STATEMENT BY NEAHTAWANTA SUMMER RESORT ASSOCIATION IN SUPPORT OF H.B. 4312 AND H.B. 4313

To: House Local Government Committee
From: Neahtawanta Resort Association
Date: October 17, 2023
Re: Why HB 4312 and HB 4313 are needed

EXECUTIVE SUMMARY

The Neahtawanta Resort Association ("Neahtawanta") is a Summer Resort Association ("SRA") organized under the Summer Resort and Park Association Act, 1897 PA 230, MCL 455.1, *et seq.* ("Act 230").

Together, House Bills 4312 and 4313 will enable an SRA organization incorporated under Act 230 to use the Nonprofit Corporation Act of 1982, MCL 450.1746 ("NCA"), to convert to a nonprofit corporation. This is the same purpose sought to be achieved by previous versions of this legislation that were introduced in past sessions, beginning in 2016 (HBs 5508 and 5509, HBs 4048 and 4049, which were introduced by Rep. Inman, and HRs 5463 and 5464, which Rep. Roth introduced in the last session). The first time they were introduced they passed in the House and had advanced to the third reading in the Senate when Treasury (through State Tax Commission Executive Director, Heather Frick) requested time for additional review to ensure that the bills had no revenue or property tax implications.

Unfortunately, by the time Treasury completed its review, found that the Bills had no adverse revenue effects, and released its hold request, too little time remained to complete the enactment process, so they were reintroduced in each of the three following sessions. Each time they had not progressed far enough when events beyond anyone's control derailed them, including the problems that Rep. Inman encountered and the enactment of a Senate Bill introduced by Senator Schmidt in the last session that addressed some, but not all, of the problems that make conversion to a modern non-profit corporation a preferable alternative to continuing as an SRA.[1]

Several of the Act 230's 126-year-old provisions are inconsistent with the way modern corporate organizations are managed and operated and have become burdensome for Neahtawanta. Among them are the following:

- <u>The SRA originally limited the value of personal property an SRA can hold to $200,000.</u>[2] Neahtawanta's "rainy day fund," which is used for maintenance and repair of streets and

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[1] Senator Schmidt's Bill, SB 129, a copy of which is attached, modified some of the troublesome provisions of Act 230, but did not allow conversion to a non-profit corporation. This memo notes the points on which Senator Schmidt's bill altered some provisions of Act 230, and the new problems caused by some of the amendments made.

[2] SB 129 increased this amount to $6,000,000, but did not remove the limitation on the value of personal property that an SRA may hold. It remains an arbitrary limitation that no

common areas and to enable it to implement long term planning, is close to that limit. By contrast, the NCA places no limit on the value of the personal property a non-profit corporation may hold.

- Under Act 230 only shareholders could be directors. MCL 455.9. That made it difficult for a small association like Neahtawanta, which has only 60 members, to compose a board slate, because, after several generations, many of its single membership shares are held by trusts and LLCs, rather than by a single individual. In contrast, the NCA allows a fiduciary to hold shares, MCL 450.2445, and a director need not be a shareholder. MCL 450.2501.

  Though SB 129 amended Act 230 to allow a shareholder to designate a family member to act as a director ("a stockholder may nominate an immediate family member to exercise the stockholder's right to become a director"), *that actually introduced a new problem*: Because Act 230 still provides that "if a director ceases to own any stock of the corporation, the director ceases to be a director" it is unclear whether an immediate family director nominated by a stockholder to serve as a director satisfies the stock ownership requirement, or what happens if the stock devolves to someone other than the person who nominated the director to exercise that stockholder's right to become a director.

- Act 230 forbade the board to expend more than $1,000 without a vote of the shareholders. MCL 455.10. As a result of inflation, this limitation had become absurdly small, in effect requiring that shareholders approve even the most routine expenditures. This requirement was especially cumbersome, because, even in summer, a quorum of members is seldom available without significant advance notice. Typically, shareholders meet only once annually, and only a quorum was required to do business.

  Though SB 129 increased this amount to $30,000, it also introduced a new limitation that makes corporate governance unwieldy: It requires *that all expenditures by approved by* ***a majority of all the shares of stock*** *by the corporation* ***in a meeting duly assembled.***

  As noted, most summer associations, by their very nature, have difficulty even meeting the former quorum requirement. Now a Board that wishes to approve a significant expenditure for what should be routine road or waterfront preservation improvements must secure both the *attendance* and *support* of the owners of *a majority of all outstanding shares*.

  In addition, a vote by proxy is still not expressly permitted. Indeed, SB 129's apparent requirement of actual presence ("in a meeting duly assembled") appears to have been perpetuated.

- Act 230's cap on the number of shares poses a problem for Neahtawanta and other SRAs, as members bequeath their single share through the generations, or as lots held by the association are acquired and developed by new members.

  Senator Schmidt's bill did not address this problem, leaving the devolution of share ownership through generations a complicated and potentially conflict-producing process that requires the creation of a separate trust or corporation to hold the single share, often

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longer serves any purpose; the amendment merely increased the limitation by roughly the amount by which it increased with the cost of living in the 125 years since Act 230's enactment and pegged it to the cost of living going forward. It remains an arbitrary limitation that serves no apparent purpose.

requiring several separate decisions at the family trust or corporation level to determine how the single share allowed under Act 230 will be voted.

Under LARA's current interpretation of Act 230,[3] an association formed under Act 230 may not convert to non-profit form because Act 230 itself does not specifically authorize conversion. This is unsurprising, because there was no non-profit corporation act 126 years ago, when Act 230 was enacted.

HB 4312 and HB 4313, like each of their previous versions, are designed simply to allow an association formed under Act 230 whose members wish to convert to a non-profit form of corporate organization to do so.

These bills do **not** make conversion mandatory; an association formed under Act 230 may choose to remain organized under it. The bills would simply allow an association formed under the SRPA to convert to a modern non-profit corporation if its members wish to do so, and they include a provision protecting the rights of minority shareholders by requiring a super-majority of all shares to approve the conversion.

Approximately 45 Michigan SRAs continue to be organized under the SRPA.[4] Neahtawanta wrote to all of them describing this proposed legislation. None opposed the Bills, and five sent letters of support for them.

As noted above, after its review, Treasury and the State Tax Commission were satisfied that the Bills have no tax or revenue impacts on other associations, or on state or local taxing authorities.

Following this summary, for those on the Committee who may wish to review more detailed information, we have included an appendix containing a more detailed background account of why Neahtawanta has been obliged to seek legislative assistance to attain the modest goals of this legislation outlined above.

We thank you for this chance to be heard and are happy to answer any questions the committee may have.

Submitted respectfully,

Anne Treadway, President, Neahtawanta Summer Resort Association
and
Frederick M. Baker, Jr., Frederick M. Baker, Jr., PLLC (517) 318-6190

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[3] Several instances have been found in which LARA and its predecessor permitted SRAs to convert to non-profits, but, at some point, LARA's interpretation of Act 230 changed for reasons it eiher could not or would not explain..

[4] At least one Act 230 SRA, the Cascade Hills Country Club, was allowed to convert by merger into a nonprofit corporation in 1980, apparently before LARA adopted its current interpretation of Act 230.

APPENDIX
HISTORICAL BACKGROUND TO THE PROPOSED AMENDMENTS

To understand why Neahtawanta has come to the legislature for a solution to its problem, some recent history is required.

Neahtawanta began the process of addressing the problems described in the "Executive Summary" above by first exploring whether conversion to a modern corporate form was permitted under existing law.

Neahtawanta looked first to the conversion provisions of the Business Corporation Act ("BCA"), because, although Neahtawanta has always operated as a non-profit entity, the BCA, MCL 450.1123 says that it "applies" to summer resort associations, but that they "shall not be incorporated under this act":

> Unless otherwise provided in, or inconsistent with, the act under which a corporation is or has been formed, this act applies to deposit and security companies, summer resort associations, brine pipeline companies, telegraph companies, telephone companies, safety and collateral deposit companies, canal, river, and harbor improvement companies, cemetery, burial, and cremation associations, railroad, bridge, and tunnel companies, and agricultural and horticultural fair societies. The entities specified in this subsection shall not be incorporated under this act.

Neahtawanta inquired of LARA whether, because the BCA provides that it "applies" to SRAs, Neahtawanta could use the BCA's conversion provisions to convert to a non-profit corporation.

LARA's answer was no: LARA's position is that because Act 230 itself contains no provision expressly authorizing an association formed under it to convert to another form of corporation, Section 1123's exception to the application of the BCA to an association when it is "otherwise provided in, or inconsistent with" the SRPA was controlling.

Thus, since Act 230 itself does not expressly authorize conversion, LARA will not allow conversion unless Act 230 itself is amended to permit it. In other words, LARA deems the SRPA's silence on the question of whether conversion is allowed as the equivalent of being "otherwise provided," even though the BCA seems to say that it "applies" to summer resort associations.

LARA was unmoved when it was pointed out that its interpretation essentially nullifies Section 1123.

ALTERNATIVES TO CONVERSION ENTAIL GREAT RISK

Neatawanta also asked LARA whether it would recognize a merger of Neatahwanta's Act 230 corporation with a newly created non-profit corporation. LARA was unsure this could be permitted, again because a merger is not expressly permitted by the SRPA.

LARA told us that if we wanted to test whether a merger was possible, Neahtawanta would have to (1) prepare and submit to LARA a certificate of merger, new by-laws, and the documents

necessary to dissolve Neatawanta's existing Act 230 corporation, and (2) have Neahtawanta's shareholders approve all of these (all with the understanding that LARA might ultimately not approve the merger). Only then would LARA review the merger to determine whether it was permissible under existing law.

Neahtawanta also asked LARA if we could prepare the merger document package and submit them to LARA for prior review and approval, along with an outline of how we would proceed if LARA approved them, without actually conducting the shareholder vote that would be required to implement the merger. LARA said no, we had to go through the whole process, including securing shareholder approval of a dissolution of the existing SRPA corporation, before it would even review a merger plan. LARA did not suggest what Neahtawanta should do if LARA concluded that a merger was not permissible and Neahtawanta's shareholders had already voted to dissolve the corporation formed under the SRPA.

We explained that if such a merger were attempted, but then not approved by LARA, it might trigger drastic consequences for Neahtawanta and its members.

The problem with the approach LARA suggested is that the provisions authorizing a merger are all found in the BCA and the NCA.

Since LARA has already determined that, even though section 1123 provided that the BCA "applies to summer resort associations," Neahtawanta may not make use of the BCA's conversion procedure, we saw no reason to be optimistic that we could expect a different outcome if we tried to use the BCA's merger provisions.

Neahtawanta concluded that this alternative was too risky (for reasons explained within), because LARA could give no assurance that it would, or even might, reach a different result if a merger alternative was used.

LARA's position was daunting for two reasons: First, even if LARA ultimately decided to allow a merger, the dissolution of the (SRPA) corporation that had to precede it presented a great risk

Second, if the merger was not approved, or if Neahtawanta simply dissolved itself and formed a new nonprofit corporation without attempting a merger, the same risk was present.

This risk stems from what we believe is a provision unique to Act 230, one that Senator Schmidt's bill did not address or remedy: It is found at MCL 455.21, which prescribes the consequences of dissolving a corporation formed under the Act 230:

> In case such corporation should for any reason be disolved [sic – dissolved; it is misspelled in the code] or wound up by any court of competent jurisdiction, by reason of the termination of its charter or otherwise, each stockholder to whom a lot or lots have been assigned, allotted or confirmed, shall be entitled to receive the

same in fee[5] upon complying with such terms and conditions as may be imposed by the court having jurisdiction of the winding up of such corporation and **all parks, roads or walks** shown upon the plat of the property of such corporation recorded as aforesaid, **shall be and become dedicated to the public use as parks, roads and walks** in the same manner and to the same extent as parks, roads and drives are or may be so dedicated within the limits of cities, towns or villages in this state. (Emphasis added).

In short, if Neahtawanta were to dissolve and attempt to merge with, or simply form, a new, non-profit corporation, it would be exposed to a very real risk of losing ownership of all association-owned common areas.[6]

Indeed, because Neahtawanta's plat predates its incorporation under Act 230,[7] a number of "platted" (but non-existent) roads that criss-cross what is in fact a large, undeveloped forest subject to a conservation easement that Neahtawanta has granted to the public, would arguably be at risk of forfeiture.

In addition, structures located on commonly owned association land, such as the clubhouse, tennis courts, beach house, and, of course, the platted roads that actually do exist, and are in fact in use in the occupied portion of the association, would also arguably be at risk.

Thus, as a result of LARA's apparent change in its interpretation of Act 230, Neahtawanta finds itself in a situation not of its own making that creates a problem that Neahtawanta cannot solve by itself.

Neahtawanta submits that the law should be clear, and that anyone should be able to tell what the consequences of acting will be.

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5 Unlike many associations formed under the SRPA, which own all of the land in common, but not the members' cottages constructed on the lot assigned to each member, Neahtawanta's members already own both the land and their cottages.

6 Certainly, Neahtawanta has arguments for why a dissolution that is not part of a "winding up of such corporation," but merely part of a reorganization of the corporation in a different form, should not cause "the plat of the property of such corporation recorded as aforesaid, [to] be and become dedicated to the public use as parks, roads and walks," as MCL 455.21 provides. But Neahtawanta's directors, acting as fiduciaries, prudently concluded that they could not take that risk.

Neahtawanta submits that it, and the other associations formed under Act 230 that have indicated their support for the amendments, should not be obliged to risk litigation and an uncertain outcome, or, alternatively, the loss of all of their common areas, as the price of simply trying to modernize their corporate governance.

7 Neahtawanta's founders acquired the already-platted property after a predecessor association was liquidated in insolvency proceedings. Neahtawanata's predecessor was formed under a different summer resort association act that will be amended by the bills with which HB 4312 and HB 4313 are now tie-barred.

CONCLUSION

No simple solution to the problems posed by the antiquated (and now, with the enactment of SB 129, even more confusing) provisions of Act 230 is now available to Neahtawanta under existing law.

Neahtawanta seeks the amendments contained in HB 4312 and HB 4313 solely to make the law clear in a situation in which it is now both unclear and fraught with potential hazards.

It appears that the legislature tried to make the conversion procedures available under the BCA available to associations formed under Act 230 by providing that it "applies" to them unless "otherwise provided in, or inconsistent with, the act under which a corporation is or has been formed."

LARA's apparent change in its former interpretation of this law now requires that Act 230 itself must affirmatively provide that a particular BCA provision applies, however, before an association formed under Act 230 may invoke it. Otherwise, LARA will deem Act 230 to "provide otherwise" or be "inconsistent" with BCA §1123, leaving it to summer resort associations to guess what part of the BCA "applies" to them.

Neahtawanta seeks only the correction or clarification of Act 230 that LARA's current interpretation of the BCA requires. It is a clarification consistent with both §1123's language (providing that it "applies" to "summer resort associations") and with the apparent past practice of permitting at least one association organized under the SRPA to convert by merger to the non-profit form of corporate organization.

Treasury has thoroughly vetted these proposed amendments and found them unobjectionable. By enacting these amendments, the legislature will merely be permitting SRAs to become what Neahtawanta wishes to be: a modern, conveniently governable, non-profit corporation.

Most of Neahtawanta's common area land is subject to conservation easements. We have tried to preserve the quiet, rural character of these common lands for the benefit of all area residents (both members and non-members) and the environment. Under the current state of the law, however, Neahtawanta risks forfeiting all association-held common lands by using the only alternative even potentially available to it under LARA's interpretation, because it would first have to dissolve, potentially triggering their forfeiture under MCL 455.21.

Neahtawanta, and other SRAs that may be in the same position now or in the future, should not have to guess about the consequences of trying to remedy the practical governance problems posed by operating under Act 230, which Senator Schmidt's Bill, SB 129 did not cure, and, in some respects, actually aggravated. Under the current state of the law, no one, not LARA, not the half-dozen lawyers who have examined this problem, and not even this Committee, can tell Neahtawanta how to proceed without risking the destruction of an association of families and friends who have shared their little community for over a century.

Neahtawanta asks only that the legislature provide all associations organized under Act 230 a clear, reliable way to proceed in a manner that complies with LARA's current interpretation of Act 230.

Act No. 20
Public Acts of 2022
Approved by the Governor
March 10, 2022
Filed with the Secretary of State
March 10, 2022
EFFECTIVE DATE: Sine Die

STATE OF MICHIGAN
101ST LEGISLATURE
REGULAR SESSION OF 2022

Introduced by Senators Schmidt, Bumstead and Theis

ENROLLED SENATE BILL No. 129

AN ACT to amend 1897 PA 230, entitled "An act to provide for the formation of corporations for the purpose of owning, maintaining and improving lands and other property kept for the purposes of summer resorts or for ornament, recreation or amusement, and to repeal all laws or parts of laws in conflict herewith; and to impose certain duties on the department of commerce," by amending the title and sections 3, 9, 10, and 23 (MCL 455.3, 455.9, 455.10, and 455.23), the title and section 3 as amended by 1982 PA 117.

The People of the State of Michigan enact:

TITLE

An act to provide for the formation of corporations for the purpose of owning, maintaining, and improving lands and other property kept for the purposes of summer resorts or for ornament, recreation, or amusement; to provide for the powers and duties of certain state governmental officers and entities; and to repeal acts and parts of acts.

Sec. 3. (1) The articles of association must be filed with the department of licensing and regulatory affairs.

(2) All persons who subscribed the articles of association, stockholders of the corporation, and their successors shall be a body politic and corporate, by the name specified in the articles of association.

(3) The majority of the stockholders may direct the owning, holding, or purchasing and disposing of any real or personal property or estate. Real property must not exceed 700 acres of land. Personal property must not exceed $6,000,000.00, adjusted for inflation using the Consumer Price Index. As used in this subsection, "Consumer Price Index" means the most comprehensive index of consumer prices available for this state from the Bureau of Labor Statistics of the United States Department of Labor.

(4) The corporation may own, maintain, control, and operate a hotel, clubhouse, or other buildings for the entertainment, comfort, or convenience of its stockholders.

(5) The corporation may sue and be sued in all courts of law or equity in this state.

(6) The corporation may have a common seal and may alter and change the common seal.

(7) The corporation may alter or amend its articles of association at any regular meeting of the stockholders, or at any special meeting called for that purpose, by a vote of not less than 2/3 of all the shares of the capital stock of the corporation. Any amendment to the articles of association must be certified by the president and secretary of the corporation and filed and recorded in the same manner as the original articles of association. Any amendment to the articles of association that is filed and recorded becomes a part of the articles of association.

Sec. 9. (1) The board of directors shall consist of not less than 3 and not more than 9 members as determined by the articles of association. The members of the board of directors are stockholders. A stockholder may nominate an immediate family member to exercise the stockholder's right to become a director. A nomination under this subsection must be in writing. As used in this subsection, "immediate family member" means a stockholder's spouse, child, stepchild, or child's spouse.

(2) The full number of the board of directors must be elected at the first meeting of the corporation and must be divided into 3 equal classes. The first class shall hold their office for 1 year, the second class shall hold their office for 2 years, and the third class shall hold their office for 3 years. At each annual meeting after the first meeting, 1/3 of the total number of directors must be elected who shall hold their office for 3 years and until their successors are elected. At any election, a majority of the votes cast are sufficient to elect a director.

(3) If there is a vacancy in the board of directors, the remaining board of directors shall appoint an individual to fill the vacancy. The appointee must hold office until the next annual meeting, at which meeting the stockholders shall elect a director to fill the unexpired term.

(4) If a director ceases to own any stock of the corporation, the director ceases to be a director.

(5) A majority of the directors are a quorum for the transaction of business.

Sec. 10. (1) The board of directors of the corporation shall manage and control the stock, business, finances, rights and interests, buildings, and real and personal property of the corporation.

(2) The board of directors of the corporation has jurisdiction over the real property of the corporation and all streets, alleys, and highways passing through and over the real property of the corporation or which the corporation causes to be constructed, laid out, or maintained within that real property and over the water within and in front of that real property.

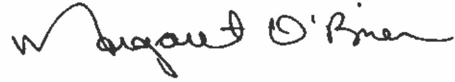
(3) The board of directors of the corporation shall not authorize any expenditure or incur any liability on behalf of the corporation that exceeds $30,000.00 annually, adjusted for inflation using the Consumer Price Index, unless authorized by a majority of all the shares of stock by the corporation in a meeting duly assembled. As used in this subsection, "Consumer Price Index" means the most comprehensive index of consumer prices available for this state from the Bureau of Labor Statistics of the United States Department of Labor.

Sec. 23. (1) The stockholders of the corporation, at a special meeting called for that purpose by a vote of a majority of all the capital stock, may authorize the board of directors to provide for special dues in addition to the annual dues authorized in section 16, not exceeding $750.00 per share in any 1 year, adjusted for inflation using the Consumer Price Index. As used in this subsection, "Consumer Price Index" means the most comprehensive index of consumer prices available for this state from the Bureau of Labor Statistics of the United States Department of Labor.

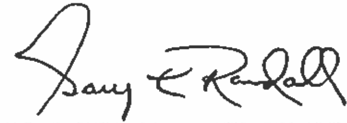
(2) The board of directors shall only use special dues assessed under this section for the purpose of paying any existing indebtedness of the corporation or for improving and bettering the property of the corporation, improving the sanitary condition of the property, providing protection from loss or damage by fire or water, or erecting, purchasing, or maintaining any hotel, clubhouse, or other building for the entertainment, comfort, or convenience of the corporation and its stockholders.

(3) Any resolution adopted by the stockholders authorizing special dues under this section must determine the purpose for which the board of directors shall use the proceeds of the special dues and the period of time in which the board may levy the special dues.

(4) The payment of special dues authorized under this section may be enforced by the corporation in the same manner provided in section 16 for the enforcement of the annual dues.



Secretary of the Senate



Clerk of the House of Representatives

Approved______________________________

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Governor