



# **Business Law and Bankruptcy**

## **Class 8**



# The Shareholder - Key Features

- Anyone can be a shareholder, including:
  - Individual investors
  - State and private pension funds
  - Mutual funds
  - Companies
  - Employees
- These different investors each have their own unique set of concerns and interests.
- Thus, they must assert their individual voices in order to achieve their financial goals that led them to invest in the first place.
- Investors therefore must act with intelligence, strategically, and often together with other shareholders in order to have their needs met.



# Rights of the Shareholder

- Acts of shareholders (usually come at the Annual Meeting or at a special meeting called by the directors)
- Election of directors; by
  - Single Slate
  - Staggered Board
    - (to protect from hostile bidders and to simplify the transition)
- Approve or disapprove fundamental changes in the organization
- The right to vote at a meeting is determined by who owned the shares on the “record date,” which is set up by the directors in advance of the meeting.
  - Purchasers of shares after the record date cannot vote those shares at the meeting.



# Shareholder Voting: The Proxy System

- Definition: An authorization, given by the shareholder to a third party to vote in the shareholder's place (to whatever extent the shareholder would be allowed to vote)
  - Note: The person who is being appointed to vote for the shareholder is also known as a “**proxy**”
- Purpose: To allow shareholders who can't physically make it to the meeting to vote anyway



# Shareholder Voting: The Proxy System

- General Requirements for a **proxy authorization document**:
  - Names of the shareholder and the proxy voter and number of shares to be voted
  - What the authorized vote is (e.g., “yes” or “no” on an issue)
  - A shareholder can limit the authorization to whatever he or she wants
  - The duration of the proxy
    - Default rule: capped at 11 months (to cover only one annual meeting)



# Shareholder Voting: The Proxy System

- Proxies are usually fully revocable, but can be irrevocable if:
  - the proxy is “coupled with an interest” (i.e., there is consideration given for the proxy)
  - there is a voting contract (disallowed by some states) that can be specifically enforced
  - there is a “voting trust” agreement between the shareholders (works similarly to a regular trust)



# How Shareholders Get Their Money from a Corporation

- **Dividends:**

- The Board declares how much will be given on a per share basis
- Once a dividend has been declared, it becomes a debt of the corporation and the corporation must pay it; the shareholders can actually sue to enforce the dividend.
- Taxed as income to the shareholder

- **Share Repurchase Plan:**

- Gives the option to shareholders to sell back their shares to the company (either unlimited or limited to a percentage of the shareholder's holding in the corporation) for a set price



# How Shareholders Get Their Money from a Corporation

- **Dissolution dividends:**

- Each shareholder gets his or her percentage of the corporation's assets when the corporation dissolves
- This usually doesn't amount to much because, when big corporation dissolve, it's usually because they're bankrupt

- **Distribution of corporation property**

- (usually only relevant in small corporations)



# QUIZ TIME!



# The Right of Appraisal

- When applicable: Applies whenever a corporation is dissolving or completely selling out to another company, such as:
  - Merging with another company
  - Being acquired by another company
  - Dissolution/ bankruptcy
  - A change that affects voting rights of the stock
  - Changes to a class of stock that affects its voting or dividend rights



# The Right of Appraisal

- Note: In order to seek an appraisal, the shareholder must have dissented from the proposed action!
- The shareholders of the selling company have the right to have a court determine that they are being fairly compensated for their shares.
- In an extreme case, a court can say that the deal has to be undone because it's unfair to shareholders. However, usually appraisal actions are to determine what the fair value that each shareholder should get for his or her shares.



# Factors a Court will Consider in Determining Fair Value

- Public price of the stock (if available) at time of transaction and during period prior to transaction (usually tracked over 5 years at a minimum)
- Price of the stock as paid by the purchasing company in the transaction
- Any competing bids offered in the transaction
- Professional evaluation of the value of the company and its shares (usually done by investment bankers from both the company and the shareholder – typically a discounted cash flow model is made)
- Value of the assets transferred (real property, machinery, goodwill, etc.)
- Value of any shares of the purchasing company transferred (if shares exchanged in the sale)
- Overall economic and legal health of the firm – particularly as concerns the chances that the firm may be forced into bankruptcy