

## Advisory | Corporate



May 2019

### Sale of Corporate Assets in Nevada

From time to time corporate attorneys consider [Nevada Revised Statutes \(NRS\) 78.565](#) to determine its applicability to a sale of assets transaction where a significant portion of the assets of a corporation are being sold to a buyer. This GT Advisory introduces the Nevada statute, discusses its plain meaning, and reviews case law interpreting “all” and “substantially all” in the sale of assets statutes in various other jurisdictions including Delaware, California, Connecticut, and Illinois.

NRS 78.565(1) provides that:

Unless otherwise provided in the articles of incorporation, every corporation may, by action taken at any meeting of its board of directors, sell, lease or exchange all of its property and assets, including its goodwill and its corporate franchises, upon such terms and conditions as its board of directors may approve, when and as authorized by the affirmative vote of its stockholders holding stock in the corporation entitling them to exercise at least a majority of the voting power.

NRS 78.565(1) was enacted in 1925, and although amended occasionally, to this date the substance of the statute remains the same.<sup>1</sup> The meaning of NRS 78.565 has not been considered by a Nevada court. It was,

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<sup>1</sup> In 1925 the statute read, in pertinent part, “Every corporation may, by action taken at any meeting of its board of directors, sell, lease or exchange all of its property and assets, including its good will and its corporate franchises, upon such terms and conditions as its board of directors deem expedient and for the best interests of the corporation, when and as authorized by the affirmative vote of stockholders holding stock of the corporation entitling them to exercise at least a majority of the voting power given to stockholders ...” See Statutes of Nevada 1925, page 302.

however, described by a federal district court as being parallel to Delaware’s sale of assets statute,<sup>2</sup> notwithstanding the fact that Nevada’s statute, by its terms, governed the sale of all assets, and the Delaware statute, by its terms, governed the sale of all *or substantially all* of the assets of a corporation.<sup>3</sup>

In 2017 the Nevada Legislature amended Nevada’s corporate statutes to include a declaration that the plain meaning of enacted laws govern the internal affairs of a Nevada corporation and, importantly, the plain meaning of corporate statutes must be followed and not supplanted or modified by laws or judicial decisions from other jurisdictions.<sup>4</sup> The legislative history of the declaration anticipated that Delaware and other states laws would continue to be cited, discussed, and potentially used to interpret Nevada corporate law; however, where such laws were contrary to the applicable Nevada statute, the Nevada statute would control over the statutory or case law from the other state.<sup>5</sup>

### Plain Meaning of the Sale of Assets Statute

The plain meaning of NRS 78.565 is clear. The statute states that the board of directors has the authority to sell the assets of a corporation unless the sale, lease or exchange is of “*all of its property and assets, including its goodwill and its corporate franchises,*” (emphasis added) which, in such event, the sale, lease or exchange must also be approved by the affirmative vote of its stockholders holding at least a majority of the voting power of the corporation.

The operative word in the sale of assets statute is “all.” Common meanings of “all” include “the whole amount,” “every member or individual component,” and “wholly altogether.” If such meanings are applied in the application of NRS 78.565, stockholders would only vote on the sale of all assets if “every” asset of the corporation is sold. If the corporation withheld from the sale-of-assets transaction \$100, it would not be a sale of “all” assets of the corporation since a de minimis amount of cash was held back from the sale. Because of the retention of \$100 by the selling corporation, stockholders would not vote for or against the transaction since all property and assets of the corporation were not sold.

Moreover, the asset held back may simply be the corporate franchise. The corporate franchise is defined as the right to exist and do business as specified in its articles as a corporation. It is a grant by the sovereign power that is a “valuable right which is generally known as the corporate franchise.”<sup>6</sup> Many Nevada corporations are formed to conduct “all lawful businesses,” and if all assets other than the corporate franchise are sold, then the stockholders would not need to approve the transaction if the selling corporation continues to conduct business lawfully permitted in the state of Nevada.

In comparing NRS 78.565 to sale of assets statutes enacted in other jurisdictions, we note that other than in Nevada and the U.S. Virgin Islands,<sup>7</sup> no U.S. statute governing the sale of a corporation’s assets refers to “all” assets. The statutory language of 32 states and Puerto Rico reflects the “all or substantially all” standard.<sup>8</sup> Of the remaining U.S. states or possessions (including the District of Columbia), 16 statutes

<sup>2</sup> *Umbriac v. Kaiser*, 467 F. Supp. 548, 553 (D. Nev. 1979).

<sup>3</sup> 8 Del. C. § 271.

<sup>4</sup> NRS 78.012.

<sup>5</sup> Testimony of Lorne Malkiewich before the Assembly Committee on Judiciary held May 25, 2017.

<sup>6</sup> *Bank of America v. San Francisco*, 142 Cal. 276, 279, 75 Pac. 832 (1904) where the California Supreme Court determined that the corporate franchise was an asset of the corporation and subject to assessment by the city of San Francisco.

<sup>7</sup> 13 V.I.C. § 28, which provides in pertinent part that “Every corporation may ... sell, lease or exchange all of its property and assets, including its good will, upon such terms ... when authorized by the affirmative vote of the holders of a majority of stock issued and outstanding ...”.

<sup>8</sup> Maryland’s statute simply refers to “assets.”

contain language reflective of a bright line percentage similar to that present in the Revised Model Business Corporation Act (RMBCA).<sup>9</sup>

Enacted in 1925, NRS 78.565 remains substantively as written, so a review of similar statutes of other states and cases that were in effect at or about 1925 may be helpful in interpreting Nevada's sale of all assets statute.

### **“All” Means “All”**

In *Klopot v. Northrup*, 131 Conn. 14 (Conn. 1944), the court interpreted Connecticut's sale of assets statute, which at the time was similar to Nevada's current sale of assets statute. The Connecticut statute stated that in order to sell all of the corporation's property and assets, including its goodwill and franchise, on such terms as the board of directors deemed expedient, the sale needed to be approved by a two-thirds vote of the outstanding stock of each class of the corporation's stock, at a meeting held for the purpose of approving the sale of all assets.<sup>10</sup> In *Klopot*, a corporation sought to sell the assets of a newly created and financially struggling line of business to a wholly owned subsidiary while retaining its original line of business. A stockholder of the corporation sought to enjoin the transaction and demand dissenter's rights. The court upheld the plain meaning of the statute and did not require a stockholder vote because not “all” of the assets of the corporation were sold in the transaction.

In *Klopot*, the court refused to construe and held inapplicable cases that interpreted statutory language that referred to sales of corporate assets in terms such as: (i) “any interest therein or any part thereof” (New York); (ii) “entire property or any of the property of the corporation essential to the conduct of its corporate purposes” (Maine); or (iii) “all or substantially all” (Ohio).

When NRS 78.565 was enacted in 1925, Section 361a of the California Civil Code was similar to it in structure.<sup>11</sup> Section 361a provided that “no sale, lease, assignment, transfer or conveyance of the business, franchise and property, as a whole, of any corporation now existing or hereafter formed in the state, shall be valid without the consent of stockholders thereof, holding of record at least two-thirds of the issued capital stock of the corporation ....”<sup>12</sup> In *Shaw v. Hollister Land & Improv. Co.*, the court considered a sale of all properties of a corporation that conducted a horse racing business where two-thirds of the stockholders of the corporation did not consent to the sale of such properties. The court acknowledged the corporation's argument that the statute applied where the sale included the corporate franchise, but the court did not address this argument, noting that “if a corporation be engaged in business, such business must be included in the sale before such sale can be brought within either the terms or the meaning of the section upon which this action is based. In *Shaw*, the court held that the statute was not implicated because the operative sale document included only the real property, which the court construed as not including a sale of the business of the corporation. In defining “business,” the court held that “business” does not mean “stock or machinery or capital and the like ... but the activities in which they are

<sup>9</sup> §12.02(a) of the RMBCA reads as follows: “A sale, lease, exchange, or other disposition of assets, other than a disposition described in section 12.01, requires approval of the corporation's shareholders if the disposition would leave the corporation without a significant continuing business activity. If a corporation retains a business activity that represented at least 25% of total assets at the end of the most recently completed fiscal year, and 25% of either income from continuing operations before taxes or revenues from continuing operations for that fiscal year, in each case of the corporation and its subsidiaries on a consolidated basis, the corporation will conclusively be deemed to have retained a significant continuing business activity.”

<sup>10</sup> *Klopot*, 131 Conn. at 22, 37 A.2d 700, at 704, citing Conn. Gen. Stat. §3384.

<sup>11</sup> In 1931, California's sale of assets statute was amended to refer to a corporation's attempt to “sell, lease, convey, exchange, or transfer or otherwise dispose of all or substantially all of its property and assets.” *Seeburg v. El Royale Corp.*, 54 Cal. App. 2d 1, 3 (Cal. App. 1942). The current version of the statute is Cal. Corp. Code §1001.

<sup>12</sup> *Shaw v. Hollister Land & Improv. Co.*, 166 Cal. 257, 258 (Cal. 1913).

employed.” Since the corporation could lease racetracks, the corporation could conduct business and therefore the business of the corporation was not sold in connection with the sale of the racetrack.

### “All” Means “Substantially All”

In *Fisk v. Toys & Novelties Publishing Co.*,<sup>13</sup> the publishing house defendant sought to sell a magazine and a directory, including the goodwill and other assets essential to the future business of publishing each of them, leaving out only paper stock on hand and accounts or bills receivable. A minority stockholder brought a claim for dissenter’s rights. *Fisk* was a case of first impression in Illinois, and the court acknowledged that it intended to review New York cases that considered New York’s “somewhat similar” sale of assets statute. Although the Illinois statute applied to a sale of “all corporate assets,” and the New York statute applied to a sale of “all corporate assets or a part thereof,” the court nevertheless relied on the New York interpretations of the New York sale of asset statute set forth in *Matter of Timmis* and *In re Drosnes*.<sup>14</sup> The court cited with approval the holding in *Timmis* that a corporation “cannot sell all its property, or even a part thereof, so integral as to be essential for the transaction of its ordinary business, because such a sale is wholly or partly an act of self-destruction and a practical dissolution without compliance with law.” Ultimately, the court held that it was the intent of the legislature that the sale of assets statute should be applicable even though not all assets were sold in the transaction. Important to the court’s holding was the fact that the statute provided dissenter’s rights for stockholders objecting to a sale of all corporate assets to protect minority stockholders. If the word “all” were taken literally, it would be easy for corporations to circumvent the stockholder approval statute, which would cause the dissenter’s rights statute to have no meaning.

### Conclusion

We cannot predict the outcome of any conflict surrounding the interpretation of Nevada’s sale of assets statute. The declaration enacted in 2017 by the Nevada Legislature directs the application of the plain meaning of Nevada corporate statutes. The statute’s plain meaning is straightforward: “all” means “every”; and a sale that does not include all assets will not require the vote of stockholders. The plain meaning of Nevada’s sale of assets statute may erode approval rights by stockholders since the opportunity to approve asset sales by stockholder would be limited to the sale of “all” assets.

Application of the interpretation set forth in *Shaw v. Hollister Land & Improv. Co.* has some appeal. Although Nevada’s statute does not refer to the sale of “business” of the corporation, it does refer to goodwill of the corporation. Goodwill is the result of “the expectation of continued public patronage,”<sup>15</sup> arguably, the equivalent to business. If goodwill is retained by the corporation, then “business” would continue to be conducted with customers and other patrons. In that context, as long as the selling corporation is able to conduct business, a sale of all assets has not occurred, and the vote of stockholders would not be required in connection with the sales transaction.

It is also possible that a court would follow the reasoning of *Fisk v. Toys & Novelties Publishing Co.*, which held that “all” should not be taken literally, and the court interpreted “all” to mean “all or substantially all.” However, reading “substantially all” into the statute may defeat the purpose of the declaration to apply the plain meaning of the statute.

<sup>13</sup> 259 Ill. App 368 (Ill. App. 1930).

<sup>14</sup> *Matter of Timmis*, 200 N.Y. 177 (N.Y. App. 1910) (a printing company sold its calendar division) and *In re Drosnes*, 187 A.D. 425 (N.Y. App. 1919) (a theater company renovated its sole asset, a theater, into a theater and three stores and sold the property retaining only a ground lease).

<sup>15</sup> *Shaw v. Hollister Land & Improvement Co.*, 166 Cal. 257, at 260, 135 P. 965, at 966 (Cal. 1913).

Although we cannot predict the resolution of interpretation of the sale of assets statute, we can predict that the addition of Nevada's declaration to apply the plain meaning of Nevada corporate statutes may cause unintended consequences in the interpretation of the statutes.

In the meantime, if more certainty is desired, consider holding a stockholder vote to approve an asset sale if a significant amount of assets will be sold, even if sufficient assets remain after the sale for the corporation to conduct business.

Alternatively, the corporation can consider providing a framework in its articles of incorporation. Nevada corporate law permits a corporation to include in its articles of incorporation a provision that "is not contrary to the laws of the state for the management of business or the conduct of the affairs of the corporation."<sup>16</sup> A provision in the articles of incorporation, carefully drafted, quantifying the assets that may be sold only upon receiving stockholder approval may alleviate many of the questions encountered by the board to make sure that the corporation's asset sales are validly approved by all appropriate corporate constituencies. If such a provision is included in the articles of incorporation, the corporation will need to monitor decisions of the Nevada state courts and acts of the Nevada legislature in the event a change of law necessitates amendment of the provision.

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<sup>16</sup> NRS 78.037(1).