANN. tit. 8, § 229 (1974) provides:

> Whenever notice is required to be given under any provision of this chapter or the certificate of incorporation or bylaws, a written waiver, signed by the person entitled to notice, whether before or after the time stated therein, shall be deemed equivalent to notice. Attendance of a person at a meeting shall constitute a waiver of notice of such meeting, except when the person attends a meeting for the express purpose of objecting at the beginning of the meeting, to the transaction of any business because the meeting is not lawfully called or convened. Neither the business to be transacted at, nor the purpose of, any regular or special meeting of the stockholders, directors, or members of a committee of directors need be specified in any written waiver of notice unless so required by the certificate of incorporation or the bylaws.

82. WYO. STAT. § 17-36.25 (1965).
83. WYO. STAT. § 17-36.25 (1965).
84. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 26 (1960).
85. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 28, at 583 (2d ed. 1971).
86. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 28 (2d ed. 1971).

Quorum Requirements

The Wyoming provisions relating to quorums at shareholders' meetings begin by mixing provisions relating to nonprofit corporations with those for business corporations.[87] There is no excuse for the fact that provisions relating to quorums for members of nonprofit corporations are contained not in the sparse statute relating to such corporations, but in another Act.[88] If nothing else is done in this area, removal of these provisions to their proper location seems essential.

Wyoming sets a majority of the eligible shares as a quorum only where the articles are silent; otherwise there is no limit.[89] In this regard it varies from the Model Act provision in effect at the time of the adoption of the Wyoming Act, which allowed the articles of incorporation to set the quorum as low as one-third of such shares.[90] Why the authors of the Wyoming Act chose to vary from the Model Act in this respect is not explained; all of the earlier editions of the Model Act also limited quorums to not less than one-third.[91]

In the absence of any limit in the statute or by-laws at all, the general rule appears to be that any two shareholders constitute a quorum.[92] A theory of great liberality in setting quorums is consistent with the remainder of the Act, since the Act does not set a minimum vote of all shares entitled to vote for election of directors, or for other actions. The only areas where minimums exist are those major actions not in the ordinary course of business, such as sale of all corporate

87. WYO. STAT. § 17-36.29 (1965).
88. Non-Profit Corporations Act, WYO. STAT. § 17-122.1 *et seq.* (1965).
89. The provisions of section 17-36.29 of the Wyoming Statutes (1965) relevant to business corporations provide:

> Unless otherwise provided in the articles of incorporation, a majority of the shares entitled to vote, represented in person or by proxy, shall constitute a quorum at a meeting of shareholders. If a quorum is present the affirmative vote of the majority of the shares represented at the meeting and entitled to vote on the subject matter shall be the act of the shareholders, unless the vote of a greater number or voting by classes is required by this act or the articles of incorporation or by-laws. . . .

90. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 30 (1960).
91. ABA-ALI MODEL BUS. CORP. ACT § 30 (1950); ABA-ALI MODEL BUS. CORP. ACT § 30 (1953, 1957 Printing); ABA-ALI MODEL BUS. CORP. ACT § 30 (1959, 1961 Printing). All references are to "Handbook A" of the American Law Institute.
92. 5 FLETCHER, *supra* note 36, § 2013.

assets,[93] merger,[94] amendment to the articles of incorporation,[95] dissolutions,[96] and the like. The contemporary commentary on the Wyoming Act is silent on this matter.[97] There are a number of states with no limit on how high or low the quorum may be set in the articles.[98]

The question, then, is whether any limit should be placed on the quorums. Those who favor contractual freedom for the corporate enterprise, especially when closely held, would presumably argue that this is a matter for the shareholders, and not for the state. Professor Folk, on the other hand, argues vigorously that allowing low quorums permits a dominant but minority shareholder to abuse such a position by setting the quorum so that a single shareholder constitutes a quorum.[99] Indeed, he has singled out Wyoming's provision as being vague, and suggests that perhaps the drafters intended to authorize greater-than-majority provisions while barring those for less than majority.[100] Whether they achiev-

93. WYO. STAT. § 17-36.70 (1965).
94. WYO. STAT. § 17-36.65 (1965).
95. WYO. STAT. § 17-36.52 (1965).
96. WYO. STAT. § 17-36.75 (1965).
97. Rudolph, *supra* note 2.
98. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 30, 1st sent., ¶ 2.02, at 481 (1960).
99. Professor Folk, writes: "Any layman can readily see that a corporation dominated by, say, a twenty per cent block of stock, need only fix a twenty per cent shareholder quorum and thereafter, with the aid of some other statutory provisions, need never fear God, man, or the courts." Folk, *Corporation Statutes: 1959-1966. 1966* DUKE L.J. 875, 915 (1966).

Presumably the provisions to which Professor Folk has reference include provisions which allow corporate meetings to take place outside the jurisdiction, such as Section 17-36.25 of the Wyoming Business Corporation Act, and which allow regular meetings to be held without notice of the purpose, as in Section 17-36.26 of the Wyoming Business Corporation Act. Thus, it is theoretically possible for a 20% shareholder in such a corporation to take a vacation in Bermuda and hold a meeting while there. But note that the place of the meeting must be set in the by-laws under Section 17-36.25 of the Wyoming Statutes (1965).
100. Folk, *supra* note 99, at 195, n. 233. Professor Folk leveled special criticism at the provisions of the Iowa Act, which specifically allowed quorums to be set as low as one-sixth of the voting shares, apparently to accommodate local telephone corporations and the like, which have hundreds of holders of one share each. He also stated:

> Regrettably some other statutes, while not so blatant as Iowa, are vague on reducing a statutory quorum of a majority. Uusally this comes from stating the majority quorum rule along with a phrase 'unless otherwise provided. . . .' WYO. STAT. ANN. § 17-36.29 (1965). Arguably, then, any percentage will do if the articles so state. However, since this statute is simply the Model Act language with the final clause preserving a minimum quorum of one-third, it looks rather as if the draftsmen wished to authorize super-statutory quorums ('unless otherwise provided') but bar less-

ed this is doubtful, and it represents an area deserving of clarification.

A strong argument can be made for limits on corporate flexibility in this area, whether the corporation is closely or broadly held. Since the promoters and founders of a corporation are ordinarily in control of the drafting of the articles and by-laws, which are rarely if ever read by later investors in the company, the legislature might consider a minimum quorum provision such as that currently provided in the Model Act—the holders of not less than one-third of the outstanding shares entitled to vote at the meeting.[101] Such a provision would prevent a controlling "insider" group from calling shareholder meetings on short notice at inconvenient times in order to guarantee its own control. While the likelihood of such an abuse seems remote, it can readily be prevented by adopting the provisions of the Model Business Corporation Act, which have not met with resistance eleswhere.

Voting Agreements

Where shareholders have divided into two unfriendly camps, it may be necessary for the members of each group to enter into agreements concerning voting for directors, in order to preserve their proportionate representation on the board. If each member of the group simply votes for the candidates he prefers individually, without coordination with his allies, the result may be minority control of the board.[102] Under these circumstances, an enforceable voting agreement,

than-statutory quorums. For an explicit provision, *see* S.C. CODE ANN. § 12-16.8(a) (Supp. 1965).
Id.

101. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 32 (2d ed. 1971).
102. An example of this problem is found in the famous case of Ringling Bros.-Barnum & Bailey Combined Shows v. Ringling, 29 Del. Ch. 610, 53 A.2d 441 (Sup. Ct. 1947). In that case Mrs. Ringling and Mrs. Haley each owned 315 shares, while North owned 370 shares, that being all of the outstanding stock. There were seven directorships to fill annually. If Ringling & Haley combined their votes, they could elect five members of the board. If each of them voted her 315 shares for seven separate candidates, none of them mutually agreed upon, then 14 candidates would each receive 315 votes. Under the cumulative voting system in effect for the corporation, North had 370 shares times 7 directorships, or 2590 votes. If North were to spread these votes over 6 candidates, he could cast at least 431 votes for each, and elect 6 of the 7 directors.

by which the shareholders in each group agree to pool their votes, becomes an absolute necessity.

Problems arise in this area if the agreement fails to grant irrevocable proxies coupled with an interest, for a court may refuse to imply such a proxy and fail to decree how the shares should be voted.[103] On the other hand, if the proxy is too effective, or exists too much of the time, courts may find an illegal voting trust, and refuse to enforce the agreement.[104] The Model Act solves the illegal voting trust problem,[105] as does Wyoming's Act.[106] The Model Act does not attempt to deal with the enforcement problems created by Delaware cases holding that absent the express grant of a proxy to vote shares in accordance with the voting agreement, no such power exists by implication in the other parties to the agreement.[107] Absent the express grant of such a power, the Delaware Supreme Court has held that its only power is to declare that there has been a breach of contract among the shareholders, and invalidate the votes cast in violation of the contract.[108] This determination may leave the objecting shareholder in a worse position than before, since part of the votes of his group are then cancelled entirely,

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103. Ringling Bros.-Barnum & Bailey Combined Shows v. Ringling, *supra* note 102.

104. Abercrombie v. Davies, 36 Del. Ch. 371, 130 A.2d 338 (Sup. Ct. 1957).

105. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 34 (2d ed. 1971) provides: Agreements among shareholders regarding the voting of their shares shall be valid and enforceable in accordance with their terms. Such agreements shall not be subject to the provisions of this section regarding voting trusts.

106. The Wyoming Act provides:

> A written contract between two or more shareholders concerning the manner in which the parties shall vote their shares for the election of directors or on other matters requiring shareholder action under the provisions of this act or the articles of incorporation shall be valid and enforceable. In an action by a shareholder who is a party to such an agreement a court of competent jurisdiction may enjoin another party or parties to such agreement from voting his or their shares in violation thereof, and the court may, in an action to which the corporation is a party, by appropriate decree set aside an election of directors or other action resulting from the voting of shares in violation of such agreement, and in addition the court may grant such other or further relief as is appropriate under the circumstances for the enforcement of such agreement. WYO. STAT. § 17-36.31 (1965).

107. Ringling Bros.-Barnum & Bailey Combined Shows v. Ringling, *supra* note 102.

108. *Id.*

leaving the opposition with proportionately greater voting power.[109]

The drafters of the 1961 Wyoming provisions attempted to deal with the enforcement provisions, without creating a proxy in the hands of the parties to the agreement unless such a power was expressly granted by the agreement. Rather than simply invalidate votes cast in breach of such an agreement, Section 31 gives the court power to set aside an election where votes are miscast, to enjoin shareholders from voting in violation of their agreement, and to "grant such other or further relief as is appropriate under the circumstances . . . ."[110] Does this language, which probably does no more than codify the inherent powers of a court in equity, allow a court to order a shareholder to vote his shares affirmatively in a manner specified by the court? Delaware courts would apparently take the negative on this issue.[111] The commentary of the committee head who partiticipated in the drafting is silent on this matter.[112] Nevertheless, Wyoming's grant of enforcement power is at once more specific and broader than that of any other state, and has been complimented as being a "particularly valuable addition in this area."[113] The problem still arises, however, whether a court can decree specific performance absent an express grant of a proxy to someone, in view of the doctrine that a shareholder has a right not to vote.[114]

The problem, then, is whether the Act fully provides for effective affirmative relief where the drafters have either neglected to provide for an irrevocable proxy, or where a court fails to find a sufficient interest coupled with the proxy to support irrevocability. It is doubtful whether the mutual promises of the shareholders will be enough, and

109. *Id.* By cancelling miscast votes, the court left the dominant shareholder group with only one-half of the directors, rather than the majority it would have had if the shares were voted pursuant to the agreement.
110. WYO. STAT. § 17-36.31 *supra* note 106 (1965).
111. Ringling Bros.-Barnum & Bailey Combined Shows v. Ringling, *supra* note 102.
112. Rudolph, *supra* note 2.
113. Folk, *supra* note 99, at 926.
114. In *Ringling Bros.*, the Delaware Supreme court noted that "The ownership of voting stock imposes no legal duty to vote at all." Ringling Bros.-Barnum & Bailey Combined Shows v. Ringling, *supra* note 102, at 447.

many drafters, despite the *Ringling* case, are likely to neglect reference to the problem. The court could be granted the power to enforce through specific performance, in the hope that this would leave sufficient room for interpretation of the agreement where it was clear the parties did not want to grant power to vote their shares to someone else, or intended to leave damages as the only remedy.

Voting Trusts

Because of early judicial hostility to the voting trust, legislation, including the Model Act, reflecting this hostility, has severely limited the usefulness of the voting trust by imposing a ten year time limit on such trusts.[115] Wyoming adopted the Model Act provisions in effect at the time without alteration.[116] As a result, many attorneys have found other devices, such as share classification and voting agreements, more useful. The lives of such arrangements are not limited, and they provide a method of controlling the corporation for the lives of the participating shareholders, if this is desirable.[117] The utility of these alternatives may be reflected in the lack of major changes in the Model Act provisions relating to voting trusts. One of the few changes which has been made since Wyoming adopted its Act is a sentence which obligates the trustee to keep records of the number and class of shares deposited by each certificate holder.[118] Statutory provisions dealing with voting trusts are generally notable not so much for what they do as for their omissions. For

115. WYO. STAT. § 17-36.31 (1965); 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 32 (1960).
116. WYO. STAT. § 17-36.31 (1965); 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 32 (1960).
117. The second paragraph of Section 17-36.31 of the Wyoming Statutes (1965) expressly authorizes voting agreements and makes them enforceable. How enforceable depends on, as discussed *supra*, text at notes 102-14, whether the Wyoming Courts adopt the approach of the Delaware Supreme Court in *Ringling Bros.* (Ringling-Bros.-Barnum & Bailey Combined Shows v. Ringling, *supra* note 102), which held that in the absence of a proxy, a voting agreement provided no enforcement device; or the far more sympathetic approach of the Illinois Supreme Court, which granted specific performance without concerning itself with the problem of whether proxies existed. Galler v. Galler, 32 Ill.2d 16, 203 N.E.2d 577 (1964). The usefulness of share classifications as a control device is illustrated in Lehrman (Lehrman v. Cohen, 222 A.2d 800 (Del. Sup. Ct. 1966)). Sympathetic courts impose no arbitrary time limits on such agreements, as can be seen in the *Galler* case, in which the court implied a limitation based on the lives of the stockholders who signed the agreement.
118. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 34 (2d ed. 1971).

example, do certificate holders have the same right as shareholders to inspect corporate books and records? The present Wyoming Act is silent on this question, and one doubts, if the corporation is not a party, whether it is possible to create such rights in the voting trust agreement itself.[119] The Model Act provisions relating to inspection of books and records have been modernized to provide the same rights of inspection for the holders of voting trust certificates.[120] Few states have gone beyond the Model Act provisions. Delaware and New York allow for extensions of voting trusts beyond the ten year limitation, with the qualification that such extensions only bind those certificate holders who consent to the extension.[121] California, on the other hand, formerly provided for early termination by a vote of the majority in interest of the voting trust certificate holders, a device which drastically limited the usefulness of the voting trust.[122]

Perhaps the most severe problems lie in two areas. First is the ability of the voting trustee to abuse his fiduciary duties by self-dealing transactions to lock the trustee into a lucrative management position and avoid liability. Second is the question whether the voting trustee, in the absence of provisions in the trust agreement, can vote on matters concerning organic corporate changes which are specifically reserved to the stockholders rather than the directors in the Business Corporation Act.[123]

Voting trust agreements will often be drafted on behalf of a dominant stockholder who wishes to become the trustee, or by the attorneys for the trustee if the trustee is to be a third party. It is only natural and human for the drafters to obtain as much protection as possible for the trustee, including exculpatory language which tends to protect him against negligence, and in some cases may go even further. The authorities uniformly concede the validity of agreements

119. The Wyoming Act grants rights of inspection only to "a shareholder of record" who meets certain requirements. WYO. STAT. § 17-36.44 (1965).
120. 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 52 (2d ed. 1971).
121. N.Y. BUS. CORP. LAW § 621(d) (McKinney 1963); DEL. CODE ANN. tit. 8, § 218(b) (1974).
122. CAL. CORP. CODE § 2231 (West 1955). This provision was repealed by the new CAL. CORP. CODE § 706 (Supp. 1976).
123. *See* notes 93-96, *supra*.

which exculpate a trustee from negligence,[124] but the cases are also in general agreement that a trust agreement may not exculpate against gross negligence or fraud.[125] To the extent such language is obtained by the force of will of a dominant shareholder who is becoming the trustee, it is probably unenforceable.[126] Other unresolved questions are whether it is a breach of a trustee's duty to become a director or officer of the corporation, or to take compensation from the corporation beyond that expressly provided for in the trust instrument. At least one author recommends prohibition of a trustee serving in such dual capacities.[127] In a closely held corporation this may not be what the participants have in mind, especially if the trustee is a shareholder. His business experience and acumen may be essential to the success of the enterprise. An approach more consistent with the philosophy of modern business corporation statutes would be to prohibit such dual capacities unless otherwise provided in the trust agreement.

A separate problem involves removal of a voting trustee-director for breach of his duties as a director. As long as the voting trust cannot be terminated for a fixed period of time, the trustee is in a position to assure his own election to office, even when this act is against the best interests of the corporation. Since reserving the right of removal to the holders of the voting trust certificates as well as the shareholders provides a method for destroying the binding nature of the voting trust, a more balanced approach might be to provide for removal of voting trustees as directors for cause

124. BOGERT, TRUSTS & TRUSTEES § 542 (2d ed. 1960); 3 SCOTT, THE LAW OF TRUSTS § 222 (3d ed. 1967); NEWMAN, TRUSTS 433 (2d ed. 1955) and RESTATEMENT (SECOND) OF TRUSTS § 222 (1959). *But see* N.Y. EST., POWERS & TRUSTS § 125 (McKinney 1967).

125. *See, e.g.*, Tuttle v. Gilmore, 36 N.J. Eq. (9 Stew.) 617 (Ct. Err. App. 1883) (the leading case describing what is a "willful" default); RESTATEMENT (SECOND) OF TRUSTS § 222(2) (1959) and Payne *Exculpatory Clauses in Corporate Mortgages and other Instruments*, 19 CORNELL L.Q. 171, 191 (1934).

126. RESTATEMENT (SECOND) OF TRUSTS § 222(3) (1959) provides: "To the extent to which a provision relieving the trustee of liability for breaches of trust is inserted in the trust instrument as the result of an abuse by the trustee of a fiduciary or confidential relationship to the settlor such provision is ineffective."

127. Ballantine, *Voting Trusts, Their Abuses and Regulation*, 21 TEX. L. REV. 139, 166 (1942) and Burke, *Voting Trusts Currently Observed*, 24 MINN. L. REV. 347, 375 (1940).

by a court sitting in equity. Guidance in this complex area might be obtained from such sources as the Trust Indenture Act[128] and the Investment Company Act,[129] both of which attempt to regulate fiduciary duties in the corporate area.

The Wyoming Act expressly allocates to the shareholders the power to control a number of major corporate decisions, other than election of directors, including decisions concerning amendments of articles of incorporation,[130] approval of plans of merger or consolidation,[131] approval of the sale of all or substantially all of the assets not in the ordinary course of business[132] and dissolution.[133] Should a broad grant of power to the trustee, which is silent on these votes, be treated as a grant to the trustees of the basic power to make all these decisions? Again the prudent approach may be to provide that unless otherwise provided in the trust agreement itself, these votes shall be cast by the certificate holders. Such an approach would again attempt to balance the need for flexibility in drafting and planning with the need for some protection against overreaching.

128. Trust Indenture Act of 1939, 15 U.S.C. § 77aaa *et seq.* (1970). Generally, the Act recognizes that where securities are issued under an indenture of trust, with a third party serving as trustee to represent the securities holders, the terms of the indenture are negotiated between the issuer and the trustee without representation of the prospective security holders. The fear of Congress was that in such cases the terms of the indenture would be unfair to investors, and consequently Congress required registration of the securities offered under the indenture and SEC review to determine that both the trustee and the indenture are eligible and qualified. Trustees with conflicts of interest are disqualified under Section 310(b) of the Trust Indenture Act (15 U.S.C. § 77jjj(b) (1970)) both at the inception and during the life of the indenture. Trustees are disqualified if they are trustees under another indenture, or if they are in control of or controlled by the obligor, to name several grounds. 15 U.S.C. § 77jjj(b) (1) and (2) (1970). In the event such disqualification occurs during the life of the indenture, the trustee must, within 90 days, either eliminate the conflict or resign, or, if it chooses to do neither, notify the security holders of this fact, in which case any security holder may petition a court for removal and replacement of the trustee. The Act also contains provisions concerning the financial responsibility of trustees.

129. Investment Company Act of 1940, 15 U.S.C. § 80a *et seq.* (1970). The Act requires that contracts with investment advisers must be approved by a majority of the disinterested directors (15 U.S.C. § 80a-15(c) (1970)), provides for removal of trustees of investment trusts by vote of the holders of certificates of beneficial interest in the trust (15 U.S.C. § 80a-16(c) 1970)) and prohibits certain exculpatory provisions relieving officers, directors or investment advisers from liability (15 U.S.C. § 80a-17(h) to -17(i) (1970)).

130. WYO. STAT. § 17-36.52 (1965).

131. WYO. STAT. § 17-36.65 (1965).

132. WYO. STAT. § 17-36.70 (1965).

133. WYO. STAT. § 17-36.75 (1965).

The Delaware Act contains a provision for resolving disputes among co-trustees. In the event that they are unable to agree and the trust agreement does not itself contain a provision for resolution, the votes will be cast according to the majority decision, or in the event of an equal division, the votes will be divided among the trustees equally.[134] The addition of such provisions to the Wyoming Act could anticipate and avoid disputes which might paralyze voting trusts, disenfranchise the trustees and frustrate the purposes of the certificate holders.

DIRECTORS

Much of the foregoing has focused on the need for legislation flexible enough to accommodate the variety of contractual arrangements which may be desired by participants in the closely held enterprise. Such laws presume carefully structured allocations of power designed to protect the respective interests of the participants. When we turn to legislation governing directors in such enterprises, the focus shifts from accommodating conscious contract arrangements to protecting the participants from innocent oversights and arrangements which violate formalistic requirements of corporation law. Participants in closely held corporations often ignore the distinction between directors, shareholders and officers; fail to hold meetings, or to keep adequate records. Every attorney has seen records of such enterprises which end with the organizational meeting shortly after incorporation.

Formal Action by Directors and Shareholders

Participants in closely held corporations frequently serve three functions, as shareholders, officers and directors. In such cases there is considerable likelihood that casual conversations among all of the owners will replace formal meetings of the board of directors and shareholders. This mode of action creates considerable uncertainty for the corporation, since the courts often seem free to hold either that the

134. DEL. CODE ANN. tit. 8, § 218(a) (1974).

action was not authorized by the full board of directors at a proper meeting,[135] or that such formal action is unnecessary, largely because of equitable considerations.[136] Section 121 of the Wyoming Act adopts the Model Act approach, authorizing informal action either by shareholders or directors when it is accomplished by unanimous consent.[137] While the provision is a modern one which recognizes the reality of corporate informality, the question remains whether it goes far enough. Both for shareholders and directors, the written consent must be unanimous. Delaware goes one step further, authorizing informal action by shareholders when the consent to the action is signed by shareholders holding a sufficient number of shares to take the action at any meeting.[138] For directors, Delaware, like Wyoming, requires unanimous consent.[139] The justification for this distinction may be that the board of directors is regarded as a deliberative body, while the shareholders are not. Obviously the necessity for deliberation disappears only when all of the directors are in agreement, and so long as one director dissents from a proposed course of action, the theory of both Acts seems to be that a director should have an opportunity to persuade fellow directors. Where shareholders and directors are identical, this type of distinction becomes meaningless. Indeed, under the Delaware Act, where a close corporation is formed and the shareholders take over the functions of directors, it seems to be obliterated by the close corporation provisions of that Act.[140] North Carolina recognizes the practice of irregular directors' meetings with a statute which specifically validates actions which are either consented to in writing unanimously by all of the directors, known to all of the shareholders, who do not object, or customarily taken by directors who act informally.[141]

135. Hurley v. Ornsteen, 311 Mass. 477, 42 N.E.2d 273 (1942); Baldwin v. Canfield, 26 Minn. 43, 1 N.W. 263 (1879).
136. *See, e.g.*, Sherman v. Fitch, 98 Mass. 59 (1867).
137. WYO. STAT. § 17-36.121 (1965).
138. DEL. CODE ANN. tit. 8, § 228(a) (1974).
139. DEL. CODE ANN. tit. 8, § 141(f) (1974).
140. DEL. CODE ANN. tit. 8, §§ 341-356 (1974). *See also* TEX. BUS. CORP. ACT ANN. art. 2.30-1 to -5 (Vernon Supp. 1976).
141. N.C. GEN. STAT. § 55-29(a) (1973) provides:

Informal or Irregular Action by Directors of Committees.

(a) Action taken by the required majority of the directors or

The Perils of Informality—The "Alter Ego" Doctrine

Some courts still hold that informal director actions taken by means other than those expressly authorized in the corporation act are not valid acts of the board. It is possible that these same courts may hold in such cases that the directors, especially when they are identical with the shareholders of the corporation, are said to be acting individually as owners of the business, and in effect, are acting as a partnership.[142] In the imprecise language of some of the cases, the corporation is said only to be the "alter ego" of the individual owners of the enterprise, which they are really operating in their individual capacities, as partners. This raises the specter of unlimited personal liability for the shareholder-directors.[143] The consequences, it is submitted, are far too drastic in relation to the "wrong," if any, which was committed in failing to observe the corporate formalities. The evil may in fact be encouraged by the unanimous consent provisions of the present Act,[144] since once the directors learn that they need not hold meetings if they all consent in writing, they are even more likely to disregard the need for meetings, and may conclude that their attorney can draw up the appropriate documents after the fact, if they are ever needed. They may also extend the reasoning that if unanimous consent in writing is sufficient in lieu of a meeting, majority consent must also be sufficient, since only majority action is required at a meeting.

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members of a committee without a meeting is nevertheless board or committee action if:

(1) Written consent to the action in question is signed by all the directors or members of the committee, as the case may be, and filed with the minutes of the proceedings of the board or committee, whether done before or after the action so taken, or if

(2) All the shareholders know of the action in question and make no prompt objection thereto, or if

(3) The directors or committee members are accustomed to take informal action and this custom is generally known to the shareholders and if all the directors or committee members, as the case may be, know of the action in question and no director or committee member makes prompt objection thereto.

142. See Walkovszky v. Carlton, 29 App. Div.2d 763, 287 N.Y.S.2d 546 (1968). In *Minton v. Cavaney,* Justice Traynor stretched the doctrine to include any case where the corporation was undercapitalized and the owners participate actively in the conduct of corporate affairs. Minton v. Cavaney, *supra* note 21. Also *see* WYO. STAT. § 17-36.122 (1965).

143. Minton v. Cavaney, *supra* note 21; WYO. STAT. § 17-36.122 (1965).

144. WYO. STAT. § 17-36.121 (1965).

The question is whether a corporation act should attempt to protect director-shareholders if they should act in this fashion, or leave them to the present consequences of ignoring the forms. Delaware's close corporation provisions, in addition to allowing shareholders to act in writing by less than unanimous consent,[145] expressly validate agreements by shareholders of such corporations which otherwise might be invalid as attempting to treat the corporation as a partnership.[146] Agreements restricting the discretion of directors of close corporations are also validated.[147] Thus Delaware, without abrogating the "alter ego" doctrine, has gone a long way in that direction by validating acts which otherwise would not be treated as corporate acts. Presumably if shareholders attempt to use a thinly capitalized corporation as a shield for operating a personal business, the "alter ego" doctrine will remain available, but it should not catch innocent parties who inadvertently act in violation of the present formal requirements.

Voting Requirements

Section 36 of the Wyoming Act expressly authorizes quorum requirements greater than a majority of the board of directors if provided in the articles of incorporation or the by-laws. It also provides that while the general rule is that action by a majority of a quorum shall be that of the board of directors, a higher vote may be required by the articles of incorporation or the by-laws.[148] Since the statute does not impose any upper limit, there is no reason to think that unanimous voting requirements may not be imposed. It is worth noting that the statute allows only an *increase* in the voting and quorum requirements for directors. This contrasts with the provisions relating to quorum requirements for shareholders, which seem to allow quorums to be either more or less than a majority of the shares, but, as in the provisions on director voting, allow the articles or by-laws of the corporation to set a voting requirement larger than the holders

145. DEL. CODE ANN. tit. 8, § 228(a) (1974).
146. DEL. CODE ANN. tit. 8, § 354 (1974).
147. DEL. CODE ANN. tit. 8, § 350 (1974).
148. WYO. STAT. § 17-36.36 (1965).

of a majority of the shares present.[149] If unanimous voting requirements are permissible, certainty could be gained by an express provision to that effect.

Director Conflicts of Interest

In the closely held corporation director conflicts of interest are a frequent fact of life. The Wyoming Act is silent on the validity of transactions involving interested directors, leaving the matter to common law. In other jurisdictions there has been a progressive liberalization in this area, moving away from the original theory that all contracts involving a director dealing with his own corporation were voidable, without regard to fairness or the participation of the interested director in the decision.[150] Courts, moving from this rigid rule, have employed a variety of approaches. Some require approval by a disinterested majority of the board, without counting the interested directors for purposes of determining a quorum.[151] More recently, the judicial trend has been toward approving contracts which were fair to the corporation, regardless of whether approved by a disinterested majority of the board, or whether a quorum of such members was present.[152] While the Wyoming case law is sparse and the discussion in the only case is less than satisfactory, this may already be the rule in Wyoming.[153] The difficulty with the only decision in this area is its failure to directly discuss the quorum problem or the requirement of approval by a disinterested majority of the board. The facts indicated that neither a disinterested quorum was present nor was the transaction approved by a disinterested majority. However, the case was poorly pleaded, and the comforting language of the Wyoming court in this area may be suspect at this date.[154]

149. WYO. STAT. § 17-36.29 (1965).
150. Marsh, *Are Directors Trustees? Conflict of Interest and Corporate Morality*, 22 BUS. LAW 35, 36 (1966).
151. *Id.* at 39.
152. *Id.* at 43.
153. Smith v. Stone, 21 Wyo. 62, 128 P. 612 (1912).
154. The Court stated:

> The fact that two corporations are controlled by the same officers or stockholders does not prevent them from dealing with each other or the purchase by one of the property of the other, unless the acts of the majority in control are fraudulent as against the corporation and the complaining

The present version of the Model Act has attempted to deal with these problems specifically. It provides that interested directors may be counted for purposes of determining the presence of a quorum, and ratifies such contracts if fair, the relationship is disclosed, and the transaction approved by a majority of a quorum of the board, without counting the votes of interested directors.[155] If it is impossible to obtain such consent from the board, the transaction may be submitted to the shareholders for ratification.[156] In the absence of shareholder ratification, the contract will not be voidable if it is fair and reasonable to the corporation.[157] This revision adopts the rule which is implicit in *Smith v. Stone*,[158] and would clarify an area which has been the subject of all too much doubt.

Directors' Liabilities

The problem of the standard of care of directors and their liabilities for failure to live up to that standard has been left largely to common law development. Stated generally, the standard required is that of a prudent man caring for his own affairs.[159] The rule has been somewhat modified to reflect the fact that not all directors are as able as all others. In one case, for example, Judge Learned Hand stated expressly that he would not hold the director liable simply because he was inexperienced at the particular business, since that was the responsibility of the shareholders who selected him.[160] Courts have further protected directors from

stockholders. [Citation omitted] The courts will closely scrutinize a sale of corporate property effected by majority stockholders to another corporation which they control or are interested in. Such a sale is not void or constructively fraudulent.

128 P. 612, 617.

155. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 41(a) (2d ed. 1971).
156. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 41(b) (2d ed. 1971).
157. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 41(c) (2d ed. 1971).
158. *Supra* note 153.
159. Hun v. Cary, 82 N.Y. 65 (1880).
160. In *Barnes v. Andrews*, Judge Hand stated:

> True, he was not very well-suited by experience for the job he had undertaken, but I cannot hold him on that account. After all, it is the same corporation that chose him which now seeks to charge him. I cannot agree with the language of Hun v. Cary, supra, that in effect he gave an implied warranty of any special fitness. Directors are not specialists, like lawyers or doctors. They must have good sense, perhaps they must have acquaintance with affairs; but they need not—indeed, perhaps they should not—have any technical talent. They are the general advisers of the business,

their mistakes with the "business judgment" rule, which in essence holds that directors will not be held liable for mistakes honestly made.[161] The result has been that there are very few cases holding directors who attend to business and who commit no fraud liable for lack of care.[162]

Nevertheless, directors are forced to make business decisions of major magnitude, which they fear may expose them to liability for good faith mistakes. The Wyoming Act, like the Model Act of its time, provides for director liability to the corporation for illegal distributions of corporate assets—whether in the form of excessive dividends, share repurchases, or a liquidating distribution.[163] Even so, such directors are excused if they rely in good faith upon financial statements presented by the appropriate corporate officers or by independent certified public accountants.[164] The Act expressly provides a method for dissenting from illegal board actions.[165] While the Wyoming Act provides that such directors may obtain contribution from other culpable directors as well as receiving shareholders,[166] its provisions on indemnification are quite limited.

> and if they faithfully give such ability as they have to their charge, it would not be lawful to hold them liable. Must a director guarantee that his judgment is good? Can shareholders call him to account for deficiencies which their votes assured him did not disqualify him for his office?

Barnes v. Andrews, 298 F. 614, 618 (S.D.N.Y. 1924).

161. Fletcher, *supra* note 36, § 1039; HENN, LAW OF CORPORATIONS § 242 (2d ed. 1970); Simon v. Socony-Vacuum Oil Co., 179 Misc. 202, 38 N.Y.S.2d 270 (Sup. Ct. 1942), *aff'd*, 267 App. Div. 890, 47 N.Y.S.2d 589 (1944).

162. Professor Bishop states:

> The search for cases in which directors in industrial corporations have been held liable in derivative suits for negligence uncomplicated by self-dealing is a search for a very small number of needles in a very large haystack. Few are the cases in which the stockholders do not allege conflict of interest, still fewer those among them which achieve even such partial success as denial of the defendant's motion to dismiss the complaint. Still, it can not be denied that there is a small number of relatively recent cases which do seem to lend a modicum of substance to the fears of directors of industrial or mercantile corporations that they may be struck for what they like to call 'mere' or 'honest' negligence. My own collection, based on extensive (although not exhaustive) investigation includes four such specimens. Bishop, *Sitting Ducks and Decoy Ducks: New Trends in Indemnification of Corporate Directors and Officers*, 77 YALE L.J. 1078, 1099 (1968).

163. WYO. STAT. § 17-36.41(a)-(c) (1965).

164. WYO. STAT. § 17-36.41 (1965).

165. WYO. STAT. § 17-36.41 (1965).

166. WYO. STAT. § 17-36.41 (1965).

The Wyoming Act remains identical to the current Model Act on director's liability, but falls well behind in indemnification.[167] Wyoming limits indemnification to officers and directors for expenses "actually and reasonably incurred by him in connection with the defense of any action . . . except in relation to matters as to which he shall be adjudged in such action, suit or proceeding to be liable for negligence or misconduct in the performance of duty. . . ."[168] After setting such a limited standard, the Act also authorizes corporations to "make any other indemnification that shall be authorized by articles of incorporation or by any by-law or resolution adopted by the shareholders after notice."[169]

A major shift took place with the 1967 revision of the Delaware Act,[170] and the virtually identical revision of the Model Act at that time.[171] While the Wyoming Act leaves in doubt the ability of the corporation to go beyond these limitations as to fault and liability, such provisions have not prevented lawyers in other jurisdictions faced with similar statutes from adopting broader indemnification language. The author's own experience under a similar provision in the Colorado version of the Model Act[172] indicated that many lawyers were willing to advise clients to adopt indemnification provisions as broad as or broader than those in the Delaware and current Model Acts.

Statutes such as the Wyoming Act and the former Colorado Act leave considerable doubt about the public policy limitations which a court might impose on such language in corporate documents, especially where the complaining shareholder was not a party to its adoption. Current Model Act provisions with respect to indemnification no longer limit it to matters where the director is judged not to be liable for negligence or misconduct. Section 5(a) of the Model Act

167. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 5 (2d ed. 1971).
168. WYO. STAT. § 17 36.4(o) (1965).
169. WYO. STAT. § 17-36.4(o) (1965).
170. DEL. CODE ANN. tit. 8, § 145 (1974). *See* Sebring, *Recent Legislative Changes in the Indemnification of Directors, Officers and Others*, 23 BUS. LAW. 94 (1967).
171. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 5 (2d ed. 1971).
172. COLO. REV. STAT. § 31-2-1(15) (1973).

now includes not only expenses of litigation, but "judgments, fines, and amounts paid in settlement" if the director "acted in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the corporation."[173] That Act now covers derivative suits, a matter not discussed in the Wyoming version. Even where the director is found liable for negligence or misconduct, he may still be indemnified if the court determines that he is fairly and reasonably entitled to indemnity.[174] This leaves the matter entirely to the judgment and discretion of the court.

The current Model Act goes further—it gives the director who is successful in defending such actions an absolute right to indemnification, so that he is not dependent upon language in articles or by-laws, or the good will of the other directors or shareholders.[175] This may be particularly important where a director not protected by preexisting provisions in the articles or by-laws uses his best judgment and goes against the wishes of the majority or controlling shareholders, and then must look to those persons for indemnification. The present Model Act expressly authorizes indemnification in addition to that provided by the Act,[176] and authorizes the furnishing of liability insurance for directors and officers.[177] The language goes far to eliminate current doubts about the power and legality of corporate indemnification, while essentially preserving the exposure of directors to liability for acts which are willful or fraudulent.

While authorization of such broad indemnification may be subject to attack when applied to publicly held companies,[178] there is little evidence of actual abuse, and little likelihood that insurers will write policies designed to encourage director abuses. On the other hand, broadening of indemnification and insurance provisions may enhance the likelihood

173. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 5(a) (2d ed. 1971).
174. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 5(b) (2d ed. 1971).
175. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 5(c) (2d ed. 1971). Also *see* DEL. CODE ANN. tit. 8, § 145(c) (1974).
176. ABA-ALI MODEL BUS. CORP. ACT ANN. § 5(f) (2d ed. 1971). Also *see* DEL. CODE ANN. tit. 8, § 145(f) (1974).
177. ABA-ALI MODEL BUS. CORP. ACT ANN. § 5(g) (2d ed. 1971). Also *see* DEL. CODE ANN. tit. 8, § 145(g) (1974).
178. NADER, GREEN & SELIGMAN, *supra* note 11, at 66.

that responsible outsiders will participate on the boards of closely held companies.

Removal of Directors

One of the most glaring omissions in the Wyoming Act concerns removal of directors, either with or without cause, by the shareholders. The only hint in the present statute is that "at the first annual meeting of shareholders and at each annual meeting thereafter the shareholders shall elect directors to hold office until the next succeeding annual meeting. Each director shall hold office for the term for which he is elected and until his successor shall have been elected and qualified."[179] At the time of the adoption of the Business Corporation Act in 1961,[180] the version of the Model Act most commonly in use was the 1953 revision, printed in 1957,[181] which was also silent on the question of removal. The 1959 revision, which added an optional Section 36A on removal,[182] was not printed until 1960 and was not generally available until 1961.[183]

The silence of the Wyoming Act on the question of removal was not unusual at the time of its adoption. The Delaware Act was also silent.[184] Indeed, during the 1950's the

179. WYO. STAT. § 17-36.34 (1965).
180. 1961 Wyo. Sess. Laws ch. 85 (effective July 1, 1961).
181. ABA-ALI MODEL BUS. CORP. ACT (1957).
182. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 36A (1960) provides as follows:

> At a meeting called expressly for that purpose, directors may be removed in the manner provided in this section. The entire board of directors may be removed, with or without cause, by a vote of the holders of a majority of the shares then entitled to vote at an election of directors. If less than the entire board is to be removed, no one of the directors may be removed if the votes cast against his removal would be sufficient to elect him if then cumulatively voted at an election of the entire board of directors, or, if there be classes of directors, at an election of the class of directors of which he is a part.
>
> Whenever the holders of the shares of any class are entitled to elect one or more directors by the provisions of the articles of incorporation, the provisions of this section shall apply, in respect of the removal of a director or directors so elected, to the vote of the holders of the outstanding shares of that class and not to the vote of the outstanding shares as a whole.

183. ABA-ALI MODEL BUS. CORP. ACT ANN. (1960). The copy of this three volume work in the library of the University of Wyoming College of Law contains a notation that it was received February 27, 1961. A paperback edition, HANDBOOK A, ABA-ALI MODEL BUS. CORP. ACT (1961), indicates that the 1960 edition was printed in December. ABA-ALI MODEL BUS. CORP. ACT xii (1961).
184. DEL. CODE ANN. tit. 8, § 101 *et seq.* (1974).

courts were struggling with whether shareholders, in the absence of a specific statutory authorization, had authority to remove a director for cause—a reflection of the ambivalence of the law of the time on whether directors were merely agents of the shareholders, and thus subject to termination of the agency relationship, or held some status as fiduciaries which gave them greater tenure than ordinary agents. The case law during the 1950's seemed to hold that a director could be removed for cause, although many of the opinions were careful to state that some semblance of due process must be observed—that the director must be given notice of the charges against him and an opportunity to defend.[185]

The cases now seem generally in agreement that every corporation has the power to remove a director for cause.[186] The strictures of recent cases that notice of charges must be given and an opportunity for the director to respond to the charges seem highly unrealistic in the light of proxy voting and the fact that the removal attempt will probably be the result of a struggle between two factions for power. If some semblance of due process is to be observed in the removal procedures, does this mean that "interested" stockholders must disqualify themselves from voting? A rule such as this would conflict with statutory provisions granting shareholders the right to vote. The real questions are whether the statute should recognize the presently questioned right of shareholders to remove a director without cause,[187] and if

185. Auer v. Dressel, 306 N.Y. 427, 118 N.E.2d 590 (1954) and Campbell v. Loew's, Inc., *supra* note 184. These are leading cases establishing the power of the shareholders to remove a director from office during his term for cause. Also *see* Abberger v. Kulp, 156 Misc. 210, 281 N.Y.S. 373 (Sup. Ct. 1935); Toledo Traction, Light & Power Co. v. Smith, 205 F. 643 (N.D. Ohio 1913). These early cases did not focus directly on the question of destroying the right of cumulative voting, although the opinion in *Campbell v. Loew's* notes the danger of destruction of cumulative voting, stating: "And it is certainly evident that if not carefully supervised the existence of a power in the stockholders to remove a director even for cause could be abused and used to defeat cumulative voting." Campbell v. Loew's, Inc., *supra* note 184, at 858. Also *see*, FLETCHER, *supra* note 36, §§ 351-358.

186. 2 FLETCHER, *supra* note 36, § 351 and cases cited in note 185, *supra;* 1 O'NEAL, *supra* note 10, § 3.59.

187. Everett v. Transnation Development Corp., 267 A.2d 627 (Del. Ch. 1970) held that in the absence of cumulative voting a by-law authorizing removal of a director by the shareholders without cause was valid, and not in conflict with Delaware corporation law. To date no Delaware case has dealt with this problem where cumulative voting exists. Cumulative voting is optional, not mandatory under the Delaware Act. DEL. CODE ANN. tit. 8, § 214 (1974). Also *see* O'Neal, *supra* note 2.

removal without cause is to be allowed, what protection should be granted to directors elected by cumulative voting, to make certain that the majority does not remove a director elected cumulatively, thus destroying the minority shareholder's right. The current version of the Model Act suggests a solution which seems workable and realistic.[188] It allows removal with or without cause, but safeguards minority rights by providing that if the votes cast against removal would have been sufficient to elect the director if cast cumulatively at a regular election, the director may not be removed.[189]

Shareholder Control: Selection and Removal of Officers

In the typical closely held enterprise, the shareholders are active participants, and are deeply concerned over the way in which control is allocated among them. This concern extends to the amount of money taken out of the business, and the form in which it is taken. To shareholders active in operating their own business, it is often the total amount of dollars taken out by each participant which is crucial, rather than distinctions between salaries, dividends and the like. Officers' salaries are frequently a large share of the cash withdrawn by the owners.[190] The attorney for the closely held enterprise must implement the desires of the prospective shareholders for participation in management as officers as well as directors, and must assure that the arrangements are enforceable.

Shareholders may wish to retain the power to elect and remove officers as well as directors of the corporation. Attempts to achieve this through the articles or by-laws are likely to be frustrated in Wyoming by the provisions of Sec-

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188. 1 ABA-ALI MODEL BUS. CORP. ACT ANN. § 39 (2d ed. 1971).

189. 1 ABA-ALI MODEL BUS. CORP. ACT § 39 (2d ed. 1971). The second paragraph of section 39 provides:

> In the case of a corporation having cumulative voting, if less than the entire board is to be removed, no one of the directors may be removed if the votes cast against his removal would be sufficient to elect him if then cumulatively voted at an election of the entire board of directors, or, if there be classes of directors, at an election of the class of directors of which he is a part.

190. This article will not deal with tax problems, such as when salary payments may be treated as the equivalent of dividends for tax purposes.

tions 42 and 43 of the Act.[191] The provisions of the Act, taken directly from the Model Act, carry out the requirement of Section 33 of the Act that the business and affairs of the corporation shall be managed by its board of directors.[192] As a result of these provisions, attempts to place the appointing and removing power in the shareholders are likely to be held invalid.[193] By-laws giving shareholders the power to ratify or veto the appointment of officers by the board have also been held invalid.[194] Similarly, by-laws giving shareholders the power to elect or remove officers have been held invalid.[195] Yet such by-law provisions do appear in actual practice from time to time, apparently utilized by attorneys who regard the Act as enabling legislation, rather than vesting exclusive power in the board of directors.

An alternative approach is an agreement among the shareholders, entered into either prior to incorporation or shortly thereafter. That agreement, among other things, may provide that shareholders, having been elected as directors, will elect specified persons to the corporate offices, sometimes with a provision that they shall serve only during good behavior, but often not. Such agreements are frequently held not to be binding on the corporation, or even on the directors as such, since they infringe on the authority of the board of directors to select and remove officers at their

191. WYO. STAT. §§ 17-36.42 and .43 (1965). Section 42 provides in part:

> The officers of a corporation shall consist of a president, one or more vice presidents as may be prescribed by the by-laws, a secretary, and a treasurer, each of whom shall be elected by the board of directors at such time and in such manner as may be prescribed by the by-laws.

Section 43 provides:

> Any officer or agent may be removed by the board of directors whenever in its judgment the best interests of the corporation will be served thereby, but such removal shall be without prejudice to the contract rights, if any, of the person so removed. Election or appointment of an officer or agent shall not of itself create contract rights.

192. WYO. STAT. § 17-36.33 (1965).

193. Taylor v. Hutton, 43 Barb. 195 (N.Y. 1864) held that in the absence of any by-laws, inherent power to remove officers rested in the directors, rather than the stockholders. Also *see* 1 O'NEAL, §§ 5.16-.17.

194. Capitol Cab Cooperative Ass'n, Inc. v. Darden, 169 A.2d 463, 464 (D.C. Mun. Ct. App. 1961).

195. Bechtold v. Stillwagon, 119 Misc. 177, 195 N.Y. Supp. 66 (1922) held that such a by-law was invalid stating that where "the power to elect a treasurer is by statute given to the directors, the power to remove him must likely be lodged with them." *Id.* at 66-67.

pleasure.[196] In some cases this doctrine has been used by courts to frustrate the desires of the contracting parties, even where it was perfectly apparent that the acts of the directors in breach of their contract were grossly unfair.[197] The current version of the Model Act has not changed this approach.[198]

Several options are possible in this area. The Act may provide that officers shall be selected and removed in the manner presently provided by the Act, or in the manner provided in the articles of incorporation or bylaws, if they specifically so provide, or finally, that they may be selected and removed by the shareholders.[199] The alternative approach, allowed in Delaware, is to provide that for specified closely held corporations the shareholders may, if the articles of

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196. Fells v. Katz, 256 N.Y. 67, 175 N.E. 516 (1931); Goldfarb v. Dorset Products, Inc., 82 N.Y.S.2d 42 (Sup. Ct. 1948).

197. In *McQuade v. Stoneham and McGraw*, the court sustained the action of the directors in ignoring their agreement as shareholders to elect one party as treasurer, stating:

> Although it has been held that an agreement among stockholders whereby it is attempted to divest the directors of their power to discharge an unfaithful employee of the corporation is illegal as against public policy [citation omitted], it must be equally true that the stockholders may not, by agreement among themselves, control the directors in the exercise of the judgment vested in them by virtue of their office to elect officers and fix salaries. Their motives may not be questioned so long as their acts are legal. The bad faith or the improper motives of the parties does not change this rule [citation omitted]. Directors may not by agreements entered into by stockholders abrogate their independent judgment. McQuade v. Stoneham and McGraw, 263 N.Y. 323, 189 N.E. 234, 236 (1934).

O'NEAL, *supra* note 10, § 5.17, at ____, n.8, argues that most modern decisions sustain the validity of such agreements as long as they do not work a fraud on the corporation or minority shareholders.

198. 2 ABA-ALI MODERN BUS. CORP. ACT ANN. §§ 50 and 51 (2d ed. 1971). It retains the formalistic approach which requires the separation of the functions of management, which are in the hands of the board, from those of the shareholders. Because of this, it is likely to frustrate the legitimate desires of many shareholders in closely held enterprises.

199. 2 ABA-ALI MODEL BUSINESS CORP. ACT ANN. § 50 (2d ed. 1971) outlines some of these provisions. DEL. CODE ANN. tit. 8, § 142(b) (1974) provides, for example:

> Officers shall be chosen in such manner and shall hold their offices for such terms as are prescribed by the by-laws or determined by the board of directors or other governing body. Each officer shall hold his office until his successor is elected and qualified or until his earlier resignation or removal. Any officer may resign at any time upon written notice to the corporation.

Presumably if the shareholders are given the power of selection and appointment of officers, they also have the power of removal. The power to appoint agents is generally considered to carry with it the inherent power of removal, with or without cause. 3 THOMPSON, COMMENTARIES ON CORPORATIONS § 1926 (3d ed. 1927).

incorporation so provide, retain and exercise all of the powers of the board of directors.[200]

CORPORATE DISPUTES

Like a partnership, the close corporation is likely to experience deep and damaging disagreements because of the need for the active participation of all or most of the investors in the enterprise. The shareholder in the close corporation frequently expects more than a return on his investment. He may also expect employement, a voice in management as a director, or perhaps more direct day-to-day control as an officer or employee. He may also expect the respect of the other participants, and perhaps prestige as a result of being an officer and director. In short, egos as well as investments are involved.

Dispute Resolution

The partnership approach has been to leave dispute resolution to the partnership agreement, by allowing partners maximum latitude in management.[201] The corporation laws have traditionally been drafted for publicly held corporations, with majority voting requirements, and have not focused on the increased prospects for deadlock found in the two-shareholder corporation or the corporation with high quorum and voting requirements designed to give minority shareholders a veto. Wyoming's Act also overlooks these problems, a not surprising omission for the times, since pro-

200. DEL. CODE ANN. tit. 8, § 351 (1974) provides in part:

> The certificate of incorporation of a close corporation may provide that the business of the corporation shall be managed by the stockholders of the corporation rather than by a board of directors. So long as this provision continues in effect:
>
> (1) No meeting of stockholders need be called to elect directors;
>
> (2) Unless the context clearly requires otherwise, the stockholders of the corporation shall be deemed to be directors for purposes of applying provisions of this chapter; and
>
> (3) The stockholders of the corporation shall be subject to all liabilities of directors.

This approach was followed in Texas. *See* TEX. BUS. CORP. ACT ANN. art. 2.30-1(G) (Vernon Supp. 1976).

201. The Uniform Partnership Act, WYO. STAT. § 17-212 (1965), provides rules determining rights and duties of partners, "subject to any agreement between them."

visions tailored for close corporations were just developing at the time of its adoption.[202]

Since 1960 statutes such as Delaware's have provided for custodians or receivers[203] and court-appointed provisional directors[204] in the event of deadlock, and have implicitly allowed arbitration in language validating delegation of authority by directors.[205] While court remedies are generally awkward and ill-suited to the day-to-day operation of a business, clauses allowing contractual solutions by which directors can delegate their authority provide flexibility for the ingenuity of counsel to mold solutions to the particular situation.

The Model Act has been strangely silent in this area, while other states, such as Delaware, have worked out new and flexible solutions to problems created by the formalism of statutes which have historically focused on publicly held corporations.

Dissolution in the Fifty-Fifty Corporation

One of the least successful parts of the statute dealing with corporate disputes involves liquidation and dissolution. Section 86 of the Wyoming Act[206] adopts the Model Act approach, and in shareholder actions merely gives the courts *power* to liquidate where certain circumstances occur. Considerable difficulties have arisen in New York under a similar statute, where the courts have been extremely solicitous of the corporate life, thus forcing disputing shareholders to remain in business together, or to voluntarily work out their own solution. One case involved a dispute where the president of the company was forced to go without salary

202. Professor O'Neal points out that pleas for special legislative treatment for close corporations only began after World War II, and that it has only been since 1960 that legislation has been developed to deal with the close corporation. 1 O'Neal, *supra* note 10, § 1.13a.

203. DEL. CODE ANN. tit. 8, § 352 (1974).

204. DEL. CODE ANN. tit. 8, § 353 (1974).

205. DEL. CODE ANN. tit. 8, § 350 (1974).

206. WYO. STAT. § 17.36-86 (1965). Subsection (a) deals with shareholder actions for liquidation. It omits the Model Act provision authorizing the Attorney General to bring such actions. 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 90(d) (1960).

for a three year period because the other shareholder refused to sign salary checks, yet the court refused dissolution because the business was "thriving."[207] Commentators have indicated a judicial split on whether this language should be construed strictly or generously.[208] The basic provisions of the Model Act have not changed since Wyoming adopted its statute.[209] The comments of the Model Act do not indicate any dissatisfaction with the judicial treatment of such language.[210]

Attorneys attempting to solve the problem through drafting techniques may provide in articles of incorporation that upon the happening of any of the events which are a prerequisite to judicial dissolution, that all of the shareholders shall vote their shares for voluntary dissolution pursuant to Section 74 of the Act.[211] The commentators are again divided on whether this technique will work.[212]

Recent statutes, such as California's, have taken the view that corporation dissolution should, like partnership dissolution,[213] be readily available to any shareholder who feels abused by his associates. Voluntary dissolution is available in Wyoming upon approval by the board of directors and the holders of two-thirds of the shares of the company.[214] The radical departure of statutes such as the recent California Act is the focus on needs of shareholders for dissolu-

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207. *In re* Radom and Neidorff, Inc., 307 N.Y. 1, 119 N.E.2d 563 (1954). The New York Law was amended in 1963 to provide that dissolution shall not be denied "because it is found that the corporate business has been or could be conducted at a profit." N.Y. BUS. CORP. LAW § 1111(b)(3) (McKinney 1963).

208. *See* Israels, *The Sacred Cow of Corporate Existence—Problems of Deadlock and Dissolution*, 19 U. CHI. L. REV. 778, 786 (1952); Hornstein, *Stockholders' Agreements in the Closely held Corporation*, 59 YALE L.J. 1040 (1950); Chayes, *Madame Wagner and the Close Corporation*, 73 HARV. L. REV. 1532 (1960) and 2 O'NEAL, *supra* note 10, § 9.27.

209. *Compare* 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 90 (1960) *with* 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 97 (2d ed. 1971).

210. 2 ABA-ALI MODEL BUS. CORP. ACT ANN. § 97 (2d ed. 1971).

211. WYO. STAT. § 17-36.74 (1965).

212. Israels, *supra* note 208, at 791-92 indicates that the technique will be upheld by the courts. *But see* Hornstein, *supra* note 208, at 1047.

213. CAL. CORP. CODE § 1800(b)(5) (West 1977). Also *see* the Wyoming Uniform Partnership Act, WYO. STAT. § 17-225 (1965).

214. WYO. STAT. § 17-36.75 (1965).

tion,[215] absent proof of illegal, oppressive or fraudulent acts, as currently required in Wyoming.[216]

Modern statutes such as Delaware's allow the shareholders to agree in advance on dissolution on the vote of any shareholder or the holders of a specified number of shares, a provision akin to that of partnerships.[217] The Delaware provision also allows shareholders to agree on dissolution upon the occurrence of any specified event,[218] thus allowing them to provide effective protection for minority shareholders, which overcomes the rigidity of earlier cases.

THE INCORPORATED PARTNERSHIP ALTERNATIVE

As Professor O'Neal has observed, in states where little or nothing has been done to modify statutes unfavorable to close corporations, "even an experienced and resourceful corporation lawyer may find it difficult or impossible, because of restrictive or ambiguous statutes, to set up with any assurance of validity the kind of control pattern participants in a close corporation may want."[219] This article has attempted to point out some of the specific difficulties such attorneys may encounter with the present Wyoming statute, and compare some other statutory approaches to these specific problems. Such solutions must be carefully drawn, because as part of a general corporation law, they also apply to publicly held corporations.

Separate provisions for closely held corporations have been adopted with increasing frequency since 1960.[220] The general approach of these statutes has been to allow incorporated partnerships.[221] They allow shareholders to take

215. CAL. CORP. CODE § 1800(b)(5) (West 1977). Also *see* WYO. STAT. § 17-225 (1965).
216. WYO. STAT. § 17-36.86 (1965).
217. DEL. CODE ANN. tit. 8, § 355 (1974).
218. DEL. CODE ANN. tit. 8, § 355(a) (1974).
219. 1 O'NEAL, *supra* note 10, § 1.13, n.3.
220. N.C. GEN. STAT. §§ 55-1 to -175 (1975); N.Y. BUS. CORP. LAW § 101 *et seq.* (McKinney 1963); S.C. CODE §§ 12-11.1 to -31.2 (Cum. Supp. 1975); DEL. CODE ANN. tit. 8. §§ 341-356 (1974); TEX. BUS. CORP. ACT ANN. art. 2.30-1 to -5 (Vernon Supp. 1976). *See generally* 1 O'NEAL *supra* note 10, §§ 1.14a -.14b.
221. *See, e.g.*, DEL. CODE ANN. tit. 8, § 354 (1974).

over the functions of directors without liability beyond that normally borne by directors.[222]

The 1977 Session of the Wyoming State Legislature has adopted a "Limited Liability Company Act," which could be utilized by some entrepreneurs to achieve an incorporated partnership.[223] The Act is an amalgam of provisions from the Business Corporation Act,[224] the Uniform Limited Partnership Act[225] and the Uniform Partnership Act.[226] It appears to be an attempt to create a corporate entity taxable as a partnership, although it lacks one essential characteristic of a partnership or limited partnership—unlimited liability.[227] The distinctive feature of the new act is that it enables the shareholders, or members, as they are called, to manage the enterprise directly,[228] as in the close corporation provisions of Delaware and other states.[229]

To the extent that the Limited Liability Company Act allows an incorporated partnership, it would seem to provide an alternative for promoters seeking limited liability. Unfortunately, the Act leaves more questions unanswered than it solves, and for that reason alone does not represent a viable alternative for most enterprises, absent some costly drafting to provide solutions for those matters uncovered by its provisions. The Wyoming Business Corporation Act

222. *See, e.g.*, DEL. CODE ANN. tit. 8, § 351 (1974).
223. 1977 Wyo. Sess. Laws ch. 158, §§ 17-294-329.
224. WYO. STAT. § 17-36.1 *et seq.* (1965).
225. WYO. STAT. § 17-263 *et seq.* (Supp. 1975).
226. WYO. STAT. § 17-195 *et seq.* (1965).
227. Section 17-306 of the Limited Liability Company Act expressly provides:

> *Liability of members and managers.* Neither the members of a limited liability company nor the managers of a limited liability company managed by a manager or managers are liable under a judgment, decree or order of a court, or in any other manner, for a debts, obligation or liability of the limited liability company.

1977 Wyo. Sess. Laws ch. 158, § 17-306.
228. Section 17-309 provides that the management of a liimted liability company shall be vested in its members in proportion to their capital contributions, without providing any voting or quorum requirements for action. In this respect the act seems to be like the Partnership Act, leaving these questions to the agreement of the parties. Apparently each member may be granted apparent authority to bind the entity, since Section 17-310 of the Act provides that any member may contract debts and incur liabilities on behalf of the company, unless management is vested in managers by the articles of organization. In this respect it resembles Section 9(1) of the Uniform Partnership Act which makes every partner an agent of the partnership for the purpose of its business. WYO. STAT. § 17-203(1) (1965).
229. *See* statutes cited in note 220, *supra.*

has 125 sections, of which approximately 26 appear in the Limited Liability Company Act, some substantially modified. While other parts of the Business Corporation Act are covered by provisions from the Uniform Partnership Act[230] and the Uniform Limited Partnership Act,[231] the omissions are still substantial. The new Act, for example, contains no provisions authorizing a complex capital structure, and none concerning meetings of members or voting requirements for management of the enterprise. No provisions for indemnifying managers or active members are included, and there are no provisions for removal of managers. Likewise, nothing is said about the ability of such companies to merge, either with like companies, or with corporations organized under the Business Corporation Act. Rather than add these provisions as a modification of the existing Business Corporation Act, as the close corporation provisions of other jurisdictions do, this statute stands independent of the Business Corporation Act. While it may be a viable alternative to the limited partnership if it receives favorable treatment from the Internal Revenue Service,[232] which is by no means assured, it seems doubtful that it will appeal to most attorneys as an alternative to drafting designed to tailor the Business Corporation Act to the needs of the close corporation.

230. Several provisions of the Wyoming Uniform Partnership Act appear in the new Limited Liability Company Act. *Compare* WYO. STAT. §§ 17-203, 17-204 and 17-225 (1965) *with* Sections 17-310, 17-311 and 17-316(a)(iii) respectively of the Limited Liability Company Act.

231. Although some of the provisions of the Wyoming Uniform Limited Partnership Act appearing in the new Limited Liability Company Act are not reproduced verbatim, they are clearly the source of the language appearing in certain sections of the new Act. *Compare* WYO. STAT. §§ 17-265(a)(i)(F), (G), (K), (M); 17-278 to -282; 17-286 to -289 (Supp. 1975) *with* Sections 17-300(a)(v)-(viii); 17-312 to -15, 17-319, 17-322, 17-322(c) and 17-323 respectively of the Limited Liability Company Act.

232. Corporate characteristics are listed in the Treasury Regulations as:

> (i) Associates, (ii) an objective to carry on business and divide the gains therefrom, (iii) continuity of life, (iv) centralization of management, (v) liability for corporate debts limited to corporate property, and (vi) free transferability of interests. . . . An organization will be treated as an association [corporation] if the corporate characteristics are such that the organization more nearly resembles a corporation than a partnership or trust.
> Treas. Reg. § 301.7701-2(a) (1960).

It is not immediately clear that the Limited Liability Company will be any less a corporation for tax purposes than a professional service corporation formed under state professional corporation laws which limit participation in the management of the enterprise to the professionals owning shares who are licensed to practice in the jurisdiction.

CONCLUSION

This article has only attempted to expose some of the problems and opportunities facing Wyoming in the area of close corporations. The problems stem from a statute whose roots are in an era which dealt primarily with public corporations, and which retains some of the formalism and rigidity of an earlier day. Legislative opportunity now exists for allowing corporations the flexibility now available to a partnership, and giving participants the freedom to contract for creative solutions to complex problems.