CHAPTER 18

Statutory Close Corporation Supplement

ARTICLE 1

Creation

**SECTION 33‑18‑101.** Short title.

 This chapter is known and may be cited as the South Carolina Statutory Close Corporation Supplement.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The Model Statutory Close Corporation Supplement is an optional statute developed for states that determine that it is advisable to enact an integrated statute dealing with the problems of closely held corporations. This Supplement is not part of the Revised Model Business Corporation Act (“MBCA”), and the decision whether to enact this Supplement should be considered independently of the enactment of the Model Act.

This Supplement was developed on the assumption that the state in question has enacted the Revised Model Business Corporation Act, or at least a statute with the same degree of flexibility as the Revised Model Act in the following areas: issuance of shares for nontraditional forms of consideration (MBCA Section 6.21) (Section 33‑6‑210), preemptive rights (MBCA Section 6.30) (Section 33‑6‑300), supermajority voting rights for shareholders (MBCA Sections 7.27, 10.21) (Sections 33‑7‑270 and 33‑10‑210) and directors (MBCA Sections 8.24, 10.22) (Sections 33‑8‑240 and 33‑10‑220), action by shareholders or board of directors without a meeting (MBCA Sections 7.04, 8.21) (Sections 33‑7‑104 and 33‑8‑210), voting by voting groups (MBCA Section 7.27) (Section 33‑7‑270), cumulative voting for directors (MBCA Section 7.28) (Section 33‑7‑280), shareholder voting agreements (MBCA Section 7.31) (Section 33‑7‑310), voting trusts (MBCA Section 7.30) (Section 33‑7‑300), irrevocable proxies (MBCA Section 7.22(d)) (Section 33‑7‑220(d)), share transfer restrictions (MBCA Section 6.27) (Section 33‑6‑270), protection of class voting rights for the election and removal of directors (MBCA Sections 8.04, 8.08(b), 8.08(c)) (Sections 33‑8‑104, 33‑8‑108(b) 33‑8‑108(c)), filling of vacancies on the board of directors (MBCA Section 8.10(b)) (Section 33‑8‑100(b)), flexibility in appointment of officers (MBCA Section 8.40) (Section 33‑8‑400), shareholders’ voting rights with respect to amendments of articles of incorporation and mergers (MBCA Sections 10.04, 11.03(f)) (Sections 33‑10‑104, 33‑11‑103(f)), dissenters’ rights (MBCA ch.13) (see ch. 13 of this title), and judicial dissolution (MBCA Section 14.30) (Section 33‑14‑300).

In addition, section 8.01 (Section 33‑8‑101) of the 1984 Model Act authorizes a corporation with less than 50 shareholders to dispense with the board of directors or limit its authority in whole or in part. This authorization is replicated in the Model Statutory Close Corporation Supplement. [Note: the 50 shareholder limitation was not adopted as part of this Act. See the South Carolina Reporters’ Comments to Sections 33‑8‑101 and 33‑18‑103.].

Under a statute with the flexibility of the Revised Model Act, it is usually possible to achieve any desired legal result within a closely held corporation without recourse to the Close Corporation Supplement by the use of sophisticated contracts among the shareholders and special provisions in the articles of incorporation and the bylaws. This Supplement therefore does not significantly change the results that may be obtained under the Revised Model Act; rather, the advantages of the Supplement lie in the certainty and flexibility that it provides. Also, in many situations, this Supplement facilitates the achievement of desired results with significantly less drafting and significantly lower probabilities that some factor has been overlooked. The Supplement further provides an optional standard‑form buy‑out arrangement in the recurring situation where a shareholder in a closely held corporation has died or been incapacitated leaving a spouse who is unable or unwilling to work in the enterprise.

Many states have adopted a variety of different provisions relating to closely held corporations; the Model Statutory Close Corporation Supplement draws from this broad experience within various states, and develops principles for closely held corporations based on this experience. Not all states, however, have adopted integrated statutes analogous to the Supplement; some state legislatures have not adopted special provisions relating to close corporations; others have chosen to enact such provisions on a non‑integrated basis as part of their general corporation statutes. The 1969 Model Act essentially adopted a non‑integrated approach.

Examples of situations in which the Supplement may be advantageous include:

(1) A small enterprise that is likely to remain a closely held business, all or substantially all of whose shareholders are active in the business, may avoid the expense of drafting an elaborate set of specially tailored close corporation documents. If the shareholders elect to be governed by the Supplement, the share transfer restriction in sections 11 and 12 (Sections 33‑18‑110 and 33‑18‑120) automatically apply and a right to have their shares purchased at death may be provided by including the statement in the articles of incorporation that sections 14 through 17 (Sections 33‑18‑140 and 33‑18‑170) shall apply (with such modifications or alterations as are deemed appropriate).

(2) A professional corporation whose shareholders wish to be taxed as a corporation may operate internally as a partnership. Under sections 20 and 21 (Sections 33‑18‑200 and 33‑18‑210) the corporation may be managed entirely by the shareholders, who may provide for voting on a one‑vote‑per‑shareholder basis rather than on the basis of the usual rule of one‑vote‑per‑share.

(3) A wholly owned subsidiary corporation may be created and operated with a very simple corporate structure. Such a subsidiary corporation may operate without a board of directors (Section 21) (Section 33‑18‑210), need not adopt bylaws (Section 22) (Section 33‑18‑220), need not hold annual meetings except upon a demand from a shareholder (Section 23(b)) (Section 33‑18‑230(b)), and may have a single officer with authority to sign all legal documents on behalf of the corporation (Section 24) (Section 33‑18‑240).

This Supplement may also be useful in situations in which the shareholders of a closely held corporation obtain basic protection of their rights through sophisticated contractual arrangements, but cannot achieve desired management flexibility and remedies under the general business corporation statute. The shareholders, for example, may wish to authorize director proxies (Section 20) (Section 33‑18‑200) or to allow less than a majority to elect to dissolve the corporation (Section 33) (Section 33‑18‑330).

SOUTH CAROLINA REPORTERS’ COMMENTS

1. The need for special statutory provisions to accommodate close corporations has been recognized for many years. See, e.g., Freeman v. King Pontiac Co., 236 S.C. 335, 114 S.E.2d 478 (1960). See, generally, F.H. O’Neal, CLOSE CORPORATIONS Sections 1.12‑1.15 (2nd ed., 1971). The 1962 South Carolina Business Corporation Act was one of the first statutes in this country to include such provisions on a systematic, comprehensive basis. Other states that have enacted special close corporation provisions include Alabama, Arizona, California, Delaware, Florida, Illinois, Kansas, Maine, Maryland, Michigan, Minnesota, North Carolina, New Jersey, New York, Ohio, Pennsylvania, Texas, and Wisconsin.

These statutes basically follow two patterns: (1) a separate chapter in the state’s business corporation act, commonly referred to as integrated close corporation statutes, and (2) close corporation provisions that are spread throughout the state’s business corporation code. The close corporation provisions in the 1962 South Carolina Business Corporation Act, most of which have been included in other parts of this act, fall within the second category. The Statutory Close Corporation Supplement, on the other hand, is an integrated close corporation statute. It contains in one chapter provisions that facilitate the organization and operation of a close corporation and reduce the amount of legal drafting that will have to be done for many routine close corporations. Sections 33‑18‑110 and 33‑18‑120, for example, contain a statutory form of share transfer restrictions which apply to a statutory close corporation unless notice of different restrictions is given; and Section 33‑18‑140 contains an elective buy‑out provision that gives the estate of a deceased shareholder the right to have the decedent’s shares purchased by the corporation or the remaining shareholders. Moreover, a statutory close corporation does not have to adopt bylaws and does not have to hold annual shareholders’ meetings except upon shareholder demand. See Sections 33‑18‑220 and 33‑18‑230. These two provisions are useful particularly for wholly‑owned subsidiary corporations.

The Statutory Close Corporation Supplement is elective. It does not apply unless the incorporators or, in the case of any existing corporation, two‑thirds of the shareholders voluntarily elect to be governed by its provisions. In other words, a close corporation can choose to be governed by Chapters 1 through 17 of this act or to elect to be a statutory close corporation. Furthermore, there are no onerous requirements for either election or termination of statutory close corporation status, and shareholders who do not vote in favor of the election or termination are entitled to dissenters’ rights. See Sections 33‑18‑103 and 33‑18‑310.

Because of planning flexibility, greater legal certainty, and reduced drafting, it is anticipated that substantial numbers of close corporations will elect to be governed by the Statutory Close Corporation Supplement. Since available statistics indicate that ninety‑five percent of all corporations have ten or fewer shareholders and ninety‑nine percent have one hundred or fewer shareholders, in time the vast majority of South Carolina domestic corporations may be statutory close corporations. Even if this is not the case, the Statutory Close Corporation Supplement will provide a viable alternative legal framework for close corporations of all types, including professional corporations.

2. Special Note on Terminology Used in the Comments and Cross References.

Several important terms used in the comments and cross references in this chapter are discussed in the South Carolina Reporters’ Comments to Section 33‑1‑101.

Two new terms are used in the comments and cross references in this chapter:

(1) MBCA, which is an acronym for the Model Business Corporation Act of 1984 (sometimes referred to in the Official Comments as the Revised Model Business Corporation Act), and which in Chapters 1 through 17 is referred to as the 1984 Model Act or Model Act; and.

(2) South Carolina Business Corporation Act, which refers to Chapters 1 through 17 of this title. Technically, this term applies to Chapters 1 through 20—see Section 33‑1‑101, but it is used in the more limited sense in this chapter and Chapter 19 for convenience. Chapters 18 and 19 are supplements and Chapters 1 through 17 constitute the general business corporate statute.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 1.

CROSS REFERENCES

Application of South Carolina Business Corporation Act, see Section 33‑18‑102.

Application to existing corporations, see Section 33‑18‑500.

Professional corporations, Professional Corporation Supplement, see Sections 33‑19‑101 et seq.

**SECTION 33‑18‑102.** Application of Business Corporation Act and Professional Corporation Supplement.

 (a) Chapters 1 through 17 of this title apply to statutory close corporations to the extent not inconsistent with the provisions of this chapter.

 (b) This chapter applies to a professional corporation organized under the South Carolina Professional Corporation Supplement (Chapter 19 of this title) whose articles of incorporation contain the statement required by Section 33‑18‑103(a), except insofar as the South Carolina Professional Corporation Supplement contains inconsistent provisions.

 (c) This chapter does not repeal or modify any statute or rule of law that is or would apply to a corporation that is organized under Chapters 1 through 17 of this title or the South Carolina Professional Corporation Supplement (Chapter 19 of this title) and that does not elect to become a statutory close corporation under Section 33‑18‑103.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

Provisions in the Revised Model Business Corporation Act apply to all statutory close corporations except to the extent they are not consistent with the provisions in this Supplement. The relationship between this Supplement and the Model Act is analogous to the relationship between the Uniform Partnership Act and the Uniform Limited Partnership Act. Whenever this Supplement is silent on an issue, the corresponding provision of the Model Act applies. These corresponding provisions are referred to in the cross‑references following each section of the supplement. See also the Official Comments to sections 31 and 32 (Sections 33‑18‑310 and 33‑18‑320) for discussion of the applicability of these statutes when a corporation terminates its status as a statutory close corporation.

Under section 2(b) (Section 33‑18‑102(b)) the provisions of this Supplement apply to all professional corporations that elect to be statutory close corporations, except to the extent the provisions are inconsistent with the provisions of the Model Professional Corporation Supplement. See the Official Comment to section 2 (Section 33‑19‑102) of the Model Professional Corporation Supplement for a discussion of the relationship between the Model Professional Corporation Supplement and the Revised Model Business Corporation Act.

Section 2(c) (Section 33‑18‑102(c)), which is derived from section 356 of the Delaware Corporation Law, makes clear that enactment of the Supplement does not affect the law applicable to corporations, including closely held corporations, that are not statutory close corporations.

SOUTH CAROLINA REPORTERS’ COMMENTS

This section explains the relationship between the Statutory Close Corporation Supplement, the Professional Corporation Supplement (Sections 33‑19‑101 et seq.) and the other chapters of the South Carolina Business Corporation Act. The rules set forth are similar to the rules governing the relationship of general and limited partnerships in the South Carolina Uniform Partnership Act and the South Carolina Uniform Limited Partnership Act. See Sections 33‑41‑210 and 33‑42‑2020 of the 1976 Code.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 2.

CROSS REFERENCES

Application of South Carolina Business Corporation Act, see Section 33‑20‑102.

Election of statutory close corporation status, see Section 33‑18‑103.

Professional Corporation Supplement, see Section 33‑19‑102.

South Carolina Business Corporation Act definitions, see Section 33‑1‑400.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 3:4 , Checklist‑Drafting Articles of Incorporation.

**SECTION 33‑18‑103.** Definition and election of statutory close corporation status.

 (a) A statutory close corporation is a corporation whose articles of incorporation contain a statement that the corporation is a statutory close corporation.

 (b) A corporation incorporated in South Carolina under this title may become a statutory close corporation by amending its articles of incorporation to include the statement required by subsection (a). The amendment must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of the corporation, voting as separate voting groups, whether or not otherwise entitled to vote on amendments. If the amendment is adopted, a shareholder who did not vote in favor of the amendment is entitled to assert dissenters’ rights under Chapter 13 of this title.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

1. 50‑SHAREHOLDER LIMIT [This limitation was not adopted—See the South Carolina Reporters’ Comments].

With the exception of a corporation having more than 50 shareholders at the time it wishes to become a statutory close corporation, all corporations are potentially eligible to make the election. (See MBCA section 1.42 (Section 33‑1‑410) for the method of determining the number of shareholders.) The election is made by including in the articles of incorporation a statement that the corporation is a statutory close corporation. An electing corporation continues to be governed by the Supplement unless the shareholders revoke this election. Other terminating events, such as an increase in the number of shareholders beyond some arbitrary maximum or the making of a public share offering, commonly found in existing close corporation statutes create the undesirable possibility of inadvertent terminations of close corporation status and do not seem to serve any purpose except to complicate the statutory framework.

The danger that a large corporation with numerous shareholders might attempt to elect close corporation status in order to operate without a board of directors, although highly unlikely as a practical matter, is the reason for the 50 shareholder limit in section 3(b) (Section 33‑18‑103(b). A new corporation that wishes to elect statutory close corporation status at the time of its initial incorporation is eligible, however, regardless of the number of subscribers. Likewise, a new or existing corporation that becomes a statutory close corporation at a time when it has fewer than 50 shareholders may continue to operate as a statutory close corporation even though it subsequently has more than 50 shareholders. The potential for abuse by evasion of the normal rules governing corporations is not considered to be sufficiently great to justify an absolute numerical limitation, which inevitably creates the possibility of an unknowing change in status, and complexity of statutory provisions designed to deal with those changes of status.

2. SPECIAL DESIGNATION.

Consideration was given to requiring a statutory close corporation to use a special designation, such as “A Statutory Close Corporation” or “S.C.C.,” on all letterhead and documents to distinguish it from a regular corporation. Special designations are used in European corporation statutes to distinguish between public and private companies. This practice has not been used in the past in the United States except with respect to professional corporations. See section 15 (Section 33‑19‑150) of the Model Professional Corporation Supplement, which under section 2(b) (33‑18‑102(b)) of this Supplement applies to a professional corporation that elects to become a statutory close corporation. The only purpose served by the designation is to provide special notice to creditors and shareholders; of course, the usual name of a corporation gives a creditor notice of the company’s limited liability and shareholders have notice of the corporation’s special status because of the notice on the share certificates required by section 10 (33‑18‑109).

3. ARTICLES OF INCORPORATION.

The articles of incorporation contain the basic information about a corporation. They may also give notice to prospective shareholders and creditors of special or unusual contractual arrangements among the shareholders.

The only required difference between articles of incorporation for a statutory close corporation and for a regular corporation is the statement designating the corporation to be a statutory close corporation. Although statutory close corporations may use a form of articles of incorporation identical to that for any corporation, a special format that takes into account the provisions respecting share transfer restrictions (sections 11 and 14) (Section 33‑18‑110 and 33‑18‑140), the possibility that the corporation will not have a board of directors (section 21) (Section 33‑18‑210), and other optional provisions that can be utilized by statutory close corporations may be more useful. See for example, the format published in 37 BUS.LAW. 309 (1981).

4. REQUIRED VOTE.

Some states, e.g. Maryland and Texas, require unanimous consent of the shareholders for an existing corporation to become a statutory close corporation. Most states, however, follow the pattern of the Delaware statute that requires a two‑thirds vote of all outstanding shares. The Close Corporation Supplement adopts a compromise between the two positions by requiring a two‑thirds vote of each class or series of shares, voting as separate voting groups, but shareholders opposed to the election are granted dissenters’ rights.

5. TRANSITION PROVISIONS.

A state having an existing close corporation statute when it enacts the Model Close Corporation Supplement may allow existing close corporations to qualify automatically for close corporation status by filing amended articles of incorporation complying with section 3 (Section 33‑18‑103). See section 50 (Section 33‑18‑500).

SOUTH CAROLINA REPORTERS’ COMMENTS

Two changes from the Model Act language in this section, which sets forth the requirements for election of statutory close corporation status by newly formed and existing corporations have been made:

First, a provision prohibiting existing corporations having more than fifty shareholders from electing to become statutory close corporations has been deleted. A corporation having fewer than fifty shareholders at the time of the election can continue to qualify as a statutory close corporation even though it subsequently has more than fifty shareholders and there is no sound policy reason why a corporation having more than fifty shareholders should not be able to elect statutory close corporation status if two‑thirds or more of the shareholders are in favor of the election. In any case, it is unlikely that very many corporations having more than fifty shareholders will want to operate as a statutory close corporation because the partnership‑like informal management structure possible under the Statutory Close Corporation Supplement will in most cases be too cumbersome and impractical for a corporation having large numbers of shareholders.

Second, subsection (b) of the Model Act Official Text has been changed to allow any shareholder who does not vote in favor of the election of an existing corporation to become a statutory close corporation to have dissenters’ rights. The Model Act requires a shareholder to vote against the election in order to qualify for dissenters’ rights. This change makes the Statutory Close Corporation Supplement consistent with the dissenters’ rights voting requirements in Chapter 13. See Section 33‑13‑210. A similar change is made in all sections of this Supplement that gives shareholders dissenters’ rights. See Sections 33‑18‑140(d) and 33‑18‑310(c).

In this connection, note that under Section 33‑7‑250, the motion to amend the articles to elect statutory close corporation status carries if two‑thirds of the votes cast vote in favor of the election.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 3.

CROSS REFERENCES

Amendment of articles of incorporation, see Sections 33‑10‑101 et seq.

Application of Professional Corporation Act, see Sections 33‑18‑102 and 33‑19‑102.

Application to existing corporations, see Section 33‑18‑500.

Articles of incorporation, see Section 33‑2‑102.

Dissenters’ rights, see Sections 33‑13‑101 et seq.

Filing fees, see Section 33‑1‑220.

Filing requirements, see Section 33‑1‑200.

Number of shareholders, see Section 33‑1‑420.

Voting by voting groups: amendment of articles of incorporation, see Section 33‑10‑104.

Voting by voting groups: generally, see Section 33‑7‑260.

“Voting group” defined, see Section 33‑1‑400.

Library References

Corporations 3, 18, 40.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 5, 25 to 27, 33, 38, 41, 62, 559.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 3:4 , Checklist‑Drafting Articles of Incorporation.

South Carolina Legal and Business Forms Section 1:25 , Close Corporations.

ARTICLE 2

Shares

**SECTION 33‑18‑109.** Notice of statutory close corporation status on issued shares.

 (a) The following statement must appear conspicuously on each share certificate issued by a statutory close corporation:

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

 (b) Within a reasonable time after the issuance or transfer of uncertificated shares, the corporation shall send to the shareholders a written notice containing the information required by subsection (a).

 (c) The notice required by this section satisfies all requirements of this chapter and of Section 33‑6‑270 that notice of share transfer restrictions be given.

 (d) A person claiming an interest in shares of a statutory close corporation which has complied with the notice requirement of this section is bound by the documents referred to in the notice. A person claiming an interest in shares of a statutory close corporation which has not complied with the notice requirement of this section is bound by any documents of which he, or a person through whom he claims, has knowledge or notice.

 (e) A corporation shall provide to any shareholder upon his written request and without charge copies of the articles of incorporation and bylaws, shareholders’ agreements, and other documents filed with the corporation that restrict transfer or affect voting or other rights of shareholders.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The purpose of this section is to put shareholders in a statutory close corporation on notice that their shares are subject to transfer restrictions and that their rights and liabilities may be different from those of shareholders in other corporations. The notice is essential to bind third parties who are not signatories to the original agreements establishing the rights of shareholders among themselves.

The notice is also drafted to satisfy the notice requirements in cases where a statutory close corporation has uncertificated shares. Under section 6.26 (Section 33‑6‑260) of the Revised Model Act, the notice required by this section would appear in the transaction statement.

SOUTH CAROLINA REPORTERS’ COMMENTS

This section sets forth the legend that must be set forth on the share certificates of a statutory close corporation. The same legend must be included in the initial transaction statement if uncertificated securities are used. South Carolina law does not at the present time authorize uncertificated securities but including the Model Act language in this act will reduce the number of amendments necessary if revised Article 8 of the Uniform Commercial Code, which contains detailed rules for uncertificated securities, is adopted.

Other legends may be necessary on the share certificates or transaction statement of statutory close corporations. For example, since the shares, in most cases, will not be registered securities, it may be advisable to include a legend stating the shares are unregistered and can be transferred only with consent of the issuer’s attorney in addition to the legend required by this section.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 10 with technical amendments to subsection (e).

CROSS REFERENCES

Attempted share transfer in breach of prohibition, see Section 33‑18‑130.

Certificateless shares, see Section 33‑6‑260.

Compulsory purchase of shares, see Sections 33‑18‑140 through 33‑18‑170.

“Conspicuous” defined, see Section 33‑1‑400.

“Notice” defined, see Section 33‑1‑410.

Share transfer restrictions: generally, see Section 33‑6‑270.

Share transfer restrictions: statutory close corporations, see Section 33‑18‑110.

Shareholders’ agreements, see Section 33‑18‑200.

Voting trust agreements, see Section 33‑6‑300.

Library References

Corporations 95.

Westlaw Topic No. 101.

C.J.S. Corporations Section 174.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:25 , Close Corporations.

**SECTION 33‑18‑110.** Share transfer prohibition.

 (a) An interest in shares of a statutory close corporation may not be voluntarily or involuntarily transferred, by operation of law or otherwise, except to the extent permitted by the articles of incorporation or under Section 33‑18‑120.

 (b) Except to the extent the articles of incorporation provide otherwise, this section does not apply to a transfer:

 (1) to the corporation or to any other holder of the same class or series of shares;

 (2) to members of the shareholder’s immediate family (or to a trust, all of whose beneficiaries are members of the shareholder’s immediate family) which consists of his spouse, parents, lineal descendants (including adopted children and stepchildren) and the spouse of any lineal descendant, and brothers and sisters;

 (3) that has been approved in writing by all of the holders of the corporation’s shares having general voting rights;

 (4) to an executor or administrator upon the death of a shareholder or to a trustee or receiver as the result of a bankruptcy, insolvency, dissolution, or similar proceeding brought by or against a shareholder;

 (5) by merger or share exchange under Chapter 11 of this title or an exchange of existing shares for shares of a different class or series in the corporation;

 (6) by a pledge as collateral for a loan that does not grant the pledgee any voting rights possessed by the pledgor;

 (7) made after termination of the corporation’s status as a statutory close corporation.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

This section sets out a standardized transfer prohibition that automatically applies unless the articles of incorporation provide otherwise. The prohibition is designed to accomplish two purposes: first, to provide a prohibition that fits the needs of the “typical” close corporation; and second, to facilitate alteration in order to fit the special needs of the shareholders in a particular corporation.

1. COVERED TRANSFERS.

The definition of transfer in subsection (a) is intended to cover every possible type of transaction that might create an interest in corporate shares, including purchase, sale, discount, negotiation, gift, trust, legacy, inheritance, pledge, mortgage, lien, creation of a security interest, hypothecation, bankruptcy, or transfer pursuant to court order.

2. EXEMPT TRANSFERS.

Subsection (b) describes a number of exemptions to the prohibition of subsection (a). Intrashareholder and intrafamily transfers are exempt on the assumption that most “typical” close corporation shareholders would want these transfers to be exempt. Transfers to executors, administrators, trustees, or receivers that result from death, bankruptcy, liquidation, or dissolution of a shareholder are also exempt. In addition transfers that are in effect merely internal recapitalizations and transfers having the approval of all the shareholders are exempt. Transactions in which the stock is pledged or hypothecated are also exempt when no voting rights are given to the pledgee. In all these situations, however, further attempted transfers by the transferees are subject to the prohibitions unless the subsequent transfer qualifies under one of the exemptions. For example, although a pledge of shares as collateral for a loan is an exempt transaction (unless the pledgee is given the power to vote the shares), a subsequent sale of the pledged stock by the pledgee in a foreclosure proceeding can only be made in accordance with section 12 (Section 33‑18‑120) unless the transfer is exempt under subsection (b).

A final type of exempt transfer is one made after the corporation ceases to be a statutory close corporation. The automatic elimination of the restrictions on transfer at termination of the close corporation election is justified on the assumption that in most cases the shareholders would want the prohibition to be ineffective after termination. The right to receive the fair value of his shares by voting against the termination (see section 31) (Section 33‑18‑310) is a reasonable remedy for the shareholders opposed to termination on any ground. Alternative methods for continuing the restriction after termination of statutory close corporation status exist. See the Official Comment to section 31 (Section 33‑18‑310).

3. BUILT‑IN FLEXIBILITY.

The statutory prohibition can be limited or modified simply by stating in the articles of incorporation that it does not apply or by specifying in the articles of incorporation the changes from the statutory language. For example, if the shareholders wanted all pledges to be subject to the transfer prohibition but otherwise found the statutory prohibition acceptable, the attorney drafting the articles of incorporation may simply provide in the articles of incorporation “Subsection 11(b)(6) (Section 33‑18‑110(b)(6)) does not apply.” All shareholders thus have some automatic basic protection against unwanted transfers plus maximum flexibility to alter or replace the statutory scheme. See generally the annotation to section 6.27 (Section 33‑6‑270) of the Revised Model Business Corporation Act, for a discussion of cases involving share transfer restrictions.

SOUTH CAROLINA REPORTERS’ COMMENTS

Sections 33‑18‑110 and 33‑18‑120 set forth standardized share transfer restrictions that automatically apply to statutory close corporations except to the extent otherwise stated in the articles of incorporation. These sections contain elements of all three basic categories of share transfer restrictions: consent restrictions (Section 33‑18‑110), first refusal options (Section 33‑18‑120(a)), and prohibitions against transfers to certain persons (Section 33‑18‑120(b)), and are designed to avoid many of the interpretive and drafting problems that are commonly encountered with share transfer restriction agreements derived from form books or other sources. See, e.g., McLeod v. Sandy Island Corporation, 251 S.C. 1, 216 S.E.2d 746 (1975). See, generally, H. Haynsworth, ORGANIZING A SMALL BUSINESS ENTITY Section 5.04(b) (1986).

The ability to alter the statutory scheme by a provision in the corporation’s articles of incorporation adding or deleting language in the statute increases the flexibility and usefulness of these sections. See paragraph 3 of the Official Comment.

No substantive changes in the Model Act language in either section is made in this act.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 11.

CROSS REFERENCES

Attempted share transfer in breach of prohibition, see Section 33‑18‑130.

Corporation’s purchase options, see Sections 33‑18‑120 and 33‑18‑130.

Information on shares: generally, see Section 33‑6‑270.

Information on shares: statutory close corporation shares, see Section 33‑18‑109.

Merger and share exchange: generally, see Sections 33‑11‑101 et seq.

Merger and share exchange: statutory close corporations, see Section 33‑18‑300.

Sale of assets: generally, see Sections 33‑12‑101 et seq.

Sale of assets: statutory close corporations, see Section 33‑18‑300.

“Shareholder” defined, see Section 33‑1‑400.

Termination of statutory close corporation status, see Section 33‑18‑310.

Library References

Corporations 113.

Westlaw Topic No. 101.

C.J.S. Corporations Section 220.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:25 , Close Corporations.

South Carolina Legal and Business Forms Section 1:57 , Formation‑Statutory Close Corporation.

**SECTION 33‑18‑120.** Share transfer after first refusal by corporation.

 (a) A person desiring to transfer shares of a statutory close corporation subject to the transfer prohibition of Section 33‑18‑110 first must offer them to the corporation by obtaining an offer to purchase the shares for cash from a third person who is eligible to purchase the shares under subsection (b). The offer by the third person must be in writing and state the offeror’s name and address, the number and class or series of shares offered, the offering price for each share, and the other terms of the offer.

 (b) A third person is eligible to purchase the shares if:

 (1) he is eligible to become a qualified shareholder under any federal or state tax statute the corporation has adopted and he agrees in writing not to terminate his qualification without the approval of the remaining shareholders; and

 (2) his purchase of the shares will not impose a personal holding company tax or similar federal or state penalty tax on the corporation.

 (c) The person desiring to transfer shares shall deliver the offer to the corporation, and by doing so offers to sell the shares to the corporation on the terms of the offer. Within twenty days after the corporation receives the offer, the corporation shall call a special shareholders’ meeting, to be held not more than forty days after the call, to decide whether the corporation should purchase all (but not less than all) of the offered shares. The offer must be approved by the affirmative vote of the holders of a majority of votes entitled to be cast at the meeting, excluding votes in respect of the shares covered by the offer.

 (d) The corporation must deliver to the offering shareholder written notice of acceptance within seventy‑five days after receiving the offer or the offer is rejected. If the corporation makes a counteroffer, the shareholder must deliver to the corporation written notice of acceptance within fifteen days after receiving the counteroffer or the counteroffer is rejected. If the corporation accepts the original offer or the shareholder accepts the corporation’s counteroffer, the shareholder shall deliver to the corporation duly endorsed certificates for the shares, or instruct the corporation in writing to transfer the shares if uncertificated, within twenty days after the effective date of the notice of acceptance. The corporation may specifically enforce the shareholder’s delivery or instruction obligation under this subsection.

 (e) A corporation accepting an offer to purchase shares under this section may allocate some or all of the shares to one or more of its shareholders or to other persons if all the shareholders voting in favor of the purchase approve the allocation. If the corporation has more than one class or series of shares, the remaining holders of the class or series of shares being purchased are entitled to a first option to purchase the shares not purchased by the corporation in proportion to their shareholdings or in some other proportion agreed to by all the shareholders participating in the purchase.

 (f) If an offer to purchase shares under this section is rejected, the offering shareholder, for a period of one hundred twenty days after the corporation received his offer, is entitled to transfer to the third person offeror all (but not less than all) of the offered shares in accordance with the terms of his offer to the corporation.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

If the proposed transfer is not exempt under section 11 (Section 33‑18‑110(b)), the shareholder may sell his shares only if he obtains an offer from a non‑shareholder who meets the requirements of subsection (b)(1) and (2) of this section. These requirements are designed to protect the corporation and other shareholders against serious adverse tax consequences that might result from having the third person as a shareholder. The mere offer by a shareholder to sell his shares to the corporation at a price he designates does not trigger the first refusal option and other rights provided by this subsection. Any broader rights guaranteeing a market for the shares by the corporation or other shareholders must be provided in a buy‑out agreement. See the Official Comment to section 14 (Section 33‑18‑140).

Subsection (a) also requires that any third‑party offer submitted to the corporation be a cash offer. An offer based on other consideration, such as shares in another corporation, is not a qualifying offer, and unless the shareholder can convince the third party to make a cash offer, the shareholder has no right to sell or transfer his shares to the third party should the corporation refuse to consent to the transfer or to purchase the offered shares. The decision to exclude noncash offers reflects that most third‑party offers are made for cash and that the mechanics of dealing with noncash offers would unduly complicate the statutory framework. If the possibility of receiving noncash offers is considered significant, appropriate language dealing with such offers may be included in the articles of incorporation. Since the corporation cannot match in specific the noncash portion of the third‑party offer, some mechanism, such as arbitration, must be set out to resolve any disputes over the adequacy of an offer made by the corporation to purchase the offered shares.

With respect to a proposed transfer to a third party, subsection (c) encourages the parties to reach an agreement in a reasonably short period of time. The 15‑day interval between the last day for holding a shareholders’ meeting to consider the third‑party offer and the cutoff date for the notice of acceptance is designed to allow time for the corporation and the other shareholders to contact potential third‑party purchasers or shareholders not present at the meeting at which the decision to purchase the shares was taken and to make any necessary arrangements to finance the purchase.

If the corporation does not arrange the purchase of the offered shares, subsection (f) permits their transfer to the third person only if made within 120 days of the date the shareholder notifies the corporation of the third‑party offer. Additionally, the transaction must be consummated on the terms set forth in the notice of the offer. For example, a sale for less than the total price specified in the notice or an installment purchase when a cash sale is specified in the notice would not qualify under this section. If the transfer to the third person is not validly made, the offering shareholder remains subject to the provisions of this section. Thus the shareholder may make a transfer exempt under section 11(b) (Section 33‑18‑110(b)) or obtain another qualifying offer from a third person at any time in the future.

If the transfer to the third party occurs, the shares remain subject to the transfer prohibition in section 11 unless the transferee has no notice or knowledge of the restrictions. See sections 10 and 13 (Sections 33‑18‑100 and 33‑18‑130).

For discussion of subsection (e), see the Official Comment to section 14 (Section 33‑18‑140).

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to the preceding section.

“Cash offer” as used in the Official Comment means dollars a share. Other terms, e.g., installment payment provisions, can be included in a qualifying third party offer. See Section 33‑18‑120(a).

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 12.

CROSS REFERENCES

Acquisition of own shares by, see Section 33‑6‑310.

“Effective date of notice” defined, see Section 33‑1‑410.

“Notice” defined, see Section 33‑1‑410.

Notice includes mail, see Section 33‑1‑400.

Share transfer prohibition of statutory close corporations, generally, see Section 33‑18‑110.

Special shareholders’ meeting, see Section 33‑7‑102.

Voting of shares, see Sections 33‑7‑200 et seq.

Library References

Corporations 113 to 115.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 220 to 228, 233 to 250.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:25 , Close Corporations.

South Carolina Legal and Business Forms Section 1:135 , Stock Transfers‑Prerequisite to Transfer‑Close Corporation‑Prior Offer to Officers and Directors.

**SECTION 33‑18‑130.** Attempted share transfer in breach of prohibition.

 (a) An attempt to transfer shares in a statutory close corporation in violation of a prohibition against transfer binding on the transferee is ineffective.

 (b) An attempt to transfer shares in a statutory close corporation in violation of a prohibition against transfer that is not binding on the transferee, either because the notice required by Section 33‑18‑109 was not given or because the prohibition is held unenforceable by a court, gives the corporation an option to purchase the shares from the transferee for the same price and on the same terms that he purchased them. To exercise its option, the corporation must give the transferee written notice within thirty days after they are presented for registration in the transferee’s name. The corporation may specifically enforce the transferee’s sale obligation upon exercise of its purchase option.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

This section provides additional protection for the effectiveness of the transfer restrictions applicable to the shares of a statutory close corporation. If the required notice of the restrictions has not been given (see section 10 (Section 33‑18‑100)) and the transferee does not have actual notice of the restrictions, the corporation is given a 30‑day option to purchase the shares. If the corporation exercises its option, the proposed transferee may pursue a breach of warranty claim or any other appropriate remedy against the proposed transferor. Section 13 (Section 33‑18‑130) is derived from the Delaware law.

This section also gives the corporation an option to purchase shares attempted to be transferred in violation of a transfer restriction that has been held unenforceable by a court.

SOUTH CAROLINA REPORTERS’ COMMENTS

No changes in the Official Text of the Model Act have been made in this section, which gives a statutory close corporation a thirty‑day option to purchase shares from a transferee when the shares do not have the legend required in Section 33‑18‑109 or when the transferee acquired the shares following a court order declaring a transfer restriction prohibiting the transfer ineffective. If the corporation exercises this option, it must pay the same price and satisfy the other purchase terms of the purchase made by the transferee.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 13.

CROSS REFERENCES

Delivery includes mail, see Section 33‑1‑400.

Effective date of notice, see Section 33‑1‑410.

“Notice” defined, see Section 33‑1‑410.

Share transfer restrictions: generally, see Section 33‑6‑270.

Share transfer restrictions: statutory close corporations, see Section 33‑18‑110.

Library References

Corporations 113.

Westlaw Topic No. 101.

C.J.S. Corporations Section 220.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:57 , Formation‑Statutory Close Corporation.

**SECTION 33‑18‑140.** Compulsory purchase of shares after death of shareholder.

 (a) This section and Sections 33‑18‑150 through 33‑18‑170 apply to a statutory close corporation only if so provided in its articles of incorporation. If these sections apply, the executor or administrator of the estate of a deceased shareholder may require the corporation to purchase or cause to be purchased all (but not less than all) of the decedent’s shares or to be dissolved.

 (b) The provisions of Sections 33‑18‑150 through 33‑18‑170 may be modified only if the modification is set forth or referred to in the articles of incorporation.

 (c) An amendment to the articles of incorporation to provide for application of Sections 33‑18‑150 through 33‑18‑170, or to modify or delete the provisions of these sections, must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of the statutory close corporation, voting as separate voting groups, whether or not otherwise entitled to vote on amendments. If the corporation has no shareholders when the amendment is proposed, it must be approved by at least two‑thirds of the subscribers for shares, if any, or, if none, by all of the incorporators.

 (d) A shareholder who does not vote in favor of an amendment to modify or delete the provisions of Sections 33‑18‑150 through 33‑18‑170 is entitled to dissenters’ rights under Chapter 13 of this title if the amendment upon adoption terminates or substantially alters his existing rights under these sections to have his shares purchased.

 (e) A shareholder may waive his and his estate’s rights under Sections 33‑18‑150 through 33‑18‑170 by a signed writing.

 (f) Sections 33‑18‑150 through 33‑18‑170 do not prohibit any other agreement providing for the purchase of shares upon a shareholder’s death nor do they prevent a shareholder from enforcing any remedy he has independently of these sections.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

1. INTRODUCTION.

Sections 14 through 17 (Sections 33‑18‑140 through 170), which are operative only if the articles of incorporation specifically so provide, guarantee a buy‑out at the death of a shareholder. By including appropriate language in the articles of incorporation, the mandatory buy‑out authorized by this section may be limited to the death of one or more specified shareholders, or to shareholders holding a particular class of shares. It may also be expanded to cover other contingencies—for example, shareholders who retire or who are disabled. Moreover, the statutory language may be modified to change the type of buy‑out. Other commonly used buy‑out arrangements include an optional sell‑optional purchase, mandatory sell‑optional purchase, and mandatory sell‑mandatory purchase, with the seller being a shareholder wishing to dispose of his shares and the purchaser being the corporation, the remaining shareholders, or a combination of the two. The optional sell‑mandatory purchase option was chosen on the ground that it was the one most likely to be chosen by a shareholder in a closely held corporation, all other factors being equal.

The decision to utilize any kind of buy‑out arrangement should be made only after careful consideration of the factors involved in the particular situation. If sections 14 through 17 (Sections 33‑18‑140 through 170) are used, the election must be made in the articles of incorporation by specifying that sections 14 through 17 (Sections 33‑18‑140 through 170) apply. The articles of incorporation may also vary the statutory provisions in any desired manner.

These sections are intended to work in tandem with the share transfer prohibition of section 11 (Section 33‑18‑110). Under the share transfer prohibition there is no obligation to purchase, while under sections 14 through 17 (Section 33‑18‑140 through 170) there is an obligation to purchase by the corporation or the other shareholders if the estate wants to sell; if this obligation is not met, the corporation will be dissolved.

The statute grants the estate of a deceased shareholder the right to compel a purchase of the decedent’s shares since this is the situation most often covered in privately drafted contractual buy‑outs. The problem of illiquidity of close corporation shares is most acute in this situation because the estate frequently needs cash for estate taxes and other purposes. At the same time the remaining shareholders are often concerned about having the decedent’s spouse and children involved in the management of the corporation. A significant amount of shareholder litigation involving close corporations involves disputes between the surviving shareholders and the successors in interest of a deceased shareholder. Having a guaranteed market for the decedent’s shares reduces the likelihood that disputes will arise. Life insurance may be used to fund part or all of the purchase obligation. In the absence of available cash, an installment arrangement may help to alleviate any financial strain on the corporation. The remaining shareholders may agree to purchase some or all of the shares or find a third‑party purchaser if it is undesirable for the corporation to purchase all of the offered shares. Furthermore, if the parties do not have an existing agreement containing a binding price formula or other terms often contained in buy‑out agreements and are unable to agree voluntarily on the price or other terms, a court action may be brought in which a judge in his discretion may resolve the differences and structure a buy‑out plan that is realistic in light of the corporation’s finances.

In summary, assuming some sort of mandatory buy‑out in a particular situation is desirable, the major advantage of electing sections 14 through 17 (Section 33‑18‑140 through 170) is that they provide basic protection in the event the shareholders have failed to enter into an appropriate private agreement, or have entered into a buy‑out agreement but have failed to agree upon a buy‑out price formula, or have agreed upon a formula but have neglected to provide other necessary terms such as interest rates or number of installments in the event deferred purchases are authorized or necessary. Sections 14 through 17 (Sections 33‑18‑140 through 170) do not prevent the shareholders from having an all‑inclusive, buy‑out agreement. See section 14(f) (Section 33‑18‑140(f)). An attorney drafting such an agreement, however, may use the provisions of sections 14 through 17 (Sections 33‑18‑140 through 170) as the basis of the agreement, making any necessary additions and modifications. This procedure may substantially reduce the amount of drafting required.

2. REDEMPTION PROBLEMS.

The ability of a corporation to redeem its shares is subject to legal limitations. Section 6.40 (Section 33‑6‑400) of the revised Model Business Corporation Act sets forth a clear set of principles dealing with permissible redemptions of shares. In states that have not adopted section 6.40 (Section 33‑6‑400), however, the rules vary in many respects. Some states apply the same limitations to redemptions that apply to dividends. Some, however, apply different tests. The result is that a wide variety of insolvency and surplus tests, sometimes in combination, exist. If corporate indebtedness is incurred in connection with a redemption, further it is often unclear in states that have not adopted section 6.40 (Section 33‑6‑400) whether the applicable test must be met at the time the transaction is entered into, at the time payments are made, or at both times. The priority ranking of redemption related corporate debt is also unclear in many of these states.

3. TAX CONSIDERATIONS.

Redemptions also involve complex tax considerations. Some redemptions, principally those that satisfy the requirements of sections 302 and 303 of the Internal Revenue Code, are taxed at capital gains rates rather than dividends under section 301.

Sections 14 through 17 (Sections 33‑18‑140 through 170) are designed to provide flexibility to permit the affected parties to negotiate a purchase scheme that takes tax considerations into account. For example, under section 15(d) (Section 33‑18‑150(d)), a portion or all of the purchase of the decedent’s shares may, with shareholder approval, be allocated to the remaining shareholders or to third parties. This provides the framework by which the interested parties may allocate the shares to minimize the corporate law and tax problems discussed above. If an acceptable allocation cannot be agreed upon, the selling shareholder may, under section 16 (Section 33‑18‑160), reject the offer made by the corporation and file a petition requesting the court to compel a purchase. In framing its decree, the court may consider the problems discussed here. The court may also, under section 16(c) (Section 33‑18‑160(c)), modify its decree on the basis of legal and financial constraints.

Flexibility to deal with other tax problems is also built into sections 14 through 17 (Sections 33‑18‑140 through 170). If certain conditions are met, payment of the estate tax on the deceased shareholder’s estate may be deferred for up to 15 years under section 6166 of the Internal Revenue Code, and interest on the deferred tax will be assessed at a rate considerably lower than the normal rate applicable to late payments. A redemption keyed into maximum use of these provisions may in appropriate cases be quite advantageous to both the estate of the deceased shareholder and to the corporation. Nothing in these sections prohibits the estate of the deceased shareholder and the corporation from working out a redemption plan with the aid of tax and corporate counsel.

An additional tax problem is to assure that the price set for shares in a buy‑out agreement will be accepted for tax purposes as the value of the shares. Tax counsel should be consulted to determine what adjustments if any, will be necessary to achieve this result under a section 18.14 (Section 33‑18‑140) buy‑out agreement.

4. MODIFICATION OF STATUTORY SCHEME.

Sections 14(b) and (c) (Sections 33‑18‑140(b) and (c)) permit the modification of the provisions of sections 14 through 17 (Sections 33‑18‑140 through 170) by a two‑thirds vote of all the shares. Section 14(d) (Section 33‑18‑140(d)) provides that a shareholder who votes against a modification that terminates or substantially alters buy‑out rights previously granted him under these sections has dissenters’ rights to obtain the fair value of his shares. Authorization of dissenters’ rights when statutory buy‑out rights are materially altered represents a compromise between requiring unanimous approval by all interested persons for the alteration and requiring less than unanimous approval but providing no statutory remedy for those opposed to the termination whose rights are adversely affected.

SOUTH CAROLINA REPORTERS’ COMMENTS

Sections 33‑18‑140 through 33‑18‑170 give the estate of a deceased shareholder the right to compel the corporation or other shareholders to purchase the decedent’s shares in a statutory the articles of incorporation specifically state that the statutory buy‑out right is elected. Furthermore, the statutory provisions can be modified by appropriate language in the corporation’s articles of incorporation. Since the statutory scheme gives the estate a “put” right but does not provide any guaranteed purchase rights to the corporation or other shareholders in the event the estate does not exercise its sale rights, it might be advisable in many cases to insert in the articles of incorporation a provision giving the corporation or other shareholders an option to purchase the estate’s share if the estate fails to exercise the purchase right granted by this section. This “call” right also could be included in a separate shareholder buy‑out agreement that supplements the statutory scheme.

The election to use the statutory buy‑out in Sections 33‑18‑140 through 33‑18‑170 should be made only after careful consideration of the financial cost and all the legal and tax problems involved in buy‑out arrangements. See, generally, H. Haynsworth, ORGANIZING A SMALL BUSINESS ENTITY Section 5.04(c) (1986). Alerting lawyers to the need to use caution in choosing any buy‑out scheme is the principal reason why these sections are elective rather than mandatory like the share transfer restriction provision in Sections 33‑18‑110 and 33‑18‑120.

There are several different types of buy‑out arrangements—see paragraph 1 of the Official Comment. The tax consequences of each type may vary considerably. The type used in Sections 33‑18‑140 through 33‑18‑170 is based primarily on considerations other than tax factors. Before choosing this or any other type of buy‑out format, advice from competent tax counsel should be obtained. In this connection, the 1986 Tax Reform Act made several significant changes in the way buy‑out agreements will be taxed.

The only substantive change in the Model Act Official Text in these sections is to amend Section 33‑18‑140(d) so that any shareholder who does not vote in favor of an amendment that modified or deletes the statutory buy‑out right is entitled to assert dissenters’ rights. The reason for this change is explained in the South Carolina Reporters’ Comment to Section 33‑18‑103.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 14.

CROSS REFERENCES

Acquisition of own shares by corporation, see Sections 33‑6‑310 and 33‑6‑400.

Amendment of articles of incorporation, see Sections 33‑10‑101 et seq.

Court action to compel purchase, see Section 33‑18‑160.

Dissenters’ rights, see Sections 33‑13‑101 et seq.

Dissolution: generally, see Sections 33‑14‑101 et seq.

Dissolution: statutory close corporations, see Section 33‑18‑430.

Exercise of compulsory purchase right, see Section 33‑18‑150.

Procedure for compulsory purchase, see Section 33‑18‑150.

Voting by voting groups: amendment of articles of incorporation, see Section 33‑10‑104.

Voting by voting groups: generally, see Section 33‑7‑260.

“Voting group” defined, see Section 33‑1‑400.

Library References

Corporations 82.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 180, 193 to 195.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:57 , Formation‑Statutory Close Corporation.

**SECTION 33‑18‑150.** Exercise of compulsory purchase right.

 (a) A person entitled and desiring to exercise the compulsory purchase right described in Section 33‑18‑140 must deliver a written notice to the corporation, within one hundred twenty days after the death of the shareholder, describing the number and class or series of shares beneficially owned by the decedent and requesting that the corporation offer to purchase the shares.

 (b) Within twenty days after the effective date of the notice, the corporation shall call a special shareholders’ meeting, to be held not more than forty days after the call, to decide whether the corporation should offer to purchase the shares. A purchase offer must be approved by the affirmative vote of the holders of a majority of votes entitled to be cast at the meeting, excluding votes in respect of the shares covered by the notice.

 (c) The corporation must deliver a purchase offer to the person requesting it within seventy‑five days after the effective date of the request notice. A purchase offer must be accompanied by the corporation’s balance sheet as of the end of a fiscal year ending not more than sixteen months before the effective date of the request notice, an income statement for that year, a statement of changes in shareholders’ equity for that year, and the latest available interim financial statements, if any. The person must accept the purchase offer in writing within fifteen days after receiving it or the offer is rejected.

 (d) A corporation agreeing to purchase shares under this section may allocate some or all of the shares to one or more of its shareholders or to other persons if all the shareholders voting in favor of the purchase offer approve the allocation. If the corporation has more than one class or series of shares, the remaining holders of the class or series of shares being purchased are entitled to a first option to purchase the shares not purchased by the corporation in proportion to their shareholdings or in some other proportion agreed to by all the shareholders participating in the purchase.

 (e) If price and other terms of a compulsory purchase of shares are fixed or are to be determined by the articles of incorporation, bylaws, or a written agreement, the price and terms so fixed or determined govern the compulsory purchase unless the purchaser defaults, in which event the buyer is entitled to commence a proceeding for dissolution under Section 33‑18‑160.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

Section 15 (Section 33‑18‑150) sets out the mechanics of exercising the buy‑out option. The procedures are similar to those in section 12 (Section 33‑18‑120) relating to third‑party offers. Like section 12 (Section 33‑18‑120), this section requires that the selling shareholder offer all of his shares for sale on the premise that a shareholder desiring to cash out his interest in the corporation ought to divest himself of all his equity interest in the business. If fewer than all his shares are offered the shareholder may pursue his rights, if any, under the corporation’s share transfer restrictions.

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to the preceding section.

Note that pursuant to subsection (e), the price and other terms of any shares to be purchased under the statutory buy‑out right in Sections 33‑18‑140 through 33‑18‑170 can be established by the articles of incorporation, bylaws, or a written agreement between the shareholders and the corporation; otherwise the value will be the fair value of the shares as determined by a court action. The court can require other terms such as installment payments with interest. See Section 33‑18‑160. Buy‑out agreements often specify a price such as book value or capitalized earnings that may or may not be the same as the fair value of the shares or, even if fair value is the standard, specify a nonjudicial method of determining the fair value (for example, appraisal or arbitration).

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 15.

CROSS REFERENCES

Compulsory purchase of shares after death of shareholder, see Section 33‑18‑140.

Court action to compel purchase, see Section 33‑18‑160.

Delivery includes mail, see Section 33‑1‑400.

“Effective date of notice” defined, see Section 33‑1‑410.

Financial statements for shareholders, see Section 33‑16‑200.

“Notice” defined, see Section 33‑1‑410.

Special shareholders’ meeting, see Section 33‑7‑102.

Voting of shares, see Sections 33‑7‑200 et seq.

Library References

Corporations 82, 115.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 180, 193 to 195, 233 to 250.

**SECTION 33‑18‑160.** Court action to compel purchase.

 (a) If an offer to purchase shares made under Section 33‑18‑150 is rejected or, if no offer is made, the person exercising the compulsory purchase right may commence a proceeding against the corporation to compel the purchase in the circuit court of the county where the corporation’s principal office (or, if none in this State, its registered office) is located. The corporation at its expense shall notify in writing all of its shareholders, and any other person the court directs, of the commencement of the proceeding. The jurisdiction of the court in which the proceeding is commenced under this subsection is plenary and exclusive.

 (b) The court shall determine the fair value of the shares subject to compulsory purchase in accordance with the standards set forth in Section 33‑18‑420 together with terms for the purchase. Upon making these determinations the court shall order the corporation to purchase or cause the purchase of the shares or empower the person exercising the compulsory purchase right to have the corporation dissolved.

 (c) After the purchase order is entered, the corporation may petition the court to modify the terms of purchase and the court may do so if it finds that changes in the financial or legal ability of the corporation or other purchaser to complete the purchase justify a modification.

 (d) If the corporation or other purchaser does not make a payment required by the court’s order within thirty days of its due date, the seller may petition the court to dissolve the corporation and, absent a showing of good cause for not making the payment, the court shall do so.

 (e) A person making a payment to prevent or cure a default by the corporation or other purchaser is entitled to recover the payment from the defaulter.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The rationale for a judicial proceeding to determine the fair value of shares and other terms of the buy‑out is explained in the Official Comment to section 15 (Section 33‑18‑150). The power of the court under section 17 (Section 33‑18‑170) to allocate all costs and counsel fees incurred in the suit should provide an adequate incentive for both sides to act in good faith. No court action will be necessary, however, if the buy‑out price and other terms are established pursuant to a written agreement among the shareholders or provisions in the articles of incorporation or bylaws. See section 15(e) (Section 33‑18‑150(e)).

If a suit to determine the fair value of shares is brought, the court has discretion to include in its order any conditions it feels are justified on the basis of the financial and other needs of the selling shareholder and of the purchaser. The court, for example, may authorize an installment sale. The order may include a provision for interest and may require collateral to secure the unpaid installments.

If the purchase is not consummated or the purchasers default, the shareholder may petition for dissolution of the corporation. The court may deny the petition for good cause shown. The proceeding, however, affords the corporation an opportunity to be heard on the matter and an opportunity to avoid dissolution. Mandatory dissolution in the event the offered shares are not purchased provides a strong incentive for the corporation and the remaining shareholders either to purchase the shares or to find another purchaser. Presumably, the corporation and other shareholders would refuse to purchase if the corporation’s financial prospects were bleak. If this is the case, then dissolution may be the appropriate solution. Under section 15 (Section 33‑18‑150) the other shareholders are given reasonable time to come up with a purchasing group and the court has power to authorize an installment purchase and any other terms that are necessary to enable the purchasing group to finance the purchase without undue financial strain on the corporation or other purchasers.

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to the preceding two sections.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 16.

CROSS REFERENCES

Appointment of appraisers, see Section 33‑18‑420.

Appraisal, see Section 33‑18‑420.

Compulsory purchase of shares after death of shareholder, see Section 33‑18‑140.

Court costs and expenses, see Section 33‑18‑170.

Dissolution: generally, see Sections 33‑14‑101 et seq.

Dissolution: statutory close corporations, see Section 33‑18‑430.

Exercise of compulsory purchase right, see Section 33‑18‑150.

“Notice” defined, see Section 33‑1‑410.

Principal office: defined, see Section 33‑1‑400.

“Proceeding” defined, see Sections 33‑1‑400 and 33‑8‑500.

Registered office: required, see Section 33‑5‑101.

Library References

Corporations 115.1.

Westlaw Topic No. 101.

C.J.S. Corporations Section 234.

**SECTION 33‑18‑170.** Court costs and other expenses.

 (a) The court in a proceeding commenced under Section 33‑18‑160 shall determine the total costs of the proceeding, including the reasonable compensation and expenses of appraisers appointed by the court and of counsel and experts employed by the parties. Except as provided in subsection (b), the court shall assess these costs equally against the corporation and the party exercising the compulsory purchase right.

 (b) The court may assess all or a portion of the total costs of the proceeding:

 (1) against the person exercising the compulsory purchase right if the court finds that the fair value of the shares does not substantially exceed the corporation’s last purchase offer made before commencement of the proceeding and that the person’s failure to accept the offer was arbitrary, vexatious, or otherwise not in good faith; or

 (2) against the corporation if the court finds that the fair value of the shares substantially exceeds the corporation’s last sale offer made before commencement of the proceeding and that the offer was arbitrary, vexatious, or otherwise not made in good faith.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

See the Official Comment to section 16 (Section 33‑18‑160).

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to Sections 33‑18‑140 and 33‑18‑150.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 16.

CROSS REFERENCES

Appraisers, see Section 33‑18‑420.

Compulsory purchase of shares after death of shareholder, see Section 33‑18‑140.

“Proceeding” defined, see Section 33‑1‑400.

Library References

Corporations 115.1.

Westlaw Topic No. 101.

C.J.S. Corporations Section 234.

RESEARCH REFERENCES

Encyclopedias

S.C. Jur. Attorney Fees Section 38, Compulsory Purchase Right Actions Against Statutory Close Corporations.

Forms

South Carolina Legal and Business Forms Section 1:57 , Formation‑Statutory Close Corporation.

ARTICLE 3

Governance

**SECTION 33‑18‑200.** Shareholder agreements.

 (a) All the shareholders of a statutory close corporation may agree in writing to regulate the exercise of the corporate powers and the management of the business and affairs of the corporation or the relationship among the shareholders of the corporation.

 (b) An agreement authorized by this section is effective although:

 (1) it eliminates a board of directors;

 (2) it restricts the discretion or powers of the board or authorizes director proxies or weighted voting rights;

 (3) its effect is to treat the corporation as a partnership; or

 (4) it creates a relationship among the shareholders or between the shareholders and the corporation that would otherwise be appropriate only among partners.

 (c) If the corporation has a board of directors, an agreement authorized by this section restricting the discretion or powers of the board relieves directors of liability imposed by law and imposes that liability on each person in whom the board’s discretion or power is vested to the extent that the discretion or powers of the board of directors are governed by the agreement.

 (d) A provision eliminating a board of directors in an agreement authorized by this section is not effective unless the articles of incorporation contain a statement to that effect as required by Section 33‑18‑210.

 (e) A provision entitling shareholders to dissolve the corporation under Section 33‑18‑330 is effective only if a statement of this right is contained in the articles of incorporation.

 (f) To amend an agreement authorized by this section, all the shareholders must approve the amendment in writing unless the agreement provides otherwise.

 (g) Subscribers for shares may act as shareholders with respect to an agreement authorized by this section if shares are not issued when the agreement was made.

 (h) This section does not prohibit any other agreement between or among shareholders in a statutory close corporation.

HISTORY: Derived from 1976 Code Section 33‑11‑220 [1962 Code Section 12‑16.22; 1962 (52) 1996; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 2]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

This section authorizes the shareholders to make any agreement they wish regulating the business of the corporation and their relationship to one another and to the corporation. Examples of provisions that may be included in an agreement are:

(1) The management of the business and the affairs of the corporation in whole or in part may be by or under the direction of all the shareholders of the corporation or by or under the direction of one or more shareholders or third parties selected by the shareholders.

(2) One or more shareholders may be given power to dissolve the corporation at will or upon the occurrence of a specified event or contingency.

(3) The manner of exercising or dividing voting power by the shareholders and directors may be established, and the use of director as well as shareholder proxies may be authorized.

(4) The terms and conditions of employment of any officer or employee of the corporation may be established, regardless of the length of employment.

(5) The identity of the directors and officers of the corporation may be established.

(6) The payment of dividends or division of profits may be established.

(7) Issues as to which the shareholders or directors are deadlocked may be made subject to arbitration, or arbitration may be required for any issue of disagreement between a shareholder in his capacity as a shareholder, director, officer, or employee and the corporation, or the other shareholders.

All the shareholders must enter into the agreement and if the agreement specifies that the corporation is not to have a board of directors or that one or more shareholders is to have a special right to dissolve the corporation, the articles of incorporation must include appropriate language authorizing these provisions. See sections 21 and 33 (Sections 33‑18‑210 and 33‑18‑330).

A shareholder agreement is valid and enforceable under this section even if it, in effect, permits the business to be operated essentially as a partnership without a board of directors. See subsection (b). Close corporations in which most or all of the shareholders are employees of the corporation are often referred to as “incorporated partnerships.” This section gives legal sanction to the customary arrangements made by the shareholders of these corporations. Section 25 (Section 33‑18‑250) reinforces this concept by providing that shareholder limited liability is to be recognized in spite of an agreement that the corporation is to be operated essentially as a partnership.

This Supplement does not deal with the effect of a shareholder agreement on the tax status of the corporation. In some circumstances the agreement may result in the taxation of the business as a partnership. See Treas. Regs. Sections 301.7701‑1 through ‑3 (1960).

The requirement of unanimity for adoption and amendment is based on the unusual nature of an agreement that so radically alters the normal corporate structure.

Subsection (h) preserves the right of shareholders to enter into any other type of shareholder voting agreement or voting trust or similar agreement that is authorized in the state’s general business corporation statutes. These statutes do not ordinarily require unanimous approval by the shareholders but in general they do not authorize as much flexibility, particularly with respect to restrictions on the normal powers of directors, as is permitted under this section. They also often contain time limitations and other restrictions that may be undesirable. See, e.g. MBCA section 7.30 (Section 33‑7‑300) (voting trust is valid for 10 years).

The shareholders of a statutory close corporation may choose to operate with or without a board of directors. Section 21 (Section 33‑18‑210) deals specifically with the requirements for making this election and the legal consequences of operating without a board of directors. If the corporation has a board of directors, any responsibilities required to be exercised by the board of directors may be delegated to one or more of the shareholders or to third parties selected by the shareholders.

If the shareholders exercise the traditional management rights and duties required by statute to be exercised by the board of directors or have delegated these rights and duties to others, they also assume the same liability as would otherwise be imposed on the directors for failure to exercise these rights or to carry out those duties in an appropriate fashion. The shareholders who assume the duties of directors would, however, be eligible for indemnification under chapter 8, Art. 5 of the Revised Model Act. See the Official Comment to section 21 (Section 33‑18‑210). If the corporation has a board of directors, the directors are responsible for the appropriate exercise of any management rights they have power to exercise and would be liable for their failure to carry out their duties.

This section is derived from similar provisions in the Maryland and Texas close corporation statutes with stylistic changes.

SOUTH CAROLINA REPORTERS’ COMMENTS

1. In the absence of specific statutory authority such as that contained in this and the succeeding sections, shareholder agreements that deal with dividends, the selection, terms and payment of executives, and other issues that are normally decided by the board of directors are legally suspect on the grounds that they improperly interfere with the statutory authority of the board to manage the business and affairs of the corporation. See H.F. O’Neal, CLOSE CORPORATIONS Section 5.06, 5.16 (2nd ed. 1971); H. Haynsworth, ORGANIZING A SMALL BUSINESS ENTITY, Section 5.02(g) (1986).

2. This section differs from Section 33‑11‑220 of the 1981 South Carolina Business Corporation Act in the following respects:

(a) No notice of the agreement in the articles of incorporation is required unless the corporation will not have a board of directors (Section 33‑18‑210) or a special right of dissolution exists (see Section 33‑18‑330). Section 33‑11‑220 required that the agreement be “set forth or its existence is clearly referred to, in the articles of incorporation.”

(b) No special notice of the agreement needs to be placed on the share certificates. Cf. Section 33‑18‑109 (legend required to be on the share certificates of a statutory close corporation). Section 33‑11‑220 required that the “text or a summary” of the agreement “shall be conspicuously on the face of every certificate for shares.”

(c) No maximum time limitation is imposed by this section. Section 33‑11‑220, however, imposed a ten year maximum term, with a right of renewal by unanimous consent of all the shareholders at any time within one year before expiration. Although the shareholders may want to limit the term of an agreement authorized by this section, there is no compelling public policy reason for a statutorily imposed time limitation. The shareholders may want at least some of the provisions commonly found in these type of agreements, for example, employment rights, to last longer than ten years. The only ways to achieve this under Section 33‑11‑220 were (1) to draft a special provision stating that the particular provisions are effective even if the Section 33‑11‑220 agreement terminates, or (2) to draft a separate agreement encompassing the provisions that are to last beyond ten years. Both alternatives are contrary to the underlying philosophy of these type statutes to allow the shareholders in a closely held corporation to enter into a comprehensive shareholder‑management agreement similar to a partnership agreement. Moreover, in many situations, the necessity for an enforceable agreement like this is greatest after the corporation has been in existence for several years and tensions have developed between the shareholders. An unreasonable shareholder with knowledge that the agreement expires soon can use this fact as leverage to extract unfair concessions from the remaining shareholders as a trade‑off for consent to renew the agreement. In any case, the shareholders, if they wish, may include a provision limiting the term of an agreement governed by this section.

(d) Under this section, if the corporation has a board of directors but delegates some of the normal board responsibilities to other persons, only those persons with delegated responsibilities assume liabilities as directors. Under Section 33‑11‑220(e), on the other hand, all the shareholders, whether or not they personally assumed any board responsibilities, were liable “for managerial acts or omissions that is (sic) imposed by law upon the board of directors to the extent that and so long as the discretion or powers of the board of directors in their management of corporate affairs is controlled by any such provision.”

(e) If there is no board of directors, a shareholder is liable only as a director if he has the right to vote on a particular issue. See Section 33‑18‑230(c)(3). All shareholders, regardless of voting rights, were liable as directors under Section 33‑11‑220(e). See (d) supra.

(f) Under this section, a provision in the agreement allowing an amendment by fewer than all the shareholders is enforceable. Assuming the agreement does not have a definite termination date, or even if it does, such a provision may be advisable as a means to protect against possible minority tyranny. The status of such a provision under Section 33‑11‑220 was very unclear.

(g) This section does not have a provision similar to Section 33‑11‑220(c) prohibiting the trading of securities of a corporation operating under a shareholder‑management agreement. As a practical matter, however, it is extremely unlikely that a corporation with this type of agreement would ever have registered securities.

3. No substantive changes in the Model Act Official Text have been made in this section.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 20.

CROSS REFERENCES

Amendment of articles of incorporation, see Sections 33‑10‑101 et seq.

Annual meeting, see Section 33‑18‑230.

Bylaws, see Section 33‑18‑220.

Dissolution at option of shareholder, see Section 33‑18‑330.

Elimination of board of directors, see Section 33‑18‑210.

Indemnification, see Sections 33‑8‑500 through 33‑8‑580.

“Shareholder” defined, see Section 33‑1‑400.

Standards of conduct for directors, see Sections 33‑8‑300 through 33‑8‑320.

Subscriptions for shares, see Section 33‑6‑200.

Voting agreements, see Section 33‑7‑310.

Voting trusts, see Section 33‑7‑300.

Library References

Corporations 180.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 327 to 330.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:25 , Close Corporations.

**SECTION 33‑18‑210.** Elimination of board of directors.

 (a) A statutory close corporation may operate without a board of directors if its articles of incorporation contain a statement to that effect.

 (b) An amendment to articles of incorporation eliminating a board of directors must be approved by all the shareholders of the corporation, whether or not otherwise entitled to vote on amendments or, if no shares have been issued, by all the subscribers for shares, if any, or, if none, by all the incorporators.

 (c) While a corporation is operating without a board of directors as authorized by subsection (a):

 (1) all corporate powers must be exercised by or under the authority of, and the business and affairs of the corporation managed under the direction of, the shareholders;

 (2) unless the articles of incorporation provide otherwise, (i) action requiring director approval or both director and shareholder approval is authorized if approved by the shareholders and (ii) action requiring a majority or greater percentage vote of the board of directors is authorized if approved by the majority or greater percentage of the votes of shareholders entitled to vote on the action;

 (3) a shareholder is not liable for his act or omission, although a director would be, unless the shareholder was entitled to vote on the action;

 (4) a requirement by a state or the United States that a document delivered for filing contain a statement that specified action has been taken by the board of directors is satisfied by a statement that the corporation is a statutory close corporation without a board of directors and that the action was approved by the shareholders;

 (5) the shareholders by resolution may appoint shareholders to sign documents as “designated directors”.

 (d) An amendment to articles of incorporation deleting the statement eliminating a board of directors must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of the corporation, voting as separate voting groups, whether or not otherwise entitled to vote on amendments. The amendment also must specify the number, names, and addresses of the corporation’s directors or describe who will perform the duties of a board under Section 33‑8‑101.

HISTORY: Derived from 1976 Code Section 33‑11‑220 [1962 Code Section 12‑16.22; 1962 (52) 1996; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 2]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

This section permits a statutory close corporation to dispense with a board of directors if a statement to that effect is included in its articles of incorporation. See the Official Comment to Section 3 (Section 33‑18‑103). It also sets out the consequences of this election. It is derived from the Maryland close corporation statute.

The shareholders of a statutory close corporation operating without a board of directors have the legal liability imposed by law on directors for managing the business and affairs of the corporation. They may appoint one or more persons to perform their duties but they are collectively liable for any mismanagement. They also have the usual duties of directors and must either hold a meeting or join in a written consent to initiate or to approve action required by statute to be taken by directors. If this option is exercised, it also is not necessary to call for an organizational meeting of directors or to hold other directors’ meetings; the statutory requirements may be fulfilled by shareholders’ meetings.

One difference between this section and the Maryland provision and the provisions found in the statutes of other states that have followed the Maryland model is found in subsection (c)(5), authorizing “designated directors” to satisfy a party dealing with the corporation who requests that certain documents be signed or approved by “directors.” Some banks and creditors have in the past refused to accept documents that do not meet specified corporate formalities. This subsection creates an admittedly artificial but practical method of satisfying this objection. The designated directors do not expose themselves to additional liability by signing documents as designated directors.

Subsection (c)(2) provides that the shareholder vote on action normally requiring director approval is tallied in the same manner as at any meeting of shareholders, i.e. the vote is tallied by shares rather than per capita by individual shareholders. This rule may be changed by an appropriate provision in the articles of incorporation. For example, if the articles of incorporation so state, shareholders may vote on a one‑vote‑per‑person basis (as is the normal rule for directors’ votes) rather than the one‑vote‑per‑share rule applicable to shareholders. The shareholder voting rule is utilized as the standard rule because it is the option most likely to be chosen. A weighted voting plan that gives one or more shareholders either a general veto power or the power to veto in designated cases is also permissible. If a corporation has different classes or series of shares with voting rights to all classes or series of shares on a particular issue, either together or as separate voting groups, the requisite vote of the various classes or series of shares must be obtained to validate the transaction. The vote under subsection (c)(2) only satisfies any requirement for director approval of proposed action.

Although unanimous approval is necessary to elect to dispense with a board of directors, the election can be terminated under subsection (d) by a two‑thirds vote of all shares. Operating without a board of directors is such a radical departure from traditional corporate law that it should not be undertaken unless all the shareholders agree because additional liabilities may be incurred as a result of the election. Terminating the election, however, reinstates the statutory requirements for a board of directors; and a two‑thirds vote, which is the voting standard used in this Supplement for most fundamental structural changes, seems sufficient. A corporation with 50 or fewer shareholders that elects not to have a board of directors under section 8.01 (Section 33‑8‑101) of the Revised Model Act, however, may make and terminate the election under that statute by majority vote.

If a corporation without a board of directors terminates its status as a statutory close corporation, it must immediately elect directors unless it has 50 or fewer shareholders and chooses to operate without a board under MBCA Section 8.01 (Section 33‑8‑101).

SOUTH CAROLINA REPORTERS’ COMMENTS

For the reasons stated in the South Carolina Reporters’ Comments to Section 33‑18‑200, this section is an improvement over Section 33‑11‑220 of the 1981 South Carolina Business Corporation Act.

The reference in the last paragraph of the Official Comment to a fifty shareholder limit for operation without a board of directors is not applicable in South Carolina. See the South Carolina Reporters’ Comments to Section 33‑8‑101.

No substantive changes have been made in the Model Act Official Text.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 21.

CROSS REFERENCES

Articles of incorporation: amendment, see Sections 33‑10‑101 et seq.

Articles of incorporation: generally, see Section 33‑2‑102.

Board of directors: action, see Sections 33‑8‑101 through 33‑8‑250.

Board of directors: standards of conduct, see Sections 33‑8‑300 through 33‑8‑320.

Bylaws: amendment, see Sections 33‑10‑200 et seq.

Bylaws: generally, see Section 33‑2‑106.

Bylaws: statutory close corporations, see Section 33‑18‑220.

Incorporators, see Section 33‑2‑101.

Number of directors, see Section 33‑8‑103.

Subscriptions for shares, see Section 33‑6‑200.

Termination of statutory close corporation status, see Section 33‑18‑310.

Voting by voting groups: amendment of articles of incorporation, see Section 33‑10‑104.

Voting by voting groups: generally, see Sections 33‑7‑250 and 33‑7‑260.

“Voting group” defined, see Section 33‑1‑400.

Library References

Corporations 281.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 433 to 434.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:57 , Formation‑Statutory Close Corporation.

**SECTION 33‑18‑220.** Bylaws.

 (a) A statutory close corporation need not adopt bylaws if provisions required by law to be contained in bylaws are contained in either the articles of incorporation or a shareholder agreement authorized by Section 33‑18‑200.

 (b) If a corporation does not have bylaws when its statutory close corporation status terminates under Section 33‑18‑310, the corporation shall adopt bylaws immediately under Section 33‑2‑106.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The purpose of bylaws is to provide regulations for the management of a corporation. Business corporation statutes universally require that a corporation adopt bylaws. Very few, however, specify more than a few mandatory provisions that must be included in the bylaws. For example, under the MBCA, the mandatory requirements are: (1) the time and place of shareholder meetings (Section 7.01) (Section 33‑7‑101); (2) the number of directors (Section 8.3) (Section 33‑8‑103); (3) the notice to be given of directors’ meetings (Section 8.22) (Section 33‑8‑220): and (4) the time, method of election, and authority of the officers (Sections 8.40 and 8.41) (Sections 33‑8‑400 and 33‑8‑410). Moreover, under section 2.06 (Section 33‑2‑106) any provision required or permitted to be in the bylaws may be placed in the articles of incorporation.

Since the type of shareholder agreement contemplated by section 20 (Section 33‑18‑200) includes much of the information normally included in bylaws, requiring the adoption of bylaws in many cases involves unnecessary duplication. This is particularly true in closely held corporations in which most or all of the investors are active in the business. These corporations normally operate on an informal basis. The highly structured formalities in typical bylaws, although necessary in larger corporations with numerous shareholders, can be cumbersome when imposed on closely held corporations.

This section gives a statutory close corporation the option to dispense with bylaws, if the matters required by statute to be included in bylaws are contained in either a section 20 (Section 33‑18‑200) shareholder agreement or in the articles of incorporation. Although this represents a break with tradition, it is generally consistent with the “incorporated partnership” concept (see the Comment to section 20)(Section 33‑18‑200)) and makes certain that all the information legally required to be in bylaws will be readily accessible to the shareholders.

SOUTH CAROLINA REPORTERS’ COMMENTS

1. As the Official Comment indicates, allowing a close corporation to operate without adoption of formal bylaws is not as radical as it may appear at first glance. In fact, Section 33‑11‑100(a) of the 1981 South Carolina Business Corporation Act states that “ [a]ny provision which may properly appear in the bylaws may be included in the articles of incorporation.”

Moreover, reliance on bylaws to protect rights of minority shareholders can prove to be a trap for the unwary. For example, in Blount v. Taft, 29 N.C. App. 626, 225 S.E.2d 583 (1976), aff’d on other grounds, 295 N.C. 472, 246 S.E.2d 763 (1978), the majority of the board of directors amended the bylaws of a close corporation to eliminate a provision requiring unanimous consent to hire new employees. Subsequently, certain relatives of the majority shareholders whose employment had been opposed by another shareholder faction were hired. This action was upheld on the grounds that under the North Carolina Business Corporation Act a majority of the directors can amend a corporation’s bylaws without any shareholder approval unless the articles of incorporation otherwise provide. The statutory provisions for amendments of bylaws in this act are similar to the North Carolina statute. See Sections 33‑10‑200 through 33‑10‑220.

Assuming a close corporation decides to have bylaws, a provision requiring a supermajority vote for director amendments to the bylaws or, alternatively, a provision requiring all bylaw amendments be approved by a supermajority vote of shareholders can be used to protect a minority shareholder against the type of action taken in Blount v. Taft.

2. The option not to have bylaws should be particularly attractive for subsidiary corporations of holding companies.

3. No substantive changes in the Model Act Official Text have been made.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 22.

CROSS REFERENCES

Articles of incorporation: amendment, see Sections 33‑10‑101 et seq.

Articles of incorporation: generally, see Section 33‑2‑102.

Bylaws: adoption, see Section 33‑2‑106.

Bylaws: amendment, see Sections 33‑10‑200 et seq.

Shareholder agreement, see Section 33‑18‑200.

Termination of statutory close corporation status, see Section 33‑18‑310.

Library References

Corporations 54.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 111, 114 to 116, 120.

RESEARCH REFERENCES

Treatises and Practice Aids

Fletcher Cyclopedia Law of Private Corporations Section 4210.10, Close Corporations.

**SECTION 33‑18‑230.** Annual meeting.

 (a) The annual meeting date for a statutory close corporation is the first business day after May thirty‑first unless its articles of incorporation, bylaws, or a shareholder agreement authorized by Section 33‑18‑200 fixes a different date.

 (b) A statutory close corporation need not hold an annual meeting unless one or more shareholders deliver written notice to the corporation requesting a meeting at least thirty days before the meeting date determined under subsection (a).

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

This section, which is derived from the Maryland close corporation statute, requires that a statutory close corporation establish a date for an annual shareholders’ meeting but provides that the meeting need not be held unless demanded. Under the Revised Model Business Corporation Act and most state corporation statutes, an annual meeting appears to be mandatory. See the Official Comment to MBCA section 7.01 (Section 33‑7‑101).

SOUTH CAROLINA REPORTERS’ COMMENTS

Because most closely held corporations operate on an informal basis, no real purpose is served by requiring an annual meeting unless one of the shareholders feels it would be desirable. This is particularly true when the shareholders have a Section 33‑18‑200 agreement which specifies who the officers and directors (if any) will be.

The fact that no annual meeting is required does not mean that minutes documenting all significant corporate action do not need to be prepared. Consent minutes should be used for this purpose. See Sections 33‑7‑104 and 33‑11‑210.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 23.

CROSS REFERENCES

Annual meetings, generally, see Section 33‑7‑101.

Articles of incorporation: amendment, see Sections 33‑10‑101 et seq.

Articles of incorporation: generally, see Section 33‑2‑102.

Bylaws: adoption, see Section 33‑2‑106.

Bylaws: amendment, see Sections 33‑10‑200 et seq.

Court‑ordered meeting, see Section 33‑7‑103.

“Deliver” includes mail, see Section 33‑1‑400.

Meeting notice, see Section 33‑7‑105.

“Notice” defined, see Section 33‑1‑410.

Shareholder agreement, see Section 33‑18‑200.

“Shareholder” defined, see Section 33‑1‑400.

Library References

Corporations 191, 193, 194.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 362 to 365, 374.

**SECTION 33‑18‑240.** Execution of document in more than one capacity.

 An individual who holds more than one office in a statutory close corporation may execute, acknowledge, or verify in more than one capacity any document required to be executed, acknowledged, or verified by the holders of two or more offices.

HISTORY: Derived from 1976 Code Section 33‑13‑130 [1962 Code Section 12‑18.13; 1962 (52) 1996; 1963 (53) 327; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 2]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

This section, which is derived from the Maryland close corporation statute, is designed to facilitate the authentication of documents in a statutory close corporation. Many small corporations have only one shareholder or one officer.

SOUTH CAROLINA REPORTERS’ COMMENTS

This section does not change the South Carolina law. See Section 33‑13‑130(d) of the 1981 South Carolina Business Corporation Act.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 24.

CROSS REFERENCES

Filing requirements, see Section 33‑1‑200.

Holding two or more offices simultaneously, see Section 33‑8‑400.

Secretary of corporation, see Section 33‑1‑400.

Library References

Corporations 310.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 475, 477 to 489.

LAW REVIEW AND JOURNAL COMMENTARIES

Annual survey of South Carolina law: Corporate law. 46 S.C. L. Rev. 191 (Autumn 1994).

**SECTION 33‑18‑250.** Limited liability.

 The failure of a statutory close corporation to observe the usual corporate formalities or requirements relating to the exercise of its corporate powers or management of its business and affairs is not a ground for imposing personal liability on the shareholders for liabilities of the corporation.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The purpose of this section is to eliminate the possible argument that the shareholders in a statutory close corporation are individually liable for the debts and torts of the business because the corporation did not follow the classical model of a corporation. Pursuant to sections 20, 21 and 33 (Sections 33‑18‑200, ‑210 and 330), a statutory close corporation may in effect function like a partnership, although legally the business is still a corporation. This section does not prevent a court from “piercing the corporate veil” of a statutory close corporation if the circumstances should justify imposing personal liability on the shareholders were the corporation not a statutory close corporation. It merely prevents a court from “piercing the corporate veil” because it is a statutory close corporation.

The section is derived from the California close corporation provisions.

SOUTH CAROLINA REPORTERS’ COMMENTS

Although this section may be criticized as being self‑serving, it is desirable because it reminds courts and lawyers that a closely held corporation should be respected as a separate entity even though it may have the managerial structure of a partnership.

No substantive changes in the Model Act text have been made.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 25.

CROSS REFERENCES

Dissolution at option of shareholder, see Section 33‑18‑330.

Elimination of board of directors, see Section 33‑18‑210.

Liability for pre‑incorporation transactions, see Section 33‑2‑104.

Library References

Corporations 215.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 414, 417, 425.

NOTES OF DECISIONS

In general 1

1. In general

The trial court properly pierced the corporate veil to make the majority shareholder individually and personally liable for his corporation’s admitted debt where he and his wife owned 100 percent of the stock and were the only 2 officers and directors, the corporation was headquartered in their home, they set his salary based on what was needed to meet their expenses at home, they held neither formal directors’ meetings nor shareholders’ meetings, they neither declared nor distributed dividends on outstanding stock, and he knew of the corporate debt, yet used available money for other purposes. Cumberland Wood Products, Inc. v. Bennett (S.C.App. 1992) 308 S.C. 268, 417 S.E.2d 617.

Chapter 7 debtor‑clothing manufacturer’s president could not be held personally liable for unpaid rent on sewing equipment that was temporarily transferred by debtor to foreign corporation that it created for production outsourcing; president was not a party to the rental contract between debtor and foreign corporation, and grounds did not exist to pierce the corporate veil with respect to any of the companies involved in the case. In re Southern Textile Knitters (C.A.4 (S.C.) 2003) 65 Fed.Appx. 426, 2003 WL 124771, Unreported. Corporations And Business Organizations 1960

ARTICLE 4

Reorganization and Termination

**SECTION 33‑18‑300.** Merger, share exchange, and sale of assets.

 (a) A plan of merger or share exchange that, if effected, would:

 (1) terminate statutory close corporation status must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of the statutory close corporation, voting as separate voting groups, whether or not the holders are otherwise entitled to vote on the plan;

 (2) create the surviving corporation as a statutory close corporation must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of each constituent corporation, voting as separate voting groups, whether or not the holders are otherwise entitled to vote on the plan.

 (b) A sale, lease, exchange, or other disposition of all or substantially all of the property (with or without the good will) of a statutory close corporation, if not made in the usual and regular course of business, must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of the corporation, voting as separate voting groups, whether or not the holders are otherwise entitled to vote on the transaction.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

Section 31 (Section 33‑18‑310) requires a minimum two‑thirds vote of every class or series of shares whether or not otherwise entitled to vote to terminate close corporation status. Each class or series is entitled to vote as a separate voting group. Section 30 (Section 33‑18‑300) imposes the same voting requirement in transactions that have the effect of terminating a corporation’s status as a statutory close corporation.

In addition, under subsection (a)(2), the shareholders of a corporation that will become a statutory close corporation in a merger or share exchange must approve the transaction by the same minimum two‑thirds vote. This is consistent with section 3(b) (Section 33‑18‑103(b)) which requires that an amendment to the articles of incorporation that results in an existing corporation becoming a statutory close corporation also be approved by a two‑thirds vote.

The exceptions to shareholder approval of mergers or share exchanges for subsidiary mergers and some other types of transactions (in MBCA chapter 11) do not apply to statutory close corporations since a shareholder vote is required in all circumstances where statutory close corporation status is elected or terminated.

Shareholders of a statutory close corporation who vote against the merger, share exchange, or sale not in the regular course of business of all or substantially all the assets have dissenters’ rights under MBCA chapter 13.

Section 31(b) (Section 33‑18‑310(b)) requires that a sale of all or substantially all the assets of a corporation not in the regular course of business be approved by a two‑thirds vote of all classes or series of shares, voting as separate voting groups, whether or not they are otherwise entitled to vote. Chapter 12 of the Revised Model Business Corporation Act does not require a vote by voting groups on such a sale (unless otherwise required by the articles of incorporation or by action of the board of directors) and limits the right to vote to shareholders who are entitled to vote generally.

SOUTH CAROLINA REPORTERS’ COMMENTS

1. This section sets forth the voting requirements for approval of mergers, share exchanges, and sale of asset transactions out of the ordinary course of business that involve statutory close corporations. The voting requirements are more stringent than those for corporations that are not statutory close corporations. The major difference is that all shareholders, and not merely those who are otherwise entitled to vote on the issue in question, must approve the proposed transaction, and, if they do not vote in favor of the transaction, are entitled to dissenters’ rights. Only a two‑thirds vote by those shareholders who are eligible to vote is necessary for corporations that are not statutory close corporations and only shareholders who are entitled to vote have dissenters’ rights. See Sections 33‑11‑103, 33‑12‑102, and 33‑13‑102. In this connection, note that under Section 33‑7‑250, the merger or sale of assets motion passes if two‑thirds of the votes cast vote in favor of the motion.

2. The only change made in the Model Act Official Text is to substitute for the phrase “the surviving” the phrase “each constituent” in item (2) of subsection (a). This change will make clearer the intent of the section to require approval of statutory close corporation status by the shareholders of all the corporations involved in a merger or share exchange where the surviving corporation is to be a statutory close corporation.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 30.

CROSS REFERENCES

Merger or share exchange, see Sections 33‑11‑101 et seq.

Sale of assets, see Sections 33‑12‑101 et seq.

Voting by voting groups: generally, see Sections 33‑7‑250 and 33‑7‑260.

Voting by voting groups: merger or share exchange, see Section 33‑11‑103.

“Voting group” defined, see Section 33‑1‑400.

Library References

Corporations 182.4(3), 583.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 340, 344, 798.

**SECTION 33‑18‑310.** Termination of statutory close corporation status.

 (a) A statutory close corporation may terminate its statutory close corporation status by amending its articles of incorporation to delete the statement that it is a statutory close corporation. If the statutory close corporation has elected to operate without a board of directors under Section 33‑18‑210, the amendment must comply either with Section 33‑8‑101 or delete the statement dispensing with the board of directors from its articles of incorporation.

 (b) An amendment terminating statutory close corporation status must be approved by the holders of at least two‑thirds of the votes of each class or series of shares of the corporation, voting as separate voting groups, whether or not the holders are entitled otherwise to vote on amendments.

 (c) If an amendment to terminate statutory close corporation status is adopted, each shareholder who did not vote in favor of the amendment is entitled to assert dissenters’ rights under Chapter 13 of this title.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

Sections 31 and 32 (Sections 33‑18‑310 and 33‑18‑320) deal with issues that arise when it is decided to terminate a corporation’s status as a statutory close corporation.

Termination is accomplished by amendment of the articles of incorporation to eliminate the special designation required by section 3 (Section 33‑18‑103). This amendment must be approved by the same vote (two‑thirds) that is necessary to elect close corporation status (unless the articles specify a higher vote); and shareholders who vote against the termination have dissenters’ rights. This is consistent with the provisions in section 3(b) (Section 33‑18‑103(b)) for election by an existing corporation to become a statutory close corporation.

If the status of a statutory close corporation that is operating without a board of directors is to be terminated, in addition to amending the articles of incorporation to delete the reference to the statutory close corporation election, the statement that it has no board of directors must also be deleted, and the corporation must immediately elect a board of directors. Or, if MBCA section 8.01(c) (Section 33‑8‑101(c)) is applicable, the corporation must amend its articles of incorporation to describe who will perform some or all of the duties of the board of directors under that section.

In the absence of agreement upon rights and duties of the shareholders, the corporation upon termination automatically becomes subject to the state’s general business corporation statute, or professional corporation act if the corporation was organized as a professional corporation. Further, except for transfer restrictions under section 11 (Section 33‑18‑110) and authority to operate without a board of directors under MBCA section 8.01(c) (Section 33‑8‑101(c)), any existing rights of the shareholders established by agreement (cf. UNIFORM COMMERCIAL CODE Section 1‑201(3)) between the shareholders or with the corporation and any rights granted to the shareholders in the articles of incorporation that are valid under the general business or professional corporation acts remain in effect.

If the shareholders desire to have transfer restrictions applicable under section 11 (Section 33‑18‑110) to continue after termination of statutory close corporation status, the restrictions must meet all requirements specified in MBCA section 6.27 (Section 33‑6‑270), or analogous section of the state’s general corporation statute. An alternative method of continuing the section 11 transfer restrictions after termination is to include a provision in the articles of incorporation that section 10(b)(7) (Section 33‑18‑110(b)(7)) (which exempts transfers made after termination of statutory close corporation status from the statutory transfer restrictions) does not apply. This eliminates the need to draft a complete set of transfer restrictions. To be binding on third parties, however, all new shares issued after the termination is effective must contain a notice meeting the requirements of MBCA section 6.27(b) (Section 33‑6‑270(b)) (or analogous provisions in state corporation statutes) and other applicable law. See UNIFORM COMMERCIAL CODE Section 8‑204. The notice required as to shares of statutory close corporations by section 10 (Section 33‑18‑109) is no longer appropriate, although it may be effective notice with respect to all shares outstanding at the time of termination.

If the Revised Model Business Corporation Act and the Model Professional Corporation Supplement have been enacted, most of the special control and distribution arrangements among the shareholders and the optional provisions that may be included in the articles of incorporation are not affected by the termination. For example, if sections 14 through 17 (Sections 33‑18‑140 through 33‑18‑170) have been elected, the buy‑out purchase option at the death of a shareholder continues to apply, unless the articles of incorporation are amended to terminate the option. See the Official Comment to section 14 (Section 33‑18‑140). Some provisions, however, may be of doubtful validity after termination. One that may be in this category is a provision in the articles of incorporation giving one or more minority shareholders the right to dissolve the corporation as authorized by section 33 (Section 33‑18‑330). At the time of termination, all relevant documents relating to the corporation and the shareholders should be carefully reviewed, and where necessary revised. This Supplement gives some automatic protection by providing in section 32(b) (Section 33‑18‑320(b)) that the special control and contractual arrangements automatically continue in effect unless they are invalid under other applicable statutes or case law.

SOUTH CAROLINA REPORTERS’ COMMENTS

This section and the next section deal with issues that arise when a corporation ceases to be a statutory close corporation. The Official Comment adequately explains the effect and intent of these provisions.

The only substantive change in the Model Act Official Text in these two sections is to amend Section 33‑18‑310(c) so that any shareholder who does not vote in favor of termination is entitled to dissenters’ rights. The Model Act text requires a shareholder to vote against the termination. This change has been made in other sections of the Statutory Close Corporation Supplement where dissenters’ rights are granted. See Sections 33‑18‑103 and 33‑18‑140(d).

Note that, pursuant to Section 33‑7‑250, the motion to terminate passes if two‑thirds of the votes cast vote in favor of the motion.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 31.

CROSS REFERENCES

Amendment of articles of incorporation, see Sections 33‑10‑101 et seq.

Bylaws for statutory close corporation, see Section 33‑18‑220.

Dissenters’ rights, see Sections 33‑13‑101 et seq.

Effect of termination, see Section 33‑18‑320.

Effective date of amendment of articles of incorporation, see Section 33‑1‑230.

Election not to have board of directors, see Section 33‑8‑101.

Filing fees, see Section 33‑1‑220.

Filing requirements, see Section 33‑1‑200.

Share transfer restrictions: generally, see Section 33‑6‑270.

Share transfer restrictions: statutory close corporations, see Section 33‑18‑110.

Voting by voting groups: amendment of articles of incorporation, see Section 33‑10‑104.

Voting by voting groups: generally, see Sections 33‑7‑250 and 33‑7‑260.

“Voting group” defined, see Section 33‑1‑400.

Library References

Corporations 40.

Westlaw Topic No. 101.

C.J.S. Corporations Section 38.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:335 , Directors’ Resolution‑Amendment of Articles of Incorporation‑Termination of Close Corporation Status.

**SECTION 33‑18‑320.** Effect of termination of statutory close corporation status.

 (a) A corporation that terminates its status as a statutory close corporation is subject thereafter to all provisions of Chapters 1 through 17 of this title or, if incorporated under the South Carolina Professional Corporation Supplement (Chapter 19 of this title), to all provisions of that Supplement.

 (b) Termination of statutory close corporation status does not affect any right of a shareholder or of the corporation under an agreement or the articles of incorporation unless this chapter, Chapters 1 through 17 of this title, or another law of this State invalidates the right.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

See the Official Comment to section 31 (Section 33‑18‑310).

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to Section 33‑18‑310. No change in the Model Act Official Text has been made in this section.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 32.

CROSS REFERENCES

Dissolution at option of shareholder, see Section 33‑18‑330.

Termination of statutory close corporation status, see Section 33‑18‑310.

Library References

Corporations 3.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 5, 62.

**SECTION 33‑18‑330.** Shareholder option to dissolve corporation.

 (a) The articles of incorporation of a statutory close corporation may authorize one or more shareholders, or the holders of a specified number or percentage of shares of any class or series, to dissolve the corporation at will or upon the occurrence of a specified event or contingency. Any shareholder exercising this authority must give written notice of the intent to dissolve to all the other shareholders. Thirty‑one days after the effective date of the notice, the corporation shall begin to wind up and liquidate its business and affairs and file articles of dissolution under Sections 33‑14‑103 through 33‑14‑107.

 (b) Unless the articles of incorporation provide otherwise, an amendment to the articles of incorporation to add, change, or delete the authority to dissolve described in subsection (a) must be approved by the holders of all the outstanding shares, whether or not otherwise entitled to vote on amendments, or, if no shares have been issued, by all the subscribers for shares, if any, or, if none, by all the incorporators.

HISTORY: Derived from 1976 Code Section 33‑21‑130 [1962 Code Section 12‑22.13; 1962 (52) 1996; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The purpose of this section is to give shareholders in a statutory close corporation, if they so elect, basically the same power to dissolve the business as general partners have under the Uniform Partnership Act. The section applies only if it is elected in the corporation’s original or amended articles of incorporation. The right may be given to a single shareholder or to any group of shareholders and may be exercisable at will or restricted to certain designated circumstances. Rights under this section are in addition to other rights a shareholder may have under the state’s general business corporation or professional corporation acts or this Supplement to dissolve the corporation.

This section gives considerable leverage to the shareholder or group of shareholders having the power to dissolve over the other shareholders. It should therefore be utilized with caution. Investors may wish to alter the statutory language to provide that the remaining shareholders have an option to purchase the shares of the shareholder(s) giving notice of dissolution under this section.

This section is generally patterned after the Delaware statute.

SOUTH CAROLINA REPORTERS’ COMMENTS

1. The 1981 South Carolina Business Corporation Act contained a similar provision. See Section 33‑21‑130 of the 1976 Code. Section 33‑21‑130, however, theoretically applied to all corporations, not just those that are classified as close corporations. It also required the text or “a clear reference to the existence and purport of such provision” to be on the back of all share certificates. The stock legend required by Section 33‑18‑109 is all that is required by this Supplement.

2. No substantive changes in the Model Act Official Text have been made in this section.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 33.

CROSS REFERENCES

Articles of incorporation: amendment, see Sections 33‑10‑101 et seq.

Articles of incorporation: generally, see Section 33‑2‑102.

Delivery includes mail, see Section 33‑1‑400.

Dissolution: generally, see Sections 33‑14‑101 et seq.

Dissolution: incorporators, see Section 33‑14‑101.

Dissolution: involuntary dissolution, see Sections 33‑18‑400 et seq.

Effective date of notice, see Section 33‑1‑410.

“Notice” defined, see Section 33‑1‑410.

Procedure following notice of dissolution, see Sections 33‑14‑103 through 33‑14‑107.

Shareholder agreements, generally, see Section 33‑18‑200.

Subscription for shares, see Section 33‑6‑200.

Library References

Corporations 614.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 835, 844.

RESEARCH REFERENCES

Forms

South Carolina Legal and Business Forms Section 1:57 , Formation‑Statutory Close Corporation.

ARTICLE 5

Judicial Supervision

**SECTION 33‑18‑400.** Court action to protect shareholders.

 (a) Subject to satisfying the conditions of subsections (c) and (d), a shareholder of a statutory close corporation may petition the circuit court for any of the relief described in Section 33‑18‑410, 33‑18‑420, or 33‑18‑430 if:

 (1) the directors or those in control of the corporation have acted, are acting, or will act in a manner that is illegal, oppressive, fraudulent, or unfairly prejudicial to the petitioner, whether in his capacity as shareholder, director, or officer of the corporation;

 (2) the directors or those in control of the corporation are deadlocked in the management of the corporation’s affairs, the shareholders are unable to break the deadlock, and the corporation is suffering or will suffer irreparable injury or the business and affairs of the corporation can no longer be conducted to the advantage of the shareholders generally because of the deadlock; or

 (3) there exist grounds for judicial dissolution of the corporation under Section 33‑14‑300.

 (b) A shareholder must commence a proceeding under subsection (a) in the circuit court of the county where the corporation’s principal office or, if none in this State, its registered office is located. The jurisdiction of the court in which the proceeding is commenced is plenary and exclusive.

 (c) If a shareholder has agreed in writing to pursue a nonjudicial remedy to resolve disputed matters, he may not commence a proceeding under this section with respect to the matters until he has exhausted the nonjudicial remedy.

 (d) If a shareholder has dissenters’ rights under this chapter or chapter 13 with respect to proposed corporate action, he must commence a proceeding under this section before he is required to give notice of his intent to demand payment under Section 33‑13‑210 or to demand payment under Section 33‑13‑230 or the proceeding is barred.

 (e) Except as provided in subsections (c) and (d), a shareholder’s right to commence a proceeding under this section and the remedies available under Sections 33‑18‑410 through 33‑18‑430 are in addition to any other right or remedy he may have.

HISTORY: Derived from 1976 Code Section 33‑21‑150 [1962 Code Section 12‑22.15; 1952 Code Section 12‑651; 1942 Code Section 7725; 1932 Code Section 7725; 1922 (32) 1026; 1962 (52) 1996, 1963 (53) 327; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)], and Section 33‑21‑155 [1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

1. Introduction.

Sections 40 through 43 (Sections 33‑18‑400 through 33‑18‑430) are derived from similar provisions in the California, Michigan, Minnesota, New Jersey, and South Carolina statutes, which in turn are derived from former section 210 of the 1948 English Companies Act (reenacted as section 75 of the 1980 English Companies Act). There are two major differences between these statutes and sections 40 through 43 (Sections 33‑18‑400 through 33‑18‑430); (1) the statutes, either specifically or by implication, provide that a shareholder may obtain relief only if he has statutory grounds therefor, whereas section 43 (Section 33‑18‑430) does not tie relief either to a suit to compel dissolution or to the establishment of grounds for dissolution; and (2) the range of relief available to the court is spelled out in greater detail.

The primary danger in granting relief for oppression and related conduct by dissolution is that the remedy is drastic and courts have usually refused to order dissolution of a solvent corporation, except in extreme cases of fraudulent conduct. Moreover, even though authority may exist to grant relief other than dissolution, courts have often been reluctant to grant any relief unless the fact situation itself justifies dissolution. This approach makes the grounds for relief too narrow to protect in an adequate fashion the rights of minority shareholders. At the same time the threat of dissolution gives minority shareholders a powerful weapon to hold over the head of the majority. Under this Supplement, dissolution is one form of relief that may be ordered by the court, but it is appropriate only as a last resort after other possibilities of resolving the dispute have failed. If a shareholder is actually seeking liquidation of the corporation, he may bring an action for dissolution under the state’s general business corporation act (assuming he qualifies to bring the proceeding) or under the option‑to‑dissolve provisions of section 33 (Section 33‑18‑330).

Although sections 40 through 43 (Sections 33‑18‑400 through 33‑18‑430) probably will be invoked most frequently by minority shareholders, the ground for relief described in section 40(a)(2) (Section 33‑18‑400(a)(2)) may be used by the holders of the majority of shares to seek relief from deadlocks created by veto rights given minority shareholders which threaten the corporation’s continued existence. Moreover, even in suits brought by minority shareholders, the court has power under section 42 (Section 33‑18‑420) to order the petitioning shareholders to sell their shares to the corporation or to the remaining shareholders, even if this is not the relief requested.

Relief available under sections 40 through 43 (Sections 33‑18‑400 through 33‑18‑430) is circumscribed to minimize the danger of abuse by shareholders. No relief of any kind may be ordered unless the court affirmatively finds that one or more of the specific conditions listed in section 40(a) (Section 33‑18‑400(a))—fraud, oppression, unfairly prejudicial conduct, deadlock, or grounds for involuntary dissolution—exist. The petitioner has the burden of proof on this issue. The court may award expenses and counsel fees to either side under section 41(b) (Section 33‑18‑410(b)) in order to discourage or punish the bringing of harassment suits. Finally, if the complaining shareholder has agreed to arbitrate the dispute in question or to resolve it in some other nonjudicial manner, these remedies must be exhausted under section 40(c) (Section 33‑18‑400(c)) before a suit under this section may be filed.

2. Grounds for Relief.

Only shareholders of record or beneficial owners of shares held by a voting trust may bring an action under section 40(a) (Section 33‑18‑400(a)) (see the definition of “shareholder” in MCBA section 1.40 (Section 33‑1‑400)). This parallels the limitations imposed on shareholder derivative proceedings by section 7.40 (Section 33‑7‑400) of the MCBA. Relief may be granted if any of the three categories of circumstances specified exist.

Section 40(a)(1) (Section 33‑18‑400(a)(1)) provides relief from oppression and related conduct that adversely affects a minority shareholder in any relationship with the corporation. Attempted squeeze‑outs in close corporations often involve removing a shareholder from his various offices or diminishing his compensation. The subsection makes clear that relief is not limited to those situations in which the value of the shareholder’s share interest has been adversely affected.

No attempt has been made to define oppression, fraud, or unfairly prejudicial conduct. These are elastic terms whose meaning varies with the circumstances presented in a particular case, and it is felt that existing case law provides sufficient guidelines for courts and litigants. See, e.g., Annot., “What amounts to ‘oppressive conduct’ under statute authorizing dissolution of corporation at suit of minority stockholders,” 56 A.L.R.3d 358 (1974).

Section 40(a)(2) (Section 33‑18‑400(a)(2)) allows relief when the corporation is deadlocked. Whether a deadlock is created by majority or minority shareholders is immaterial and either majority or minority shareholders may claim relief under this subsection. Relief may be granted even though the corporation’s financial condition is not threatened with irreparable injury if the court finds that the interest of all the shareholders is being damaged by the deadlock.

Section 40(a)(3) (Section 33‑18‑400(a)(3)) permits a shareholder to claim relief under this section if grounds for involuntary dissolution exist (see MBCA section 14.30 (Section 33‑14‑300)). By filing an action under this section, a greater range of relief is made available to the shareholder. For example, the petitioning shareholder may not wish the corporation dissolved, even though grounds for dissolution exist.

3. Prerequisites to Granting Relief.

Under section 40(c) (Section 33‑18‑400(c)), non‑judicial remedies that the petitioning shareholder has agreed to seek must be exhausted before a suit may be brought under this section. Arbitration clauses covering a wide variety of intracorporate disputes are commonly included in shareholder agreements. If a dispute is covered by an arbitration agreement, the shareholder must submit the claim to arbitration before filing suit under this section and the right to file under this section after the arbitration proceeding is commenced depends on the preclusive effect of the arbitration under state law independent of the corporation statutes.

The requirement in section 40(d) (Section 33‑18‑400(d)) that a shareholder who has dissenters’ rights with respect to a transaction must file suit challenging the transaction under this section before the time he is required to perfect his dissenters’ rights is designed to prevent a shareholder who has foregone his dissenters’ rights from filing suit under this section to prevent a proposed transaction from being consummated. If the complaining shareholder has not taken timely action to perfect his dissenters’ rights, he is relegated to whatever other rights might be available to him under state or federal law. See, e.g., Official Comment 2 to MBCA section 13.02 (Section 33‑13‑102). If the shareholder does file a timely proceeding under this section, the court must first determine whether relief under this section is warranted. If the court finds that a share purchase is the appropriate remedy, the proceeding should be treated as a valuation proceeding in a dissenters’ rights case and consolidated with any other similar dissenters’ rights proceedings involving the same transaction.

Section 40(e) (Section 33‑18‑400(e)) makes clear that the remedies available under this and sections 41 through 43 (Sections 33‑18‑410 through 33‑18‑430) are cumulative and are in addition to any other remedies the petitioner may have, except as otherwise provided in sections 40(c) and 40(d) (Sections 33‑18‑400(c) and 33‑18‑400(d)).

SOUTH CAROLINA REPORTERS’ COMMENTS

1. South Carolina was the first state in this country to adopt comprehensive close corporation remedies provisions patterned upon the English Companies Act. See Sections 12‑22.15 and 12‑15.23 of the 1962 Code, enacted as part of the 1962 South Carolina Business Corporation Act. These provisions were carried forward without substantive change in the 1981 South Carolina Business Corporation Act. See Sections 33‑21‑150 and 33‑21‑155 of the 1976 Code.

Sections 33‑18‑400 through 33‑18‑430 of this act basically follow the existing South Carolina remedies provisions which have been incorporated into Section 33‑14‑300 of this act. There are, however, several important differences:

1. A suit filed under Section 33‑21‑150 of the 1981 South Carolina Business Corporation Act and the analogous provision in this act (Section 33‑14‑300) must be cast as an involuntary dissolution action. A shareholder suit under this section, however, does not have to allege grounds for involuntary dissolution. It is a direct action against the corporation in which the directors and remaining shareholders may be joined; a request for involuntary dissolution may or may not be included in the complaint. While this difference is technical, it has the effect of broadening the jurisdictional grounds for ordering relief and enhances the possibilities that a judge will grant some substantive relief for improper conduct by the defendants even though facts that would justify involuntary dissolution have not been proven.

2. Sections 33‑18‑410 through 33‑18‑430 more clearly indicate that dissolution is the last resort remedy to be used only if no other remedy can resolve the conflict, that a court ordered buy‑out is the next most radical remedy, and that one of the “ordinary” remedies specified in Section 33‑18‑410 should be considered carefully before one of the “extraordinary” remedies in Section 33‑18‑420 (buy‑out) or Section 33‑18‑430 (dissolution) are ordered. This tiering of remedies is consistent with existing case law under Sections 33‑21‑150 and 33‑21‑155 of the 1981 South Carolina Business Corporation Act. See Segall v. Shore, 264 S.C. 442, 215 S.E.2d 895 (1975); id., 269 S.C. 31, 236 S.E.2d 316 (1977) (buy‑out, accounting, plus attorneys’ fees of two hundred thousand dollars ordered); McLeod v. Stevens, 617 F.2d 1038 (4th Cir. 1980) (dissolution); Ward v. Ward Farms, Inc., 283 S.C. 568, 324 S.E.2d 63 (1984) (dissolution). See also, Towles v. South Carolina Produce Association, 187 S.C. 290, 197 S.E. 305 (1938) (no involuntary dissolution for failure to pay dividends when failure to declare dividends was based on capital needs of the corporation); Kugh v. Coronaca Milling Co., 66 S.C. 100, 44 S.E. 566 (1903) (common law cause of action for involuntary dissolution based on fraudulent and ultra vires acts recognized). Cf. Piedmont Press Ass’n. v. Record Publishing Co., 156 S.C. 43, 152 S.E. 721 (1930) (dismissal as a director declared invalid; conflict of interest lease agreement held void).

3. Section 33‑18‑410 contains a more complete list of alternative remedies than does Section 33‑21‑155 of the 1981 South Carolina Business Corporation Act or Section 33‑14‑300 of this act. The authorization of damages in Section 33‑18‑410(a)(9) is particularly important because in McLeod v. Stevens, 617 F.2d 1038 (4th Cir. 1980), the court held that damages cannot be recovered in an equitable action such as an involuntary dissolution suit without specific statutory authorization.

4. The mechanics of a court ordered buy‑out and guidelines for issues that the judge’s order should take into account are contained in Section 33‑18‑420. Section 33‑15‑155(a)(4) of the 1981 South Carolina Business Corporation Act mentioned the possibility of a court ordered buy‑out but did not specify any details about the buy‑out order other than the fact that the shares to be purchased should be valued at their “fair value.”

5. Venue for a suit brought under Section 33‑18‑400 is in the circuit court of the county where the corporation’s principal office is located or, if it has none, in the circuit court of the county where the corporation has its registered office. See Section 33‑18‑400(b). Section 33‑21‑150 of the 1981 South Carolina Business Corporation Act did not specify the venue for such suits.

6. Section 33‑18‑400(c) specifically states that if the shareholders have agreed to arbitrate a particular type of dispute, a suit based on the dispute subject to the arbitration agreement under Section 33‑18‑400 cannot be brought until after the arbitration proceeding is concluded.

7. Section 33‑18‑400(d) provides specific guidelines for the situation where a shareholder with dissenters’ rights wants to challenge proposed corporate action in a suit brought under Section 33‑18‑400. In the absence of statutory guidelines, the relationship between dissenters’ rights and other remedies is unclear. See Vorenberg, Exclusiveness of the Dissenting Shareholder’s Appraisal Rights; 77 Harv. L. Rev. 1189 (1964).

8. Sections 33‑18‑400 through 33‑18‑430 only apply to statutory close corporations formed under this Supplement. Sections 33‑21‑150 and 33‑21‑155 of the 1981 South Carolina Business Corporation Act apply to all corporations. Although rare, involuntary dissolution suits against publicly‑held corporations have been brought. See Bottschall v. Jones and Laughtin Steel Corp., 482 A.2d 1979 (Pa. Super. 1984). The jurisdictional grounds under which such suits can be brought and the remedies that a court can order differ depending on whether a corporation is publicly held or closely held. A more “liberal” statute for close corporations to provide remedies for improper squeeze‑outs and other wrongful conduct makes sense from a policy standpoint.

2. Causes of action for breach of fiduciary duty, securities law violations and the like can be combined with a suit for relief under Sections 33‑18‑400 through 33‑18‑430. See Rules 8, 18, S.C.R.Civ. P. (1985); Harper v. Ethridge,—S.C.—, 348 S.E.2d 374, (Ct. App. 1986). A suit filed under Section 33‑18‑400 is cumulative and not exclusive. See Section 33‑18‑400(e). See also, McGaha v. Mosley, 283 S.C. 268, 322 S.E.2d 461 (Ct. App. 1984) (securities law violations); Talbott v. James, 259 S.C. 73, 190 S.E.2d 759 (1972); Jacobson v. Yaschik, 249 S.C. 577, 155 S.E.2d 601 (1967) (breach of fiduciary duty); Black v. Simpson, 94 S.C. 312, 77 S.E. 1023 (1913); Andrews v. Sumter Commercial & Real Estate Co., 87 S.C. 301, 69 S.E. 604 (1910).

3. No substantive changes in the Model Act Official Text of this section have been made.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 40.

CROSS REFERENCES

Dissenters’ rights, see Sections 33‑13‑101 et seq.

Judicial dissolution: generally, see Section 33‑14‑300.

Judicial dissolution: statutory close corporations, see Section 33‑18‑430.

Principal office: defined, see Section 33‑1‑400.

“Proceeding” defined, see Section 33‑1‑400.

Registered office: required, see Section 33‑5‑101.

Relief, see Sections 33‑18‑410 through 33‑18‑430.

Shareholder agreements, see Section 33‑18‑200.

Library References

Corporations 320.

Westlaw Topic No. 101.

NOTES OF DECISIONS

In general 1

1. In general

A trial judge properly dissolved a family corporation, under former Section 33‑21‑150, where ample evidence supported the conclusion that the corporation was deadlocked, that continuous disagreements and animosity existed between the shareholders, that the corporation had never declared a dividend, and that several lawsuits had been instituted among the shareholders concerning the corporation. Ward v. Ward Farms, Inc. (S.C. 1984) 283 S.C. 568, 324 S.E.2d 63.

Stock of plaintiffs ordered redeemed where defendants (executors and officers in corporation controlled by testator) appropriated more than $1 million proceeds for own purposes, sought to avoid accounting, continued withdrawals after Supreme Court had issued opinion establishing duty to restore profits and accounts and, in apparent act of contempt, took additional sum of $175,000 for payment of income taxes after having been enjoined from further withdrawals. Segall v. Shore (S.C. 1977) 269 S.C. 31, 236 S.E.2d 316.

While the predecessor to this section was undoubtedly intended to afford minority stockholders a method of relief against mismanagement of a corporation by majority stockholders, or the suspension of dividends for the purpose of freezing out minority stockholders, or depressing the market value of the stock of the corporation, it was never intended that the mere fact that a corporation would not pay a dividend for three years, time to be computed from three years after it has begun business, would ipso facto entitle minority stockholders to have such corporation dissolved and a receiver appointed therefor. Towles v. South Carolina Produce Ass’n (S.C. 1938) 187 S.C. 290, 197 S.E. 305. Corporations And Business Organizations 3051

**SECTION 33‑18‑410.** Ordinary relief.

 (a) If the court finds that any grounds for relief described in Section 33‑18‑400(a) exist, it may order one or more of the following types of relief:

 (1) the performance, prohibition, alteration, or setting aside of any action of the corporation or of its shareholders, directors, or officers of or any other party to the proceeding;

 (2) the cancelation or alteration of any provision in the corporation’s articles of incorporation or bylaws;

 (3) the removal from office of any director or officer;

 (4) the appointment of any individual as a director or officer;

 (5) an accounting with respect to any matter in dispute;

 (6) the appointment of a custodian to manage the business and affairs of the corporation;

 (7) the appointment of a provisional director who has all the rights, powers, and duties of an elected director to serve for the term and under the conditions prescribed by the court;

 (8) the payment of dividends;

 (9) the award of damages to any aggrieved party.

 (b) If the court finds that a party to the proceeding acted arbitrarily, vexatiously, or otherwise not in good faith, it may award other parties their reasonable expenses, including counsel fees and the expenses of appraisers or other experts, incurred in the proceeding.

HISTORY: Derived from 1976 Code Section 33‑21‑150 [1962 Code Section 12‑22.15; 1952 Code Section 12‑651; 1942 Code Section 7725; 1932 Code Section 7725; 1922 (32) 1026; 1962 (52) 1966, 1963 (53) 327; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)], and Section 33‑21‑155, [1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

The purpose of listing the types of relief available, in this section and in sections 42 and 43 (Sections 33‑18‑420 and 33‑18‑430), is to overcome the reluctance some courts have shown in the past to ordering anything other than dissolution, or possibly a buy‑out. See, e.g., Gruenberg v. Goldmine Plantation, Inc., 360 So.2d 884 (La. Ct. App. 1978); Harkey v. Habley, 552 S.W.2d 79 (Mo. Ct. App.1977); White v. Perkins, 213 Va. 129, 189 S.E.2d 315 (1972). A court should have broad discretion to fashion the most appropriate remedy to resolve the dispute. What works in one case may not work in another. Detailed standards are not provided since they might encourage litigation and also unduly restrict the court’s discretion. The dangers of including detailed standards, however, outweigh the advantages. Existing cases applying principles of equity, are, of course, precedents for the exercise of a judge’s discretion under this section.

Although most close corporation statutes contain special provisions similar to sections 40(a)(6) and (7) (Section 33‑18‑400(a)(6) and (7)), authorizing the appointment of custodians and provisional directors, the number of actual cases in which appointments will be the most appropriate remedy are probably few. Usually the threat of an outsider running the company or acting as a tie‑breaker in a deadlock situation leads to a settlement of the controversy.

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to Section 33‑18‑400.

No substantive change in the Model Act Official Text has been made.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 41.

CROSS REFERENCES

Court action to protect shareholders, see Section 33‑18‑400.

Custodianship, see Section 33‑14‑320.

Directors generally, see Sections 33‑8‑101 through 33‑8‑330.

Dissolution of statutory close corporation, see Section 33‑18‑430.

Dividends, see Section 33‑6‑400.

Officers generally, see Sections 33‑8‑400 through 33‑8‑440.

Library References

Corporations 320(12), 320(13).

Westlaw Topic No. 101.

NOTES OF DECISIONS

In general 1

1. In general

Statute gives court power to direct or prohibit any act of corporation or shareholders, directors, officers, or other parties to action, and therefore authorizes court to require shareholder in deadlocked corporation to co‑operate during transition process and enjoin that individual from taking any action calculated to cause company to loose existing contracts, or any action which might be detrimental to continued viability of company. Hendley v. Lee, 1987, 676 F.Supp. 1317.

Close corporations are subject to the sections of the Business Corporation Act governing court actions to protect shareholders, ordinary relief in such actions, and extraordinary relief in such actions in the form of a court‑ordered share purchase or dissolution. Mason v. Mason (S.C.App. 2015) 412 S.C. 28, 770 S.E.2d 405, rehearing denied, certiorari dismissed. Corporations and Business Organizations 1501; Corporations and Business Organizations 3058(1)

Special referee’s ruling, in minority shareholder’s action against family member owners of auto‑service company, and against company, seeking repurchase of his shares under judicial dissolution provision of Business Corporation Act, that action was improper in that it was not filed as a derivative action, became law of the case under the two‑issue rule, where shareholder did not address such ruling on appeal. Mason v. Mason (S.C.App. 2015) 412 S.C. 28, 770 S.E.2d 405, rehearing denied, certiorari dismissed. Appeal and Error 853

**SECTION 33‑18‑420.** Extraordinary relief: share purchase.

 (a) If the court finds that the ordinary relief described in Section 33‑18‑410(a) is or would be inadequate or inappropriate, it may order the corporation dissolved under Section 33‑18‑430 unless the corporation or one or more of its shareholders purchase all the shares of the shareholder for their fair value and on terms determined under subsection (b).

 (b) If the court orders a share purchase, it shall:

 (1) determine the fair value of the shares, considering among other relevant evidence the going concern value of the corporation, any agreement among some or all of the shareholders fixing the price or specifying a formula for determining share value for any purpose, the recommendations of any appraisers appointed by the court, and any legal constraints on the corporation’s ability to purchase the shares;

 (2) specify the terms of the purchase, including, if appropriate, terms for installment payments, subordination of the purchase obligation to the rights of the corporation’s other creditors, security for a deferred purchase price, and a covenant not to compete or other restriction on the seller;

 (3) require the seller to deliver all his shares to the purchaser upon receipt of the purchase price or the first installment of the purchase price;

 (4) provide that after the seller delivers his shares he has no further claim against the corporation, its directors, officers, or shareholders, other than a claim to any unpaid balance of the purchase price and a claim under any agreement with the corporation or the remaining shareholders that is not terminated by the court;

 (5) provide that, if the purchase is not completed in accordance with the specified terms, the corporation is to be dissolved under Section 33‑18‑430; and

 (6) provide that the corporation or remaining shareholders release or enter into an agreement to indemnify the seller from any personal liability for obligations of the corporation the seller has personally guaranteed.

 (c) After the purchase order is entered, any party may petition the court to modify the terms of the purchase and the court may do so if it finds that changes in the financial or legal ability of the corporation or other purchaser to complete the purchase justify a modification.

 (d) If the corporation is dissolved because the share purchase was not completed in accordance with the court’s order, the selling shareholder has the same rights and priorities in the corporation’s assets as if the sale had not been ordered.

HISTORY: Derived from 1976 Code Section 33‑21‑150 [1962 Code Section 12‑22.15; 1952 Code Section 12‑651; 1942 Code Section 7725; 1932 Code Section 7725; 1922 (32) 1026; 1962 (52) 1996, 1963 (53) 327; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)], and Section 33‑21‑155, [1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

A court ordered buy‑out is a drastic remedy, particularly if the shareholder ordered to sell his shares does not wish to sell. For this reason section 42 (Section 33‑18‑420) authorizes a share purchase order only if other relief short of liquidation will not, in the judge’s opinion, resolve the dispute. If a buy‑out ordered by the court is not consummated, however, an order dissolving the corporation is authorized. This may place pressure on the remaining shareholders to obey the order but also gives them the option of dissolution if they think the order is too onerous.

If the court orders a buy‑out, it must also determine the fair value and other terms of the buy‑out in accordance with subsection (b). Fair value is to be determined under principles developed in dissenters’ rights and other valuation cases. The court may require the selling shareholder to enter into a covenant not to compete and also may order an installment sale in order to protect the business and to minimize the financial strain on the purchasers. See also the Official Comment to section 14 (Section 33‑18‑140).

This section permits the designated purchasers either to consummate the purchase or to permit the corporation to be dissolved. Presumably the remaining shareholders will elect to have the corporation dissolved if its economic prospects are bleak. Leaving the choice to the remaining shareholders is fairer than ordering dissolution without giving the remaining shareholders the opportunity to buy out the complaining shareholder or requiring the remaining shareholders to purchase the shares without giving them the option of voluntary dissolution (which they would not have unless they held sufficient voting shares to approve a dissolution).

If the remaining shareholders agree to comply with the court ordered buy‑out, the sale operates as a release of all claims the selling shareholder may have against the corporation, or its directors, officers, or shareholders. The selling shareholder may still pursue any contractual claim he might have against the corporation—for example, a claim for breach of a long term employment contract—to the extent the claim is not dealt with in the court’s order. Normally, however, the order should dispose of these contractual claims. The selling shareholder also retains the right to collect any unpaid balance due on the purchase price of his shares, including the right to realize on any collateral given as security for the unpaid balance. Quite frequently the shares being sold have been pledged as security; in these situations, if there is a default, the former shareholder has the choice of foreclosing on the note and again becoming a shareholder or suing to have the corporation dissolved under section 43 (Section 33‑18‑430).

Under section 42(c) (Section 33‑18‑420(c)), the court has power to modify its final order at any time upon the petition of any party. For example, should financial or legal constraints prevent the purchasers from fulfilling the terms of a mandated buy‑out, the court might modify its order. See also the Official Comment to section 14 (Section 33‑18‑140).

Finally, the buy‑out and dissolution remedies provided by this section and section 43 (Section 33‑18‑430) are cumulative of ordinary remedies available under section 41 (Section 33‑18‑410); for example, a court may award damages in addition to compelling a buy‑out. See the Official Comment to section 40 (Section 33‑18‑400).

SOUTH CAROLINA REPORTERS’ COMMENTS

1. See the South Carolina Reporters’ Comments to Section 33‑18‑400.

2. Having the details of a court ordered share purchase spelled out in the statute avoids many problems that have arisen in other states where courts have ordered buy‑outs. See Haynsworth, The Effectiveness of Involuntary Dissolution Suits as a Remedy for Close Corporation Dissension, 35 CLEV. ST. L. REV. (1986). In this connection, the requirement that the court take into consideration the “going concern value of the corporation” is important because a court might otherwise determine the value on a liquidation basis on the grounds that the buy‑out is in lieu of dissolution. See Ronald v. 4‑C’s Electronic Packaging, Inc., 214 Cal. Rptr. 225 (Cal. App. 1985).

3. A specific paragraph protecting a shareholder whose shares are purchased from any personal liability for corporate loans he has guaranteed is recommended and is added to the Model Act Official Text as item (6) of subsection (a). Shareholder guarantees of loans made to close corporations are quite commonly required by banks and other lenders. These guarantees frequently are unlimited in time or amount. It is only fair that a shareholder whose shares are purchased be protected against any potential liability on such guarantees which arises after his shares have been purchased. The South Carolina Uniform Partnership Act provides similar protection to a general partner whose interest has been purchased by the continuing partners. See Section 33‑41‑1040 of the 1976 Code.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 42.

CROSS REFERENCES

Court action to protect shareholders, see Section 33‑18‑400.

Dissenters’ rights, see Sections 33‑13‑101 et seq.

Dissolution, see Section 33‑14‑101 et seq.; Section 33‑18‑430.

Fair value of shares in court action to compel purchase of shares, see Section 33‑18‑160.

Relief cumulative, see Section 33‑18‑410.

Share purchase on death of shareholder, see Section 33‑18‑410.

Library References

Corporations 182.4(5), 592, 606.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 340, 344, 811, 813 to 816, 818, 821, 824, 830 to 831.

NOTES OF DECISIONS

In general 1

1. In general

Imposing key man discount in forced buy out of corporation was not appropriate because neither party was willing buyer or seller and transaction was between insiders; key man discount ignores that buyers are already in business and have dominant presence in industry; any slippage was merely temporary in view of parties proven ability to perform, and any key man discount was offset by control premium considerations, in that by purchasing alleged key man’s interests, buyers would control company in which they previously owned only one half interest. Additionally, under employment contract, buyers of corporation in forced buy out had within their power ability to fire alleged key man after they began operating business. Hendley v. Lee, 1987, 676 F.Supp. 1317.

Proper date for evaluation of assets of corporation in forced buy out case is date of trial. Hendley v. Lee, 1987, 676 F.Supp. 1317. Corporations And Business Organizations 1526(7)

Remedy of forced buy out was proper where court had rejected remedy of either dissolution of corporation or division of accounts and assets and corporation was deadlocked. Hendley v. Lee, 1987, 676 F.Supp. 1317.

Division of corporation by dividing accounts and tangible assets was declined by court because of numerous unresolved and complex issues that would result. Hendley v. Lee, 1987, 676 F.Supp. 1317.

Close corporations are subject to the sections of the Business Corporation Act governing court actions to protect shareholders, ordinary relief in such actions, and extraordinary relief in such actions in the form of a court‑ordered share purchase or dissolution. Mason v. Mason (S.C.App. 2015) 412 S.C. 28, 770 S.E.2d 405, rehearing denied, certiorari dismissed. Corporations and Business Organizations 1501; Corporations and Business Organizations 3058(1)

**SECTION 33‑18‑430.** Extraordinary relief: dissolution.

 (a) The court may dissolve the corporation if it finds:

 (1) there are grounds for judicial dissolution under Section 33‑14‑300; or

 (2) all other relief ordered by the court under Section 33‑18‑410 or 33‑18‑420 has failed to resolve the matters in dispute.

 (b) In determining whether to dissolve the corporation, the court shall consider among other relevant evidence the financial condition of the corporation but may not refuse to dissolve solely because the corporation has accumulated earnings or current operating profits.

HISTORY: Derived from 1976 Code Section 33‑21‑150 [1962 Code Section 12‑22.15; 1952 Code Section 12‑651; 1942 Code Section 7725; 1932 Code Section 7725; 1922 (32) 1026; 1962 (52) 1996, 1963 (53) 327; 1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)], and Section 33‑21‑155 [1981 Act No. 146, Section 2; Repealed, 1988 Act No. 444, Section 4(1)]; 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

See the Official Comments to sections 40 to 42 (Sections 33‑18‑400 to 33‑18‑420).

SOUTH CAROLINA REPORTERS’ COMMENTS

See the South Carolina Reporters’ Comments to Section 33‑18‑400. No substantive change in the Model Act Official Text language has been made.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 43.

CROSS REFERENCES

Court action to protect shareholders, see Section 33‑18‑400.

Dissolution generally, see Sections 33‑14‑101 et seq.

Judicial dissolution, see Section 33‑14‑300.

Relief cumulative, see Section 33‑18‑410.

Library References

Corporations 592, 606.

Westlaw Topic No. 101.

C.J.S. Corporations Sections 811, 813 to 816, 818, 821, 824, 830 to 831.

NOTES OF DECISIONS

In general 1

1. In general

Corporate dissolution statute, Section 33‑21‑150, is jurisdictional, and asking for dissolution is merely prerequisite to obtaining other forms of relief under Section 33‑21‑155. Dissolution of entire corporation would clearly be improper due to continued profitability and growth potential of business and investments of time and money by parties involved in business. Hendley v. Lee, 1987, 676 F.Supp. 1317.

Close corporations are subject to the sections of the Business Corporation Act governing court actions to protect shareholders, ordinary relief in such actions, and extraordinary relief in such actions in the form of a court‑ordered share purchase or dissolution. Mason v. Mason (S.C.App. 2015) 412 S.C. 28, 770 S.E.2d 405, rehearing denied, certiorari dismissed. Corporations and Business Organizations 1501; Corporations and Business Organizations 3058(1)

ARTICLE 6

Transition Provisions

**SECTION 33‑18‑500.** Application to existing corporations.

 This chapter applies to all corporations electing statutory close corporation status under Section 33‑18‑103 after its effective date.

HISTORY: 1988 Act No. 444, Section 2.

OFFICIAL COMMENT

None.

SOUTH CAROLINA REPORTERS’ COMMENTS

1. This section states a very simple self‑evident principle: this chapter only applies to corporations that elect statutory close corporation status after the effective date of this act. This leaves open the status of corporations that have made certain elections under the 1981 South Carolina Business Corporation Act pursuant to statutory provisions that are repealed by this act. Only two provisions appear to present this issue: Section 33‑11‑220, which authorizes a ten‑year shareholder‑management agreement similar to Section 33‑18‑200 of this act, and Section 33‑21‑130, which authorizes a special right of dissolution similar to Section 33‑18‑330 of this act.

Under Section 33‑20‑104 of this act, any rights created under these two statutes would continue to exist even though Sections 33‑11‑220 and 33‑21‑130 of the 1981 South Carolina Business Corporation Act have been repealed. In this connection, the legal implications of a Section 33‑11‑220 agreement entered into before the effective date of this act and the requirements for its effectiveness, amendment, termination, and renewal would be governed by Section 33‑11‑220 and not Section 33‑18‑200 of this act. As the South Carolina Reporters’ Comments to Section 33‑18‑200 point out, there are substantial differences between the two sections. Any existing corporation in which the shareholders have a Section 33‑11‑220 agreement, however, could have the agreement construed under Section 33‑18‑200 of this act by electing to become a statutory close corporation governed by this chapter. See Section 33‑18‑103 of this act.

DERIVATION: 1984 Model Act Statutory Close Corporation Supplement Section 50.