Washington State
House of Representatives
Office of Program Research

BILL ANALYSIS

Judiciary Committee

SB 6596

Title: An act relating to the dissolution of Washington corporations.

Brief Description: Revising the dissolution of Washington corporations.

Sponsors: Senators Kline, Johnson, Weinstein and Esser.

Brief Summary of Bill

- Amends provisions of the Business Corporations Act relating to the authorization, procedures, and legal effect of a voluntary dissolution.
- Establishes claim-barring procedures affected by either, a dissolved corporation's compliance with notice requirements, a court order, or the expiration of a revised survival of claims period.
- Specifies processes by which a dissolved corporation may make reasonable provision for the satisfaction of its liabilities, and by which an unpaid claim against a dissolved corporation may be recouped.
- Establishes a shareholder's liability for knowingly accepting an unlawful distribution from the dissolved corporation.

Hearing Date: 2/20/06

Staff: Elisabeth Frost (786-5793).

Background:

The last stage of corporate existence is its dissolution and liquidation ("winding up"). Dissolution is the formal termination of the corporation's legal existence and liquidation is the procedure occurring after dissolution to settle all remaining corporate affairs (e.g., distribution of assets, payment of debts, etc.). The procedures by which a corporation may be dissolved and the effects of that dissolution are set out in Washington's Business Corporations Act (BCA). The BCA is modeled largely after the Revised Model Business Corporations Act (RMBCA), sections of which were first adopted by the Legislature in 1989. The majority of states have adopted some form of this act. Washington adopted many, but not all, of the RMBCA's provisions relating to the dissolution of corporations.

A corporation may be dissolved either voluntarily, administratively, or judicially; the procedures for each type of dissolution are found in the BCA. A corporation may be dissolved administratively by the Secretary of State's office under certain circumstances, such as when a corporation fails to pay a license fee or penalty when it becomes due. In certain situations, a corporation may be subject to dissolution in superior court as the result of proceedings brought by the Attorney General, a shareholder, or a creditor.

The procedures for distributing assets of a dissolved corporation to creditors and shareholders are found in the BCA. The Legislature has adopted the section of the RCMBA which provides the procedure to be followed for claims known at the time of dissolution. Under current law, an action for a claim that arose prior to the dissolution of a corporation must be commenced within two years of the effective date of dissolution, or it is barred.

The RCMBA also includes a provision related to post-dissolution claims, which the Legislature did not adopt. The common law rule for post-dissolution claims is that claims against corporations terminate upon the corporation's dissolution. In 2005, the Washington State Court of Appeals ruled that because the Legislature had adopted the provision of the RCMBA related to claims known at the time of dissolution, but declined to adopt the provision related to *post-dissolution* claims, any claims arising after the dissolution of a corporation (and the subsequent "winding up" period) are barred under the common law rule.

The Washington State Bar Association's Corporate Act Revision Committee was involved in drafting the version of the RCMBA that the Legislature adopted in 1989, and for approximately two years has been working on proposed revisions to the dissolution chapter of the BCA.

Summary of Bill:

The recommendations of the Washington State Bar Association's Corporate Act Revision Committee are adopted.

<u>Procedure for authorization of voluntary dissolution:</u>
By the initial directors or incorporators if a corporation has not issued shares
If a corporation has not issued shares, a majority of the initial directors, or, if initial directors were not named in the articles or incorporation and have not been elected, a majority of the incorporators, may authorize dissolution.

By the board of directors without shareholder approval
If a corporation has issued shares, a majority of the board of directors may authorize dissolution without approval by the shareholders if the board finds that the corporation is insolvent, and 10 or more days have elapsed since the corporation gave notice to all shareholders of the intent of the board of directors to authorize dissolution.
[NOTE: *For the purposes of this summary, an "insolvent corporation" is a corporation that is not able to pay its liabilities as they become due in the usual course of business, or the corporation's assets are less than the sum of its total liabilities.*]

As under current law, the board of directors may not authorize dissolution without approval of the shareholders if the articles of incorporation prohibit it from doing so.

By the board of directors with shareholder approval

If a corporation's board of directors proposes dissolution for submission to the shareholders, the corporation must notify all shareholders of the proposed dissolution. As under current law, this notice may be affected by giving notice of a shareholder's meeting as provided for in the BCA and stating that the purpose or one of the purposes of the meeting is to consider dissolving the corporation. The notice may also be given if the board of directors complies with the BCA's requirements for shareholder action without a meeting.

Procedure for effecting voluntary dissolution:
After dissolution is authorized as required by *any* of the procedures described above, the corporation may dissolve by delivering to the Secretary of State's office a copy of a revenue clearing certificate, articles of dissolution, and a statement that the dissolution was authorized by the applicable procedure.

For the purposes of the BCA's chapter on corporate dissolution, a "dissolved corporation" is defined as a corporation whose:

- dissolution has been duly authorized by the applicable procedure; and
- articles of dissolution have become effective.

A "dissolved corporation" includes any trust or other successor entity to which the remaining assets of the corporation are transferred subject to its liabilities for purposes of liquidation.

Notice of voluntary dissolution:
A dissolved corporation must, within 30 days after the effective date of its articles of dissolution, publish notice of its dissolution requesting that persons with claims against the dissolved corporation present them in accordance with the notice. The notice is to describe information that must be included in a claim, provide a mailing address where a claim may be sent, and state that claims against the dissolved corporation may be barred if not timely asserted.

The notice must be published once a week for three consecutive weeks in a newspaper of general circulation in the county where the dissolved corporation's principal office (or, if none in this state, its registered office) is or was last located.

Failure to publish notice in accordance with the above does not affect the validity or the effective date of a dissolved corporation's dissolution. However, the consequence of failure to publish is ineligibility for the claims-barring procedures discussed below and in the section immediately following that addresses judicially barred claims.

Claims-barring procedures
A dissolved corporation that has complied with the published notice requirement above may dispose of any or all known claims against it by giving written notice of its dissolution to the holders of the known claims. The notice is to include information about the claim, a mailing address where a notice of claim may be sent, the deadline by which the dissolved corporation must receive a written notice of claim, the circumstances under which the claim will be barred, and information about the claimant's right to commence a proceeding within 90 days to enforce the action, should the dissolved corporation reject the claim.

Procedures for making reasonable provision for creditors' claims:
As under current law, a dissolved corporation may not make any distributions to its shareholders if after such distribution, the corporation would not be able to pay its liabilities as they become

due in the usual course of business. As to when a transfer of assets to a trust or other successor entity constitutes a "distribution," it is clarified that a "distribution" is effected only when and to the extent that the assets have been distributed by the trust or successor entity to shareholders.

As under current law, following dissolution, a corporation may not carry on any business except what is appropriate to wind up and liquidate its business and affairs. During this "winding up" period, a corporation is to satisfy or make reasonable provisions for satisfying its liabilities. As to what constitutes "reasonable provision," it is specified that a dissolved corporation's board of directors may make reasonable provision for the satisfaction of any liability by:

- purchase of insurance coverage for liabilities;
- provision of security for liabilities;
- contractual assumption of liabilities by a solvent person; or
- any other means that the board of directors determines is reasonably calculated to provide for satisfaction of the reasonably estimated amount of such liability.

In determining what constitutes "reasonable provision" for satisfying a dissolved corporation's liabilities, the board of directors may disregard and make no provision for the satisfaction of any liabilities that it does not consider, based on the facts known to it, reasonably likely to arise prior to expiration of the survival period for claims against a dissolved corporation.

The board of directors may at any time petition to have the dissolution continued under court supervision. Upon a finding that the corporation is insolvent, the board of directors may dedicate the corporation's assets to the repayment of its creditors by making an assignment for the benefit of creditors, or obtaining the appointment of a general receiver. Once a court, an assignee for the benefit or creditors, or a general receiver assumes control over the corporation's assets, the directors are relieved of any further duties related to the liquidation of the corporation's assets or the application of assets or proceeds toward satisfaction of its liabilities.

Judicial claims-barring procedure
A dissolved corporation that has published notice of its dissolution may file an application in superior court for determination of:

- the amount and form of reasonable provision to be made for the satisfaction of any kind of claim or liability that has arisen or is likely to arise prior to expiration of the survival period; or
- whether the provision made or proposed by the board of directors for the satisfaction of any one or more claims or liabilities is reasonable.

A dissolved corporation filing such an application must give written notice to any person whose claim or potential claim is sought to be determined under the application. If there are persons with claims or potential claims under the application whose identities or mailing addresses are unknown, then the court may appoint a guardian ad litem to represent those persons. Any determination made by a court on claims under such an application is conclusive for purposes of determining the legality of any subsequent distributions to shareholders.

Provision by the dissolved corporation for satisfaction of claims or potential claims in the amount and form ordered by the court satisfies the corporation's obligations with respect to such claims, and any further or greater claims based on the same facts, dealings or contract are barred.

Provisions for collection of unpaid claims:
The holder of an unpaid claim against a dissolved corporation that is not barred by other provisions of the BCA, may, within the statute of limitations applicable to the claim commence a proceeding against the dissolved corporation to collect the amount of the claim from any remaining undistributed assets of the corporation.

If the undistributed assets are insufficient to satisfy the amount of the unpaid claim, under certain circumstances the claimant may include as part of the relief claimed, a petition to compel the dissolved corporation to collect any amounts owing to it by directors or shareholders to be applied toward payment of the claim. If the dissolved corporation fails to join those directors and shareholders who may be liable for such amounts, the claimant may join all such directors and shareholders as additional defendants in the proceeding.

Liability of shareholders for unlawful distributions:
If a shareholder accepts a distribution that the shareholder knows was made in violation of either the BCA's provisions regarding distributions to shareholders, or the articles of incorporation, the shareholder is personally liable to the corporation for the amount of any distribution received to the extent it exceeds the amount that could have properly been distributed to the shareholder.

A shareholder held liable for receiving such an unlawful distribution is entitled to contribution from every other shareholder who could be held similarly liable.

A proceeding to recoup such an unlawful distribution from a shareholder is barred unless it is commenced prior to either the expiration of two years after the date on which the distribution was effective, or the expiration of the survival period for claims against a dissolved corporation, whichever is earlier.

Administrative dissolution:
As under current law, a corporation administratively dissolved continues its corporate existence but may not carry on any business except that necessary to wind up and liquidate its business and affairs, such as taking action to reasonably provide for creditor's claims.

A corporation administratively dissolved may not have access to the claims-bar procedures available to voluntarily dissolved corporations that comply with the BCA's notification requirements.

Judicial appointment of receivers and judicial dissolution:
Judicial appointment of a receiver for a voluntary dissolution
The superior courts may appoint a receiver when a voluntarily dissolved corporation files an application with the court to determine the amount and form of reasonable provision to made for the satisfaction of claims or liabilities, or the reasonableness of the board's proposal for such satisfaction.

Judicial dissolution
The superior courts may dissolve a corporation in a proceeding brought by a creditor if the corporation has admitted in writing, or the creditor otherwise establishes that the corporation is insolvent.

A court in a proceeding for judicial dissolution of a corporation brought under the requisite circumstances by the Attorney General, a shareholder, or a creditor, may appoint one or more

general receivers to wind up and liquidate the business and affairs of the corporation. If the corporation is not yet dissolved, a court may appoint one or more custodial receivers to manage its business and affairs. Prior to appointing a general or custodial receiver, the court is to hold a hearing after notifying all parties to the proceeding and any interested parties designated by the court. The hearing, and any resulting receivership, is to be conducted in accordance with state statutory law governing receiverships.

Survival period for claims against a dissolved corporation
The survival period for claims existing prior to or arising after dissolution of a corporation is as follows:

Dissolutions effective prior to the effective date of this act
Actions or proceedings asserting claims against a dissolved corporation, its directors, officers, or shareholders, must be commenced within two years after the effective date of the corporation's dissolution.

Dissolutions effective on or after the effective date of this act
Actions or proceedings asserting claims against a dissolved corporation, its directors, officers, or shareholders, must be commenced within three years after the effective date of the corporation's dissolution.

Appropriation: None.

Fiscal Note: Not requested.

Effective Date: The bill takes effect 90 days after adjournment of session in which bill is passed.