CHAPTER TWELVE

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Section 12.01 Sale of Assets

At common law, a corporation could not sell all of its assets over the objection of even a single shareholder. *Pomierski v. W. R. Grace & Co.*, 282 F Supp 385, 394 (ND Ill 1967); *Geddes v. Anaconda Copper Mining Co.*, 254 US 590 (1921).

This rule was subject to much criticism and courts found reasons to avoid it. *See:* 6A FLETCHER CYC CORP § 2949.10 (Perm Ed 1997). For instance, courts held that a majority of shareholders could authorize the sale of all assets if the corporation proved unprofitable – even though not insolvent. *Geddes v. Anaconda Copper Mining Co.*, 254 US 590 (1921).

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In some states, courts held that the board of directors could sell all corporate assets if necessary to pay corporate debts. *Turpin v. Dunis*, 66 Wash 2d 749, 405 P2d 239 (1965).

The common law rule has been changed by statute. ORS 60.531 governs the sale of all corporate assets in the regular course of business. ORS 60.534 governs sales outside the ordinary course of business.

"In general, under Washington law, a corporation has broad power to encumber or distribute its assets, so long as creditors of the corporation are not prejudiced thereby." *Spokane Concrete Products, Inc. v. U. S. Bank of Washington*, 126 Wash 2d 269, 279, 892 P2d 98, 104 (1995).

If the sale occurs in the regular course of business, a board may authorize the sale of all corporate assets without shareholder approval. ORS 60.531(1).

For instance, if a corporation's stated purpose is to buy and sell or to lease real estate, the corporation's sale or lease of a property which constitutes the corporation's only asset may be "in the usual course of business." If so, this sale or lease does not require shareholder approval. ORS 60.531(1)(a); *Sailer v. Land-Livestock-Recreation, Inc.*, 268 Or 531, 522 P2d 214 (1974); *Western Land Corp. v. Lichtenstein*, 47 Ill App 233, 361 NE2d 730 (1977); *Eisen v. Post*, 3 NY2d 518, 146 NE2d 779, 169 NYS2d 15 (1957); *Van Buren v. Highway Ranch, Inc.*, 46 Wash 2d 582, 283 P2d 132 (1955).

Even if a corporation's "ordinary course of business" does not include obtaining a mortgage, the corporation's board may authorize it to mortgage all of its property without shareholder approval. ORS 60.531(1)(b). This is contrary to earlier law. *Sailer v. Land-Livestock-Recreation, Inc.*, 268 Or 531, 522 P2d 214 (1974).

A board may authorize the corporation to transfer all of its property to a wholly-owned subsidiary without shareholder approval – even if it is not in the usual course of its business. ORS 60.531(c).

Otherwise, the sale of substantially all corporate assets – not in the ordinary course of business – requires shareholder approval. ORS 60.534.

To obtain such approval, the board must act first and only thereafter refer the matter to shareholders for their approval. ORS 60.534(2)(a). The board may condition the proposal on any basis. ORS 60.534(3). For instance, a board may condition the proposed sale on a supermajority vote. ORS 60.534(5)

Next, the corporation give notice to all shareholders of the time,

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date and place of a shareholder meeting at which the vote on the sale is to occur – it must even give notice to shareholders not entitled to vote – and the meeting notice must include the meeting purpose and describe the proposed transaction. ORS 60.534(4). Generally, a majority vote of the shareholders entitled to vote is required to approve the sale, unless the articles or the board of directors require a higher vote. ORS 60.534(5).

Unless a corporation complies with these rules, any such sale of corporate assets is voidable by the corporation. *Naas v. Lucas*, 86 Or App 406, 739 P2d 1051, *opinion adhered to as modified*, 88 Or App 141, 744 P2d 586, *review denied*, 304 Or 680, 748 P2d 142 (1987); *Carson v. Isabel Apartments, Inc.*, 20 Wash App 293, 579 P2d 1027 (1978).

If an asset sale requires shareholder approval, the shareholders have the right to dissent. ORS 60.554(1)(c). A discussion of the right to dissent is contained in Section 8.05 of this book.

Section 12.02 Merger & Share Exchange

A. Procedures.

Merger. One or more business entities may merge into another corporation – provided the merger is permitted by the statutes governing each of the entities to the merger. ORS 60.481(1)(a).

For Oregon entities, this statute permits the merger of two or more Oregon corporations or the merger of an Oregon corporation with one or more of any of the following entities: an Oregon limited liability company (ORS 63.481); an Oregon cooperative (ORS 62.617); an Oregon general partnership organized after January 1, 1998, or is an Oregon limited liability partnership or a partnership which elects to be governed by ORS Chapter 67 (ORS 67.340(1)(D) & 67.360); an Oregon limited partnership (ORS 70.525). An Oregon corporation can also merge with a business entity organized under the laws of another jurisdiction – but only if laws of that jurisdiction permit such mergers. ORS 60.481(1)(a).

While it appears that a business corporation may merge with an Oregon professional corporation (ORS 58.045(2)), there are severe restrictions if the surviving corporation intends to engage in one of the professions. *See, for example:* ORS 58.196.

Generally in a merger, the governing board or managing group of each surviving and nonsurviving entity must adopt a plan of merger.

Share Exchange. In a similar manner, a corporation may acquire all of the outstanding shares of another corporation through a share exchange. ORS 60.484 and 60.487.

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Section 12.02

Shareholder approval. Generally, a merger or a share exchange requires shareholder approval of the plan of merger or plan of share exchange. ORS 60.487(2). In each case, the board of directors of all Oregon corporations involved in the transaction must refer the plan to the shareholders for a vote. *Id.*

Voting by voting group may be required. ORS 60.487(6). Generally, the shareholders of each corporation must approve the plan by majority vote, unless the articles or the board of directors require approval by a greater vote. ORS 60.487(5).

Filing requirement. A plan of merger must be filed with the Secretary of State. With amendments adopted in 2003, the plan of merger to be filed can now include "a summary of the material terms and conditions of the merger" – rather that the detailed terms and conditions themselves. ORS 60.481(2).

Right to dissent. If a merger or share exchange requires shareholder approval, the shareholders have the right to dissent. ORS 60.554(1)(a). The right to dissent is discussed in Section 8.05 of this book.

***B. Exception – merger of subsidiary into parent*.**

If a corporation owns at least 90% of another corporation, the merger of the subsidiary corporation into the parent may be approved by the board of the parent without the approval of shareholders of either the parent or the subsidiary corporation. ORS 60.491(1). Shareholders of the subsidiary corporation – but not shareholders of the parent corporation – have the right to dissent. ORS 60.554(1)(a).

***C. Effect of merger*.**

After a merger, the surviving corporation is responsible for all liabilities of each corporation involved in the merger, surviving and nonsurviving corporations alike. ORS 60.497(1)(c); *Nike, Inc. v. Spencer*, 75 Or App 362, 707 P2d 589 (1985); *Gaswint v. Case*, 265 Or 248, 509 P2d 19 (1973); *Lamb v. Leroy Corp.*, 85 Nev 276, 454 P2d 24 (1969).

The surviving corporation also possesses all rights and privileges possessed by each of the merged corporations. ORS 60.497(1)(b); *All Brand Importers, Inc. v. Department of Liquor Control*, 213 Conn 184, 567 A2d 1156 (1989); *Knightstown Lake Property Owners Assoc., Inc. v. Big Blue River Conservancy District*, 178 Ind App 463, 383 NE2d 361 (1978); *Diamond Parking, Inc. v. Seattle*, 78 Wash 2d 778, 479 P2d 47 (1971).

An exception may exist, however, where a competing state statute requires state approval of the holder of a license. *State ex rel Don Williams*

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Export, Inc. v. Timm, 78 Wash 2d 520, 477 P2d 15 (1970) (transfer of common carrier permit to surviving corporation required state approval). But the same may not be true where a city ordinance requires approval. *Diamond Parking, Inc. v. Seattle*, 78 Wash 2d 778, 479 P2d 47 (1971).

***D. Consolidations*.**

Consolidations are not authorized by the current Act.

In a consolidation, a new corporation comes into being and none of the original corporations survive. This same result may be achieved today by forming a new corporation and then by merging all of the old corporations into the new corporation.

Section 12.03 Dissolution, Generally

At common law, there were several ways in which a corporation could be dissolved. FLETCHER CYC CORP § 7976 (Perm Ed). But today, all states have enacted statutes for the dissolution of corporations.

A corporation may only be dissolved in the manner prescribed by statute.

"The statutes having provided the method for dissolving corporations, that method is exclusive." *Anderson v. Bures*, 110 Or 265, 269, 223 P 244, 245 (1924). *See, also: Reese Sales Co., Inc. v. Gier*, 16 Wash App 664, 557 P2d 1326 (1977).

"Failure to follow the prescribed statutory method renders ineffectual any attempt to dissolve a corporation." *Moore v. Los Lugos Gold Mines*, 172 Wash 570, 589, 21 P2d 253, 260 (1933). Some courts have held that not even a court acting in equity may dissolve a corporation absent a statute giving it such authority. *Richter v. Richter*, 202 Ga 554, 43 SE2d 635 (1947); *Enterprise Printing & Publishing Co. v. Craig*, 195 Ind 302, 144 NE 542, 145 NE 309 (1924).

The Oregon Business Corporation Act provides for only three methods of corporate dissolution: voluntary, administrative, and judicial. Each of these methods is discussed below.

While the great majority of dissolutions are intended to be voluntary dissolutions, they are technically administrative dissolutions; that is, the directors and shareholders make a conscious decision to dissolve, but then fail to go through with the formalities of a voluntary dissolution. Instead, they walk away from the business, neglect to file the next required annual report with the Secretary of State, and the corporation is administratively dissolved. As such, shareholders are not able to take advantage of the protections afforded by the voluntary dissolution

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procedures described in Section 12.04 below.

Shareholders do not normally become liable on corporate liabilities upon dissolution of the corporation. *Hambleton Bros. Lumber Co. v. Balkin Enterprises, Inc.,* 397 F3d 1217 (9th Cir 2005).

Section 12.04 Voluntary Dissolution

A. Procedures.

To voluntarily dissolve, a corporation may use one of three procedures:

(i) If the corporation has not yet issued shares or started doing business, a majority of initial directors or incorporators may dissolve the corporation by delivering articles of dissolution to the Secretary of State for filing. ORS 60.621.

(ii) The board may propose – and shareholders may approve – dissolution. The shareholder notice must state that the purpose of the meeting is to consider dissolution. Shareholders must then approve the proposal to dissolve by a majority vote of all shares, unless voting is by voting group or unless the articles require a greater vote. ORS 60.627.

(iii) All shareholders may consent in writing to the dissolution of the corporation. ORS 60.624.

The current Act is generally consistent with prior case law. The dissolution process must be initiated by the board; shareholders may vote on dissolution only after the board has referred the question to them. *Kelly v. Galloway*, 156 Or 301, 66 P2d 272, 68 P2d 474 (1937); *Powell v. Oregonian Ry. Co.*, 38 F 187 (D Or 1889). This may not apply when shareholders unanimously agree in writing to dissolve. While under prior law this did not constitute a dissolution, individual shareholders were estopped from later complaining. *Anderson v. Burgess*, 110 Or 265, 223 P 244 (1924).

A director/shareholder may not act unilaterally to dissolve and wind up the corporation's affairs – even if the only other director/shareholder has breached his fiduciary duty to the corporation and caused its business to fail. *Horton v. Whitehill*, 121 Or App 336, 241, *review denied*, 318 Or 25, 862 P2d 1305 (1993).

At any time after dissolution is authorized, a corporation may dissolve by delivering articles of dissolution to the Secretary of State. ORS 60.631(1) requires these articles of dissolution to contain:

(a) The name of the corporation;
(b) The date dissolution was authorized;
(c) If dissolution was approved by the shareholders:

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(A) The number of votes entitled to be cast on the proposal to dissolve; and

(B) The total number of votes cast for and against dissolution and a statement that the number cast for dissolution was sufficient for approval; and

(d) If voting by voting groups is required, the information required by paragraph (c) of this subsection separately provided for each voting group entitled to vote separately on the plan to dissolve.

B. Effect of dissolution on conducting business.

"A dissolved corporation continues its corporate existence but may not carry on any business except that appropriate to wind up and liquidate its business and affairs." ORS 60.637(1).

At common law, the dissolution of a corporation was the equivalent of "its civil death; dissolution immediately abated all actions by and against the corporation." *University of Alaska v. Thomas Architectural Products, Inc.*, 907 P2d 448, 450 (Alaska 1995) (interpreting Washington law). *See also: Tillett Brothers Construction Co., Inc. v. Department of Transportation*, 210 Ga App 84, 435 SE2d 241 (1993); *Indiana National Bank v. Churchman*, 564 NE2d 340 (Ind App 1990); *U. S. v. Maryland State Licensed Beverage Ass'n*, 138 F Supp 685, 708 (D Md 1956).

Later statutes usually created a fixed period after dissolution during which a corporation could continue to sue or be sued. *Clatsop County v. Taylor*, 167 Or 563, 119 P2d 285 (1941); *Service Lumber Co. v. Sumpter Valley Ry. Co.*, 81 Or 32, 149 P 531, 152 P 262, 158 P 175 (1916); *Dundee Mortgage & Trust Inv. Co.*, 77 F 855 (D Or 1896); *Pacesetter Real Estate, Inc. v. Fasules*, 53 Wash App 463, 767 P2d 961 (1989).

> Under the common law a corporation's capacity to sue or be sued terminated when the corporation was legally dissolved. Today, however, the harshness of the common law on creditors and shareholders has been replaced in every state by statutes which extend the corporate life for a definite time for the purpose of prosecuting and defending suits. However, where a statute continues the existence of a corporation for a certain period, it is generally held that the corporation becomes defunct upon the expiration of such period, at least in the absence of a provision to the contrary, so that no action can afterwards be brought by or against it and must be dismissed. (citations omitted) *Canadian Ace Brewing v. Joseph Schlitz Brewing Co.*, 629 F2d 1183, 1185 (7th Cir 1980).

Under the current Oregon Act, the right to sue and be sued continues indefinitely. ORS 60.637(2)(e) and (f). The purpose of this provision is "to provide that dissolution will not abate legal claims by and against a corporation, just as death will not abate personal claims by and against an individual." *Savannah Laundry & Machinery Co., Inc. v. Oweenby*, 186 Ga App 130, 366 SE2d 787, 789 (1988).

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C. Creditors have first claim to assets upon dissolution.

It is a well-established doctrine that upon dissolution, the assets of a corporation are to be applied first to the payment of corporate debts and then, if there are assets remaining, to the shareholders. *Smyth v. Kenwood Land Co.*, 97 Or 19, 190 P 962 (1920); *Georgia, Florida & Alabama R. Co. v. Bankers Trust Co.*, 170 F2d 733 (5th Cir 1948); *United States v. Butterworth Corp.*, 269 US 504 (1926).

Under some circumstances, a creditor who is not paid prior to the distribution of assets to shareholders may recover from shareholders. ORS 60.644(4); *Wakeman v. Paulson*, 257 Or 542, 480 P2d 434 (1971); *Lonsdale v. Chesterfield*, 99 Wash 2d 353, 662 P2d 385 (1983); *Fountain v. Burke*, 160 Ga App 262, 287 SE2d 39 (1982). *But, see: Walter A. Wood Reaping and Mowing Manufacturing Co. v. Angemeier*, 51 Ind App 258, 99 NE 500 (1912).

> The law which sends a corporation into the world with the capacity to act imposes upon its assets liability for its acts. The corporation cannot disable itself from responding by distributing its property among its stockholders and leaving remediless those having valid claims. In such a case the claims after being reduced to judgments may be satisfied out of the assets in the hands of the stockholders. *Pierce v. U. S.*, 255 US 398, 402 (1921).

As describe in Sections 10.11 and 10.12 of this book, the general rule is that a creditor of an insolvent corporation may recover debts owed to the corporation by shareholders only through an equitable proceeding naming all creditors and all shareholders located within the jurisdiction. *Wakeman v. Paulson*, 264 Or 524, 506 P2d 683 (1973); *Royer v. Maib*, 6 Wash 2d 286, 107 P2d 593 (1940). This also seems to be the rule in actions to collect improper distributions after dissolution.

> From the principle thus established in this state the proper remedy of a creditor of an insolvent corporation to reach the fund alleged to have been paid to a stockholder as a dividend in liquidation is by a suit in equity and not by an action at law as commenced in the case at bar. *Garetson Lumber Co. v. Hinson*, 69 Or 605, 610, 140 P 633, 635 (1914).

There has been a trend toward permitting a creditor to proceed directly against the shareholders without the obligation to include other creditors as parties to the lawsuit.

> Recovery of corporate assets distributed to former shareholders upon dissolution is permissible in certain circumstances. Such recovery may be proper here, and we hold that Smith may proceed against [the shareholder defendants] individually. (footnotes omitted) *Smith v. Sea Ventures, Inc.*, 93 Wash App 613, 619, 969 P2d 1090, 1093, *review denied*, 138 Wash 2d 1003 (1999).

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The doctrine of laches applies to lawsuits by creditors against shareholder for improper distributions. *Parker v. Richards*, 43 Or App 455, 602 P2d 1154 (1980).

A discussion of creditor lawsuits against directors for improper distributions is contained in Section 9.07 of this book. A discussion of creditor lawsuits against shareholders for improper distributions is contained in Section 10.12 of this book.

D. Cutting off known & unknown claims against a corporation.

Creditors have first priority to corporate assets. But at some point, the board of directors needs to know how much is available for distribution to shareholders.

Generally, a corporation should pay all known, undisputed claims, establish a reserve for the payment of disputed and unknown claims, and only then distribute the balance to the shareholders.

ORS 60.641 sets forth the procedure for cutting off corporate liability for known claims and ORS 60.644 the procedure for cutting off corporate liability for unknown claims. After such claims have been cut-off, the balance of the reserve may be distributed to the shareholders.

Known claims. ORS 60.641 establishes the procedure for disposing of known claims. It provides:

> (1) A dissolved corporation may dispose of the known claims against it by following the procedure described in this section.
> (2) The dissolved corporation shall notify its known claimants in writing of the dissolution at any time after its effective date. The written notice must:
> (a) Describe information that must be included in a claim;
> (b) Provide a mailing address where a claim may be sent;
> (c) State the deadline, which may not be fewer than 120 days from the effective date of the written notice, by which the dissolved corporation must receive the claim; and
> (d) State that the claim will be barred if not received by the deadline.
> (3) A claim against the dissolved corporation is barred:
> (a) If a claimant who was given written notice under subsection (2) of this section does not deliver the claim to the dissolved corporation by the deadline; or
> (b) If a claimant whose claim was rejected by the dissolved corporation does not commence a proceeding to enforce the claim within 90 days from the effective date of the rejection notice.
> (4) For purposes of this section, "claim" does not include a contingent liability or a claim based on an event occurring after the effective date of dissolution.

Unknown claims. ORS 60.644 establishes the procedure for

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disposing of unknown claims. It provides:

> (1) A dissolved corporation may also publish notice of its dissolution and request that persons with claims against the corporation present them in accordance with the notice.
> (2) The notice must:
> (a) Be published one time in a newspaper of general circulation in the county where the dissolved corporation's principal office is located, or if the principal office is not in this state, where its registered office is or was last located;
> (b) Describe the information that must be included in a claim and provide a mailing address where the claim may be sent; and
>
> (c) State that a claim against the corporation will be barred unless a proceeding to enforce the claim is commenced within five years after the publication of the notice.
> (3) If the dissolved corporation publishes a newspaper notice in accordance with subsection (2) of this section, the claim of each of the following claimants is barred unless the claimant commences a proceeding to enforce the claim against the dissolved corporation within five years after the publication date of the newspaper notice:
> (a) A claimant who did not receive written notice under ORS 60.641;
> (b) A claimant whose claim was sent in a timely manner to the dissolved corporation but not acted on; or
> (c) A claimant whose claim is contingent or based on an event occurring after the effective date of dissolution.

E. Distributions to shareholders.

After the board has provided for payment of all debts to third parties, the remaining corporate assets may be distributed to shareholders. Unless shareholders unanimously agree to the contrary, any such distributions are in proportion to the number of shares held by each shareholder. *Kleinschmidt v. Central Trust Co.*, 103 Or 124, 203 P 598 (1922); *Squires v. Balbach Co.*, 177 Neb 465, 129 NW2d 462 (1964); *In re Monks Club, Inc.*, 64 Wash 2d 845, 394 P2d 804 (1964).

Shareholders are entitled to distributions of cash, but not of specific corporate property. *Thimsen v. Reigard*, 95 Or 45, 186 P 559 (1920).

If there is anything still owing on a shareholder's original subscription, the corporation should offset the shareholder's distribution by such sum. *Harrison v. Skinner*, 160 Or 43, 83 P 437 (1938).

If there are two or more classes of stock, the articles of incorporation must set out the relative rights of the classes to distributions upon dissolution. ORS 60.131(3)(C)(d). The articles must provide for the distribution of all of the corporation's net assets among the various classes upon liquidation. ORS 60.131(2).

If there is a class of preferred shares, that class is entitled to

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payment of the preference amount, plus unpaid distributions, before any payments may be made to the common shareholders. *Hay v. Hay*, 38 Wash 2d 513, 230 P2d 791 (1951); *Haworth v. Hubbard*, 220 Ind 611, 44 NE2d 967 (1942). Some courts hold that if the articles are silent as to any further participation in the corporation's assets, the rights of such preferred shareholders are exhausted once the preference has been satisfied. *In re Olympic National Agencies, Inc.*, 74 Wash 2d 1, 442 P2d 246 (1968).

Any shareholder distributions – unclaimed for more than two years after the date for final distribution – are presumed to be abandoned. ORS 98.326. As such, these distributions are subject to the Uniform Disposition of Unclaimed Property Act. ORS 98.302 *et seq*. A prior version of this section was declared unconstitutional. *Realty Associates v. Women's Club*, 230 Or 481, 369 P2d 747 (1962).

In the event the board does not act to liquidate the remaining corporate assets and distribute the proceeds, the shareholders become tenants in common in those assets. *Service Lumber Co. v. Sumpter Valley Ry. Co.*, 81 Or 32, 149 P 531, 152 P 262, 158 P 175 (1916); *Ring v. Williams*, 192 Ga App 329, 384 SE2d 914 (1989); *Ban-Mac, Inc. v. King County*, 69 Wash 2d 49, 416 P2d 694 (1966). In such an event, shareholders also become co-tenants in contractual rights and chooses in action. *Follett v. Clark*, 19 Wash 2d 518, 143 P2d 536 (1944).

> Regardless of whatever the rule may have formerly been, it is now a well-established doctrine that the property of a corporation, including rights of contracts and chooses in action, upon dissolution of the corporation, become vested in the stockholders, subject to the rights of creditors; and ordinarily, and in the absence of debts, the stockholders, upon dissolution of the corporation, become the owners of its assets. (citations omitted) *Smyth v. Kenwood Land Co.*, 97 Or 19, 34-5, 190 P 962, 967 (1920).

If the board does not act to liquidate the remaining corporate assets and distribute the proceeds and if the corporation was leasing real property at the time of the dissolution, shareholders become the leasees. *Closset v. Portland Amusement Co.*, 134 Or 414, 290 P 556, 293 P 720 (1930).

Section 12.05 Administrative Dissolution

A. Grounds for administrative dissolution.

The Secretary of State may dissolve an Oregon corporation on any of the five grounds set out in ORS 60.647:

> (1) The corporation does not pay when due any fees imposed by this chapter;
> (2) The corporation does not deliver its annual report to the Secretary of State when due;
> (3) The corporation is without a registered agent or registered office

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in this state;

(4) The corporation does not notify the Secretary of State that its registered agent or registered office has been changed, that its registered agent has resigned or that its registered office has been discontinued; or

(5) The corporation's period of duration stated in its articles of incorporation expires.

ORS 60.651 describes the procedure for administrative dissolution.

Under prior law, an administrative dissolution was not automatic – a governmental official was required to take all of the steps necessary under the statute in order for the dissolution to become effective. *Klamath Lumber Co. v. Bamber*, 74 Or 287, 145 P 650 (1915). This statute was held to be penal in nature and was thus strictly construed. *Id.*

Under the current Act, an administratively dissolved corporation "continues its corporate existence but may not carry on any business except that necessary to wind up and liquidate its business and affairs" and "notify claimants." ORS 60.651(3).

Thus after dissolution, an administratively dissolved corporation can sell corporate property, but cannot acquire new property. *High v. Davis*, 283 Or 315, 584 P2d 725 (1978). But after reinstatement, the corporation may ratify an acquisition. *Id.*

Prior to enactment of the Model Act, corporations which were delinquent in payment of their annual fee or tax were held not to be able to maintain a suit in the Oregon courts. *East Side Mill & Lumber Co. v. Southeast Portland Lumber Co.*, 155 Or 367, 64 P2d 625 (1937); *Klamath Lumber Co. v. Bamber*, 74 Or 287, 145 P 650 (1915). Arguably under current law, bringing or defending a lawsuit that is "necessary to wind up and liquidate its business and affairs" would be permitted.

***B. Reinstatement*.**

An administratively dissolved corporation may be reinstated within 5-years from the date of the dissolution. ORS 60.654(1). Once the 5-year period has elapsed, the dissolution is irrevocable. *Pacesetter Real Estate, Inc. v. Fasules*, 53 Wash App 463, 767 P2d 961 (1989); *Hawley v. Bonanza Queen Mining Co.*, 61 Wash 90, 111 P 1073 (1910).

Under the current Act, an administratively dissolved corporation continues "its corporate existence but may not carry on any business except that necessary to wind up and liquidate its business and affairs." ORS 60.651(3). If a corporation is reinstated, the reinstatement relates "back to and takes effect as of the effective date of the administrative dissolution and the corporation resumes carrying on its business as if the

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administrative dissolution had never occurred." ORS 60.654(3). In such situations, corporate officers should not be personally liable for contracts signed during the period of dissolution. *Creditors Protection Association, Inc. v. Baksay*, 32 Or App 223, 573 P2d 766, 768 (1978).

Under prior law, any contracts entered into during the period of dissolution were void. *Klorfine v. Cole*, 121 Or 76, 252 P 708, 254 P 200 (1927). It was necessary for reinstated corporations to ratify acts taken during the period of dissolution. *High v. Davis*, 283 Or 315, 584 P2d 725 (1978); *Gillen-Cole Co. v. Fox & Co.*, 146 Or 208, 29 P2d 1019 (1934). But officers and directors who continued to operate a business after dissolution were *not* liable as partners.

> Although this provision suspends the right of delinquent corporations to transact business, it does not expressly invest corporate creditors with a right of action against individual officers. Absent clear evidence of legislative intent to create personal liability, such statutes have not been held to interrupt the existence of delinquent corporations so as to render its members liable as partners. Rather, they have been construed as affecting only the corporation's right to enforce contracts during the period of its delinquency. There is no indication that the legislature contemplated a harsher construction of ORS 57.779(3). In fact, that section specifically provides that claims against a delinquent corporation may be litigated by proceeding against the corporate directors as trustees of the corporation. A judgment thus obtained would be enforceable only against corporate assets, not against the directors personally, because the directors are sued only as trustees. Thus, it is clear that the legislature did not intend for delinquency to give rise to personal liability. (citations omitted) *Creditors Protection Association, Inc. v. Baksay*, 32 Or App 223, 226-7, 573 P2d 766, 768 (1978).

See, also: Micciche v. Billings, 727 P2d 367 (Colo 1986); *Spector v. Hart*, 139 So2d 923 (Fla 2d DCA 1962). *But see: Equipto Division Aurora Equipment Co. v. Yarmouth*, 134 Wash 2d 356, 950 P2d 451 (1997)(persons conducting business after dissolution will be liable if they have "actual knowledge" of the dissolution).

See also: Thomas G. Fischer, Annotation, *Liability of Shareholders, Directors, and Officers Where Corporate Business Is Continued After Its Dissolution*, 72 ALR 4th 419 (1989).

If they dissipated corporate assets during the period of dissolution, officers and directors may be liable to creditors under the trust theory. *Lents, Inc. v. Borstad*, 251 Or 296, 445 P2d 597 (1968). The trust fund theory is discussed in more detail in Section 12.07 of this Chapter.

Section 12.06 Judicial Dissolution

The Oregon circuit courts have the power to dissolve a corporation in certain proceedings initiated by the Attorney General, a shareholder, a

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creditor or the corporation. ORS 60.661 & 60.952.

The Attorney General may initiate a proceeding to dissolve a corporation if the corporation obtained its articles of incorporation through fraud or if the corporation exceeds or abuses the authority conferred upon it by law. ORS 60.661(1).

A creditor may initiate a proceeding to dissolve a corporation if the creditor has obtained a judgment against the corporation, has unsuccessfully tried to execute on that judgment and the corporation is insolvent or, alternatively, if the corporation has admitted in writing that it owes the creditor money but is insolvent. ORS 60.661(3).

ORS 60.661(2) provides that a shareholder may seek dissolution of the corporation if:

(a) The directors are deadlocked in the management of the corporate affairs, the shareholders are unable to break the deadlock and irreparable injury to the corporation is threatened or being suffered, or the business and affairs of the corporation can no longer be conducted to the advantage of the shareholders generally, because of the deadlock;
(b) The directors or those in control of the corporation have acted, are acting or will act in a manner that is illegal, oppressive or fraudulent;
(c) The shareholders are deadlocked in voting power and have failed, for a period that includes at least two consecutive annual meeting dates, to elect successors to directors whose terms have expired; or
(d) The corporate assets are being misapplied or wasted.

NOTE: In the case of close corporations, ORS 60.952 provides a similar remedy – although this statute include a number of alternative remedies short of dissolution. See Section 8.04.

A corporation may initiate a proceeding to have its voluntary dissolution continued under court supervision. ORS 60.661(4).

Courts also have the power to appoint a receiver to wind up a corporation's business and affairs. ORS 60.667.

***A. Shareholder initiated dissolutions*.**

ORS 60.661(2) permits a shareholder to seek judicial dissolution of the corporation where the majority's conduct is "illegal, oppressive or fraudulent" or where there is a voting deadlock. For close corporations, ORS 60.952 provides a similar remedy.

A more detailed discussion of shareholder actions seeking judicial dissolution appears in Section 8.04 of this book.

The term "oppression" has been addressed in a number of cases. *Naito v. Naito*, 178 Or App 1, 20-1, 35 P3d 1068 (2001);*Tifft v. Stevens*,

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162 Or App 62, 78, 987 P2d 1 (1999), *review denied,* 330 Or 331, 6 P3d 1101 (2000); *Iwasaki v. Iwasaki Bros., Inc.*, 58 Or App 543, 649 P2d 598 (1982); *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 628-9, 507 P2d 387, 393-4 (1973); *Robblee v. Robblee*, 68 Wash App 69, 76, 841 P2d 1289, 1293 (1992). Recently, the Oregon Court of Appeals said:

> Although there is not, and probably cannot be, a definitive definition of oppressive conduct under the statute, at least in a closely held corporation conduct that violates the majority's fiduciary duties to the minority is likely to be oppressive. *Cooke v. Fresh Express Foods Corp.*, 169 Or App 101, 108, 7 P3d 717 (2000).

ORS 60.661 also permits the court to dissolve a corporation in the event of shareholder or director deadlock.

"Deadlock is the inaction which results when two equally powerful factions stake out opposing positions and refuse to budge." (footnote omitted) *Wilcox v. Stiles*, 127 Or App 671, 678, 873 P2d 1102, 1105 (1994).

If one shareholder owns a majority of the shares, the corporation is not necessarily deadlocked simply because its board is deadlocked since ORS 60.661(2)(a) also requires that "the shareholders are unable to break the deadlock." *See also: Gregory v. J. T. Gregory & Son, Inc.,* 176 Ga App 788, 338 SE2d 7 (1985). Likewise, even though shareholders are deadlocked, a corporation in not necessarily deadlocked if the board itself is not deadlocked or if the shareholder deadlock has not lasted through at least two consecutive annual meeting dates. ORS 60.661(2)(c); *Jackson V. Nicolai-Neppach Co.*, 219 Or 560, 348 P2d 9 (1959).

***B. Court's power to dissolve is discretionary*.**

A court's power to dissolve a corporation under ORS 60.661 is a discretionary power, one which courts are most hesitant to exercise. For instance, after a lengthy discussion of the evolution of this power, the court in *Jackson V. Nicolai-Neppach Co.*, 219 Or 560, 348 P2d 9 (1959) said:

> The shareholder deadlock provisions of the Illinois Business Corporation Act, of the Model Business Corporation Act, and of the Oregon Business Corporation Law are clearly couched in language of permission. It is incredible that the many able lawyers who worked from time to time on these three identical acts would have used such phraseology to express a mandate. The statute contemplates that the court of equity shall take jurisdiction once a requisite showing of fact is made and contemplates further that having taken jurisdiction it will bring its discretion to bear in granting or refusing to grant equitable relief. The very fact that the legislature has made the remedy of liquidation a matter of discretion for the courts is a mandate to us to use discretion, and we would not be carrying out the legislative will by simply decreeing liquidations as a matter of course once the jurisdictional facts and nothing more are proven. The common law rule was thought to be an insufficient

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> safeguard of the rights of the half-owner of a corporation who happened to be out of power. As we read the statute its intent is to obligate the courts to thread their way from case to case without the assistance of sweeping generalizations. *Jackson V. Nicolai-Neppach Co.*, 219 Or 560, 574-5, 348 P2d 9, 16 (1959).

The *Jackson* case is discussed in a casenote: 39 OR L REV 382 (1960).

See, also: McMunn v. ML&H Lumber, Inc., 247 Or 319, 429 P2d 798 (1967); *Interlake Porsche & Audi, Inc. v. Bucholz*, 45 Wash App 502, 728 P2d 597 (1986).

In *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 507 P2d 387 (1973), the court again noted that the power granted by the judicial dissolution statute was discretionary and pointed out that this statutory power did not limit the court's more general equitable power to protect minority shareholders by fashioning remedies other than dissolution.

This author has been unable to find any Oregon appellate decision in which judicial dissolution was ordered.

Courts will usually not intervene even in the case of alleged director incompetence and mismanagement. *Beeler v. Standard Investment Co.*, 107 Wash 442, 181 P 896 (1919). One decision recognized the right of the board to shift the balance of voting power, stating that "directors . . . may in the exercise of their honest business judgment adopt a valid method of eliminating what appears to them a clear threat to the future of their business by any lawful means." *Hendricks v. Mill Engineering & Supply Co.*, 68 Wash 2d 490, 495, 413 P2d 811, 813-4 (1966).

The Oregon Supreme Court has said:

> In the absence of a fraudulent or coercive design or purpose on the part of the management neither the judgment of the court nor that of a minority stockholder can properly be substituted for the judgment of the majority of the directors and stockholders of a corporation. *Horner v. Pleasant Creek Mining Corp.*, 165 Or 683, 699, 107 P2d 989, 995, 109 P2d 1044 (1941).

Another court put it more bluntly:

> No principle of law is more firmly fixed in our jurisprudence than the one which declares that the courts will not interfere in matters involving merely the judgment of the majority in exercising control over corporate affairs. *Regenstein v. J. Regenstein Co.*, 213 Ga 157, 159 97 SE2d 693, 695 (1957).

Usually, either bad faith or fraud is required to be present in order for a court to intervene in internal corporate affairs.

A court may find inequitable conduct, but order relief short of dissolution. *Browning v. C & C Plywood Corp.*, 248 Or 574, 434 P2d 339

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(1968); *Delaney v. Georgia-Pacific Corp.*, 278 Or 305, 564 P2d 277, *supplemented*, 279 Or 653, 569 P2d 604 (1977), *appeal after remand*, 42 Or App 439, 601 P2d 475 (1979); *Agronic Corporation of America v. deBough*, 21 Wash App 459, 585 P2d 821 (1978).

***C. Court's equitable power to regulate corporate affairs*.**

In addition to the rights granted by ORS 60.661, courts retain the equitable power to dissolve or regulate the affairs of a corporation. Oregon courts are more willing to utilize their equitable powers in order to fashion remedies other than dissolution. *See, for example: Browning v. C & C Plywood Corp*, 248 Or 574, 434 P2d 339 (1968); *Baker v. Commercial Body Builders, Inc.*, 264 Or 614, 507 P2d 387 (1973); *Delaney v. Georgia-Pacific Corp.*, 278 Or 305, 564 P2d 277, *supplemented*, 279 Or 653, 569 P2d 604 (1977), *appeal after remand*, 42 Or App 439, 601 P2d 475 (1979).

Section 12.07 Insolvent Corporations; Rights of Creditors; Trust Fund Theory

***A. Duty of directors*.**

Once a corporation becomes insolvent, directors have an obligation to protect corporate assets for the corporation's creditors. As discussed below, courts have sometimes said that upon insolvency, directors become trustees holding corporate assets for the benefit of creditors.

Certainly, officers and directors cannot use their positions to obtain an unfair advantage for themselves over other corporate creditors. In particular, officers and directors may be held liable to corporate creditors if they diverted corporate funds to themselves when the corporation is insolvent.

> By the great weight of authority, where a corporation is insolvent or has reached such condition that its directors or officers see that they must deal with its assets in the view of its probable suspension, they cannot use those assets to prefer themselves as creditors or sureties in respect to past advances to the prejudice of general creditors. *Gantenbein v. Bowles*, 103 Or 277, 289-90, 203 P 614, 619 (1922).

See, also: Randall & Neder Lumber Co., Inc. v. Randall, 202 Ga App 497, 414 SE2d 718 (1992); *Wortham v. Lachman-Rose Co.*, 440 SW2d 351 (Tex Civ App 1969).

***B. Rights of creditors*.**

Directors may be held personally liable to creditors if they dissipate assets of their dissolved corporation. *Lents, Inc. v. Borstad*, 251 Or 296, 445 P2d 597 (1968).

A judgment creditor may seek the appointment of a receiver if the

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corporation is insolvent. ORS 60.661(3). Under some circumstances, a creditor may initiate an involuntary bankruptcy proceeding.

A transfer of corporate assets for inadequate consideration may be set aside as fraudulent – particularly if the transfer is to an officer, director or shareholder. *Allen v. Meinig*, 109 Or App 341, 819 P2d 744 (1991), *review denied*, 313 Or 209, 830 P2d 595 (1992); *Peterson v. Harville*, 445 F Supp 16, 24 (D Or 1977); *Eagle Pacific Insurance Co. v. Christensen Motor Yacht Corp.*, 135 Wash 2d 894, 959 P2d 1052 (1998); *Randall & Neder Lumber Co., Inc. v. Randall*, 202 Ga App 497, 414 SE2d 718 (1992); *US Marketing Concepts, Inc. v. Don Jacobs Buick-Subaru, Inc.*, 547 NE2d 892 (Ind App 1989).

In the event assets of a dissolved corporation are distributed to shareholders before payment of corporate debts, creditors may seek satisfaction from shareholders to the extent of the distributed assets. ORS 60.645(2); *Lonsdale v. Chesterfield*, 99 Wash 2d 353, 662 P2d 385 (1983); *Fountain v. Burke*, 160 Ga App 262, 287 SE2d 39 (1982); *Spokane Merchants' Association v. Lobe*, 13 Wash App 68, 533 P2d 133 (1975).

> More important, a creditor of a corporation can satisfy his claim against the corporation out of the assets distributed to stockholders upon dissolution. (citations omitted) *Wakeman v. Paulson*, 257 Or 542, 546-7, 480 P2d 434, 437 (1971).

But, see: Walter A. Wood Reaping and Mowing Manufacturing Co. v. Angemeier, 51 Ind App 258, 99 NE 500 (1912).

> The law which sends a corporation into the world with the capacity to act imposes upon its assets liability for its acts. The corporation cannot disable itself from responding by distributing its property among its stockholders and leaving remediless those having valid claims. In such a case the claims after being reduced to judgments may be satisfied out of the assets in the hands of the stockholders. *Pierce v. United States*, 255 US 398, 402 (1921).

As describe in Sections 10.11 and 10.12, a creditor of an insolvent corporation may usually recover debts owed to the corporation by shareholders only through an equitable proceeding naming all creditors and shareholders located within the jurisdiction. *Wakeman v. Paulson*, 264 Or 524, 506 P2d 683 (1973); *Davis v. Olson*, 4 Wash App 390, 482 P2d 795 (1971); *Royer v. Maib*, 6 Wash 2d 286, 107 P2d 593 (1940). This also seems to be the rule in actions to collect improper distributions after dissolution.

> From the principle thus established in this state the proper remedy of a creditor of an insolvent corporation to reach the fund alleged to have been paid to a stockholder as a dividend in liquidation is by a suit in equity and not by an action at law as commenced in the case at bar.

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> *Garetson Lumber Co. v. Hinson*, 69 Or 605, 610, 140 P 633, 635 (1914).

Some courts permit a creditor to initiate a proceeding directly against shareholders without mentioning any requirement that the plaintiff-creditor include other creditors as parties to the lawsuit.

> Recovery of corporate assets distributed to former shareholders upon dissolution is permissible in certain circumstances. Such recovery may be proper here, and we hold that Smith may proceed against [the shareholder defendants] individually. (footnotes omitted) *Smith v. Sea Ventures, Inc.*, 93 Wash App 613, 619, 969 P2d 1090, 1093, *review denied*, 138 Wash 2d 1003 (1999).

If a corporation sells its assets and, in exchange, receives insufficient consideration, fraudulent transfer statutes may also apply. ORS 95.200 *et seq*; *Allen v. Meinig*, 109 Or App 341, 819 P2d 744 (1991), *rev denied*, 313 Or 209, 830 P2d 595 (1992); *Eagle Pacific Insurance Co. v. Christensen Motor Yacht Corp.*, 135 Wash 2d 894, 959 P2d 1052 (1998); *Hall v. Armstrong Cork, Inc.*, 103 Wash 2d 258, 692 P2d 787 (1984).

If just prior to, or after, insolvency, corporate assets are transferred to officers, directors or shareholders for inadequate consideration, a court may pierce the corporate veil and impose liability for corporate debts on the person or persons receiving the assets. Piercing the corporate veil is discussed in more detail in Chapter Ten of this book.

The United States Bankruptcy Code is an alternative which may be pursued by disappointed creditors.

***C. Trust fund theory*.**

The "trust fund theory" was first set down by Mr. Justice Story in *Wood v. Dummer*, 3 Mason 308 (1824). Essentially, the trust fund theory provides that a corporation's capital stock, or, if insolvent, its assets equivalent to its capital stock, constitutes a trust fund for the benefit of its creditors. FLETCHER CYC CORP § 7369. A corporation's board of directors constitute the trustees of this trust fund.

> The doctrine that the stock of a corporation is a trust fund for the benefit of creditors is one which is founded in equity and fair dealing, and in any event has become so well established in this country that it can no longer be gainsaid. This doctrine was announced by Chancellor Kent, as early as 1824, in *Wood v. Dummer*, 3 Mason, 309, and since that time has become the established law of this country and is termed the "American doctrine," although, as shown in the case above referred to, the same doctrine had long been established in England; and so universally has this doctrine been accepted, in America especially, that the citation of authorities seems a work of supererogation. We will, however quote from 2 Morawetz on Private Corporations, § 820, the rule which is announced as follows:

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> Debts due a corporation are equitable assets, and may be reached by creditors through the aid of a court of chancery, if the legal assets which can be reached by execution prove insufficient. The liability of the shareholders to contribute the amount of their shares as capital is treated in equity as assets, like other legal claims belonging to the corporation. This liability, together with the capital actually contributed, constitutes the trust fund which in equity is deemed pledged for the payment of corporate debts.

Adamant Manufacturing Co. of America v. Wallace, 16 Wash 614, 617-8, 48 P 415, 416 (1897).

By the turn of the century, cases began to limit application of the trust fund theory to situations "involving the liquidation of a corporation by sale of all its assets to another company." *Meikle v. Export Lumber Co.*, 67 F2d 301, 304 (9th Cir 1933). *See also: Lantz v. Moeller*, 76 Wash 429, 434, 136 P 687, 688 (1913).

Under the trust fund theory, assets of an insolvent corporation were deemed to be a trust fund for all creditors and the corporation was prohibited from preferring creditors. Corporate assets were to be distributed equally and ratably among all creditors. One court said the trust fund theory means:

> an insolvent corporation may not prefer its creditors; that, although an individual creditor may do so, even to the exhaustion of his property, the right does not exist in a corporation; that its property on insolvency becomes a trust fund for the benefit of all of its creditors to be equally and ratably distributed among them. *Woods v. Metropolitan Nat. Bank*, 126 Wash 346, 218 P 266, 267 (1923).

The trust fund theory applied to all corporate assets at the time of insolvency.

> The assets of an insolvent corporation constitute a trust fund for the payment of its creditors. Those assets may consist of property in the possession of the corporation, accounts receivable, choses in action, claims of various kinds, as well as unpaid stock subscriptions, payments made to creditors in preference of the rights of other creditors, statutory claims against officers and trustees, and rights against stockholders for dividends paid out of capital. *Gaunce v. Schoder*, 145 Wash 604, 261 P 393, 393 (1927).

Under the trust fund theory, a creditor could seek to have a court set aside preferential transfers. That proceeding was in equity. *Gaunce v. Schoder*, 145 Wash 604, 261 P 393, 393 (1927). In such actions, the creditor was required to prove: (i) that the disputed transfer occurred while the corporation was insolvent; (ii) that the asset depleted corporate assets; and (iii) resulting damage to the creditor. *Cargill, Inc. v. American Pork Producers, Inc.*, 426 F Supp 499, 507 (D S Dak 1977).

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D. Oregon has never fully accepted trust fund theory.

The trust fund theory, in its broadest construction, is not widely followed today. Oregon has never fully accepted the doctrine, but rather, has limited its application.

> The trust fund doctrine first enunciated by Judge Story in *Wood v. Dummer*, 3 Mason 308, that a corporation holds its property in trust for the benefit of its creditors has not been accepted in this state as applicable to solvent corporations. It, of course, applies to insolvent corporations, or where a court has taken hold of the corporate assets for the purpose of distribution. *Loveland & Co. v. Doernbecher Manufacturing Co.*, 149 Or 58, 72, 39 P2d 668, 674 (1934).

See, also: Macbeth v. Banfield, 45 Or 553, 78 P 693 (1904).

Early Oregon cases limited the trust fund theory to situations "involving the liquidation of a corporation by sale of all its assets to another company." *Meikle v. Export Lumber Co.*, 67 F2d 301, 304 (9th Cir 1933).

Oregon courts have held over and over the trust fund theory is inapplicable to solvent corporations. Oregon courts have even refused to apply the trust fund theory to insolvent corporations which are still "going concerns."

> The existence of the trust doctrine as applicable to the assets of a corporation which is a "going concern" has been denied by this court. The rule has been settled by our adjudications that mere insolvency does not of itself convert corporate property into a trust fund; but, when a corporation ceases to transact business and is insolvent, its assets then constitute a trust fund for the payment of the corporate debts without the intervention of a court of equity to administer upon the property for the purpose of a final settlement. (citations omitted) *Garetson Lumber Co. v. Hinson*, 69 Or 605, 609-10, 140 P 633, 634-5 (1914).

See, also: Stumbo v. Paul B. Hult Lumber Co., 251 Or 20, 444 P2d 564 (1968).

Today as applied by the Oregon courts, the trust fund theory requires directors of insolvent, dissolving corporations to not prefer one group of creditors over other groups. In particular, directors must not prefer themselves.

> By the great weight of authority, where a corporation is insolvent or has reached such condition that its directors or officers see that they must deal with its assets in the view of its probable suspension, they cannot use those assets to prefer themselves as creditors or sureties in respect to past advances to the prejudice of general creditors. *Gantenbein v. Bowles*, 103 Or 277, 289-90, 203 P 614, 619 (1922).

If directors dissipate assets of an insolvent, dissolving corporation, they may be held personally liable by creditors. *Lents, Inc. v. Borstad*, 251 Or 296, 445 P2d 597 (1968).

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