

# THE ALABAMA BUSINESS ENTITIES CONVERSION AND MERGER ACT: ISSUES SURROUNDING THE EFFECT OF CONVERSION

## I. INTRODUCTION

Legislation that permits a business organized in one form to merge with a business of another form, as well as legislation allowing a single business entity to convert its organizational structure without involving a second business entity, is a relatively recent development.<sup>1</sup> The Alabama Business Entities Conversion and Merger Act (the “Act”) was passed on March 21, 2000, as Act No. 00-211, with an effective date of October 1, 2000.<sup>2</sup> The Act sets forth the uniform procedures required for the merger of business entities or the conversion of one business entity into another type of entity.<sup>3</sup>

As with any new legislation aimed to address a specific issue, practitioners may run into unanticipated problems when using the statutory scheme. The legislation may not achieve the results sought, or it may not achieve them in the manner desired. While the Alabama conversion statute has only been in effect for a short time, its application has raised a number of issues for practitioners whose clients elect to convert a business entity under the Act.<sup>4</sup> This Comment is intended to address two of those issues. First, it will examine the effect that conversion from one entity form to another has on contractual agreements which specifically state that they cannot be transferred or assigned, by operation of law or otherwise.<sup>5</sup> Second, this Comment will examine an issue specific to the Alabama conversion statute—the requirement that a corporation must file articles of dissolution upon conversion and the effect of this filing on the converting entity.<sup>6</sup>

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1. Robert C. Art, *Conversion and Merger of Disparate Business Entities*, 76 WASH. L. REV. 349, 349 (2001) [hereinafter *Disparate Business Entities*] (examining the policies, principles, and drafting issues of cross-entity conversion and merger legislation).

2. Alabama Business Entities Conversion and Merger Act of Mar. 21, 2001, No. 2000-211 (codified at ALA. CODE §§ 10-15-1 to -7 (Supp. 2000) (effective date Oct. 1, 2000)).

3. *Id.*

4. *See supra* note 2.

5. These provisions are common in contractual agreements such as leases. This Comment will address the issue by using a hypothetical agreement which contains such a provision.

6. *See* ALA. CODE § 10-15-3(b)(3) (requiring the filing of a termination document); § 10-15-2(24) (including articles of dissolution in the definition of “termination document”).

## II. THE EMERGENCE OF CONVERSION STATUTES

The process of combining two business entities of different forms has always been possible, but prior to the emergence of conversion statutes such transactions were prohibitively complex and expensive.<sup>7</sup> For example, before the existence of merger statutes, a corporation could not combine with an existing limited liability company (LLC) due to the lack of statutory authority.<sup>8</sup> However, the corporation could reach the same result through the sale of the corporate assets to the LLC in exchange for membership interests and the subsequent dissolution of the corporation and issuance of the membership interests to the shareholders as a liquidating distribution.<sup>9</sup> This traditional process may be referred to as the “long form” route of changing from one business entity to another.<sup>10</sup>

States are increasingly recognizing the benefits of conversion and merger statutes which authorize the more efficient and direct option of conversion by a single step—involving only the converting entity and fewer documents.<sup>11</sup> In recent years, many states have enacted statutory “short cut” or “short form” approaches which allow the conversion of a business entity from one form to another with one or more simple filings with the relevant state authorities.<sup>12</sup> These are normally referred to as “conversion” statutes.<sup>13</sup>

Alabama’s conversion statute is relatively new. Therefore, the relevant provisions of the Act and other sections of the Alabama Code will first be examined to highlight areas where problems may arise.<sup>14</sup>

## III. THE ALABAMA BUSINESS ENTITIES CONVERSION AND MERGER ACT

The statutory contents of the Alabama Business Entities Conversion and Merger Act are significant, as is the Act’s relationship with other provisions of the Alabama Code that may be implicated by a decision to merge or convert a business entity under the Act. Understanding this organization will aid in the later discussion of the substantive problems and issues which may arise from conversion under the Act. An entity considering conversion

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7. *Disparate Business Entities*, *supra* note 1, at 350.

8. *Id.*

9. *Id.* at 352; *see also* GREGORY M. MARKS, UNDERSTANDING AND SELECTING THE BEST CONVERSION OR MERGER APPROACH FOR PASS-THROUGH ENTITIES 2 (2002) (providing an overview of the various approaches to statutory conversion and the consequences of such a transaction), at <http://www.gtlaw.com/pub/articles/2002/marksg02b.pdf>.

10. MARKS, *supra* note 9, at 1.

11. *See Disparate Business Entities*, *supra* note 1, at 350-51.

12. MARKS, *supra* note 9, at 2; *see, e.g.*, DEL. CODE ANN. tit. 8, § 266 (2001); IOWA CODE ANN. § 490A.304 (West 2001); OR. REV. STAT. § 70.515 (2001); N.C. GEN. STAT. § 55-11A-12 (2003); OKLA. STAT. ANN. tit. 18, § 2054.1 (West 1999).

13. *See supra* note 12.

14. Alabama’s statute is referred to as “short form” because it allows conversion through the filing of documents. However, Alabama’s system may require the filing of more than one document. *See generally* ALA. CODE § 10-15-3(b) (providing for the filing of termination and formation documents to effect a statutory conversion from one business entity form to another).

should be aware that the Act is not the exclusive method of changing an entity from one form to another; it merely provides an alternative method of conversion or merger into another type of business entity.<sup>15</sup> Accordingly, business entities “may be converted or merged in any other manner provided by law.”<sup>16</sup>

#### A. *The Conversion and Merger Act*

Several aspects of section 3 of the Act are important to understanding the Act’s operation and effects. Section 3 authorizes the conversion of business entities and provides the documentation and filing requirements.<sup>17</sup> Importantly, section 10-15-3(b)(3) of the Alabama Code requires the filing of a “termination document” by a converting entity “in the office in which such document is required by law to be filed.”<sup>18</sup> The Act defines a “termination document” as “[a]ny document, such as articles of dissolution in the case of a corporation, or certificate of cancellation in the case of a limited partnership, required by law to be filed publicly with respect to the end of a business entity’s existence.”<sup>19</sup>

Section 3 also provides the method by which a conversion takes effect.<sup>20</sup> A conversion takes effect when both the formation document and termination document are filed, if both are required to be filed.<sup>21</sup> If only a formation document or only a termination document must be filed, the conversion takes effect upon the filing of that document.<sup>22</sup>

Finally, section 3 of the Act provides the effects that conversion has on the converting and resulting entity.<sup>23</sup> The Act provides that “[a] limited partnership, general partnership, corporation, limited liability company, real estate investment trust, or other business entity that has been converted pursuant to this chapter is for all purposes the same business entity that existed before the conversion.”<sup>24</sup> Upon conversion, all of the property, rights, debts, and other business attributes of the converting business entity are treated as belonging to the resulting business entity.<sup>25</sup> Finally, the Act alleviates the necessity of a deed or other instrument of conveyance to effectuate this change.<sup>26</sup>

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15. § 10-15-5.

16. *Id.*

17. § 10-15-3.

18. § 10-15-3(b)(3).

19. § 10-15-2(24).

20. § 10-15-3(c)(1).

21. *Id.*

22. § 10-15-3(c)(2).

23. § 10-15-3(d)(1).

24. *Id.*

25. § 10-15-3(d)(2).

26. *Id.*

*B. Other Provisions of Title 10 of the Alabama Code*

In discussing the problems of the Act in regard to the conversion of a corporation to another business entity, it is beneficial to examine other relevant provisions of the Alabama Code. These provisions deal with dissolution of a corporation and the substantive effect of the filing of articles of dissolution.<sup>27</sup> First, section 14.03 deals with the filing of articles of dissolution.<sup>28</sup> At any time after dissolution is authorized, the corporation may dissolve by delivering articles of dissolution to the probate judge, including certain required information.<sup>29</sup>

Second, section 14.05 provides the effects of the dissolution.<sup>30</sup> “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, including” such things as collecting its assets and discharging its liabilities.<sup>31</sup>

With knowledge of the statutory background of the Alabama Business Entities Conversion and Merger Act in place, one can delve into two of the issues facing many practitioners who have begun to utilize the statute in order to convert business entities from one form to another.

IV. THE EFFECT OF CONVERSION ON A CONTRACTUAL  
AGREEMENT PREVENTING ASSIGNMENT

The Act raises questions about the effect of conversion on an agreement which expressly states that it may not be assigned. A hypothetical agreement that raises the issue of assignment upon merger helps to illustrate this point. For the purposes of this discussion, suppose the agreement stated, as many common contractual agreements do, that “the terms of this agreement may not be amended or altered, nor may the rights hereunder be assigned or otherwise transferred, without the written consent of [the other party].”<sup>32</sup> Such an agreement posits the issue of whether or not the conversion of a business entity is considered an “assignment,” thereby triggering the duty to obtain written consent before the conversion.

This issue also presents itself in the context of a merger. In a merger transaction, “[e]very other corporation party to the merger merges into the surviving corporation and the separate existence of every corporation except

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27. See generally § 10-2B-1.01 to 17.03 (1999) (encompassing the Alabama Business Corporation Act).

28. § 10-2B-14.03(a).

29. *Id.*

30. § 10-2B-14.05(a).

31. *Id.*

32. For an example of such an agreement in the context of a merger, see *Int'l Paper Co. v. Broadhead*, 662 So. 2d 277, 278 (Ala. Civ. App. 1995).

the surviving corporation ceases.”<sup>33</sup> The effect of such a merger on the corporation is that the

surviving corporation thereupon and thereafter possesses all the rights, immunities, and franchises, of a public as well as of a private nature, of every corporation party to the merger; and all property, real, personal and mixed, and all debts due each of the corporations so merged, are taken and deemed to be transferred and vested in the surviving corporation without further act or deed.<sup>34</sup>

Of course, it must be asked whether this provision of the Alabama Code gives a definitive answer to the assignment question.

In the context of a merger, the Alabama Court of Civil Appeals has held that a merger of two business corporations does not constitute an assignment.<sup>35</sup> In *International Paper Co. v. Broadhead*, the Hammermill Paper Company, a Pennsylvania Corporation (“Hammermill Penn”), qualified for an investment tax credit under Alabama law.<sup>36</sup> Hammermill Penn met all of the statutory requirements for receiving the credit, including the signing of a contract or memorandum of agreement with the State of Alabama, which read as follows: “The terms of this Agreement may not be amended or altered, nor may the rights of a TAXPAYER hereunder be assigned or otherwise transferred, without the written consent of the STATE.”<sup>37</sup> Shortly thereafter, Hammermill Penn merged into H.P. Subsidiary, Inc., a Delaware Corporation, and subsequently merged into International Paper Company.<sup>38</sup> International Paper sought to benefit from the investment tax credit, but its request was disallowed on the basis that the certificate was not issued to International Paper, and that Hammermill Penn assigned and transferred the credit to International Paper without the written consent of the State, as required by their agreement.<sup>39</sup> On appeal, the dispositive issue was “whether the right to the credit was ‘assigned or otherwise transferred’ when Hammermill Penn merged . . . and, if so, did the transfer violate . . . the memorandum agreement” between Hammermill Penn and the State.<sup>40</sup> The Alabama Court of Civil Appeals, citing the Alabama Supreme Court, stated that “while the constituent corporation may no longer survive for some purposes, the rights and privileges which it enjoyed under the statutes of Alabama survive the merger and inhere in the surviving corporation following merger.”<sup>41</sup> Additionally, the court noted that section 10-2B-11.06 of the

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33. § 10-2B-11.06(a)(1) (regarding the effect of merger or share exchange).

34. § 10-2B-11.06(a)(2).

35. *Int'l Paper*, 662 So. 2d at 278.

36. *Id.*

37. *Id.*

38. *Id.*

39. *Id.*

40. *Id.*

41. *Id.* at 279.

Alabama Code provided that “the surviving corporation of a merger is vested with all the ‘rights, privileges, immunities, and franchises’ of the constituent corporation.”<sup>42</sup> The court ultimately held, by applying statutory and case law to the facts, that the merger did not constitute a “transfer” or an “assignment.”<sup>43</sup> The court did not interpret the term “otherwise transfer” to include a merger or a transfer by operation of law, reasoning that the State “could have obtained the desired protection by inserting *express* language which would have included the merger transaction.”<sup>44</sup>

The critical issue is whether or not conversion would result in the same determination that contractual agreements are not “transferred” or “assigned” following the transaction. First, the statutory authority providing the effect of both merger and conversion on the rights and obligations of the entity should be examined to determine if there are any differences in the intent of the legislature as to what effect these transactions should have. The statutory authority which provides the effect of conversion from one business entity to another on the rights and liabilities of the entity states as follows:

All property, real, personal, and mixed owned by the converting business entity; all rights, immunities, and franchises of the converting business entity, of a public as well as a private nature; and all debts or obligations due the converting business entity, are taken and deemed to be transferred and vested in the resulting business entity without the necessity of any deed or other instrument of conveyance to the resulting business entity, without payment and without collection by any filing officer of any deed or other transfer tax or fee.<sup>45</sup>

As discussed in *International Paper*, the language of the statutory authority which provides the effect of a merger between two corporations on the rights and liabilities of the new corporation states as follows:

The surviving corporation thereupon and thereafter possesses all the rights, immunities, and franchises, of a public as well as of a private nature, of every corporation party to the merger; and all property, real, personal and mixed, and all debts due each of the corporations so merged, are taken and deemed to be transferred and vested in the surviving corporation without further act or deed; and title to any real estate, or an interest therein, vested in any of such corporations

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42. *Id.*

43. *Id.*

44. *Id.*

45. ALA. CODE § 10-15-3(d)(2) (providing the effects of conversion).

shall not revert nor in any way be impaired by reason of such merger . . . .<sup>46</sup>

In both the merger and conversion provisions, the “rights, immunities, and franchises” are “deemed to be transferred and vested in” the resulting business entity or surviving corporation.<sup>47</sup> Since there is no difference in the statutory language, there would need to be a difference in the substantive effect on an entity that has converted, because the effect of a merger on an entity was not significant enough for the Alabama Court of Civil Appeals to find that the merger constituted a “transfer” or an “assignment” of an agreement.<sup>48</sup>

Again, we can look to the statutory definition of a merger and conversion and the result on the converting or merging entity to determine if any substantive differences warrant a different determination in the context of a conversion than in the context of the merger in *International Paper*.<sup>49</sup> In a merger, “[e]very other corporation party to the merger merges into the surviving corporation and the separate existence of every corporation except the surviving corporation ceases.”<sup>50</sup> In a conversion, “[a] limited partnership, general partnership, corporation, limited liability company, real estate investment trust, or other business entity that has been converted pursuant to this chapter is for all purposes the same business entity that existed before the conversion.”<sup>51</sup> Therefore, after the conversion of a business entity, the resulting entity is “the same business entity” that it was before, just in a different form.<sup>52</sup> This is less drastic than the result of a merger, where the “separate existence” of each merging party “ceases,” and the result is a new business entity.<sup>53</sup>

The logical conclusion is that a conversion would not result in the transfer or assignment of a hypothetical contractual agreement which restricted this type of transfer or assignment, and thus would not result in a default or breach of that agreement. Any effect that a merger has on an entity was not significant enough to warrant the Alabama Court of Civil Appeals in finding that the merger constituted a transfer or an assignment of such an agreement.<sup>54</sup> Since the effect of conversion on an entity is less drastic than the effect of merger on an entity, it is logical to conclude that the effect of a conversion on an entity would also not be significant enough to support a finding that the conversion constituted a transfer or an assignment of the agreement.

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46. § 10-2B-11.06(a)(2) (providing the effects of merger).

47. *See supra* notes 33-34 and accompanying text.

48. *See supra* note 43 and accompanying text.

49. *See supra* notes 35-44 and accompanying text.

50. § 10-2B-11.06(a)(1) (regarding the effect of a merger or share exchange).

51. § 10-15-3(d)(1) (regarding the effect of a conversion on the converting business entity).

52. *Id.*

53. § 10-2B-11.06(a)(1).

54. *See supra* note 43 and accompanying text.

## V. ISSUES SURROUNDING THE FILING REQUIREMENTS IN THE CONTEXT OF A CONVERTING CORPORATION

It has already been established that an Alabama corporation which elects to convert into another form of business entity under the Alabama Business Entities Conversion and Merger Act is required to file a termination document, which the Act defines as articles of dissolution in the context of a corporate conversion.<sup>55</sup> This section will address the decision by the Alabama legislature to require the filing of articles of dissolution by analyzing the results of this decision and its impact on the converting corporation.<sup>56</sup>

There are two questions which will be addressed in this section. First, what effect does the filing of articles of dissolution have on the converting corporation, and is such an effect desirable? Second, did the Alabama legislature make the correct decision in requiring articles of dissolution to be filed, or is there a better method for converting a corporation to another entity form?

### A. *The Effect of the Filing of Articles of Dissolution on the Converting Corporation*

The main focus of this section is to determine what effect the requirement of filing articles of dissolution has on the converting corporation. The problem is best described with the following statement, which is likely to be made by a practitioner faced with this task: "I am not *dissolving* the corporation and ending its existence and business; I am only *converting* the business from the corporate form into another form which I find more desirable."<sup>57</sup> This apprehension about filing articles of dissolution comes from the substantive effects that such a filing may have on the business entity operating in the corporate form, and the appearance that such a filing may give to those who have an interest in the continuity of the converting business.

The Fletcher Cyclopaedia of the Law of Private Corporations states that "[u]nder many corporation statutes, a corporation voluntarily dissolved upon filing articles of dissolution . . . continues its corporate existence but may not carry on any business except that appropriate to wind up and liquidate its business and affairs."<sup>58</sup> The Alabama corporation statute adheres to

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55. See *supra* notes 17-19 and accompanying text.

56. The conversion of a corporation to a different entity form has significant tax consequences which are not addressed in this Comment. For a brief analysis of those consequences, see Nach Maravilla, *Converting from a Corporation to Sole Proprietorship*, available at <http://www.powerhomebiz.com/guide/cases/Corpconversion.htm>.

57. This statement is not a quotation from any particular source. It is merely a statement that a practitioner faced with the task of converting an Alabama corporation into another entity form is likely to make when, upon consulting the statute, she realizes that she must file articles of dissolution to accomplish her task.

58. 16A WILLIAM MEADE FLETCHER ET AL., FLETCHER CYCLOPEDIA OF THE LAW OF PRIVATE



this result.<sup>59</sup> Therefore, a practitioner contemplating the conversion of a client's corporation into another business entity may be wary of filing articles of dissolution due to the effects of section 14.05.<sup>60</sup> In order to determine whether such apprehension is warranted, the relationship between the Conversion Act and the dissolution provisions must be analyzed.<sup>61</sup>

A thorough analysis of the relationship between the conversion and dissolution provisions leads to the conclusion that a practitioner should not be apprehensive about the conversion of a corporation under the Alabama system. The most reasonable place to begin the analysis is to determine when the conversion of an entity takes place.<sup>62</sup> As noted in the statutory layout above, a conversion takes effect when both the formation document and termination document are filed, if both are required to be filed.<sup>63</sup> If only a formation document or only a termination document must be filed, the conversion takes effect upon the filing of that document.<sup>64</sup> The law of the new entity form—the limited partnership law and the statutes that govern this area—determines whether or not a formation document must be filed.<sup>65</sup> For the purposes of this discussion, we will assume that no formation document is required to be filed, and thus the termination document is the only required filing.<sup>66</sup>

Upon the filing of the termination document, does the question now become whether the law of the new entity form immediately begins to govern? If so, then the provisions of the Alabama Code applying specifically to corporations would no longer govern the entity once the articles of dissolution are filed for the purposes of conversion, and thus the business would not be constrained to performing only the functions of winding up and liquidation.

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CORPORATIONS § 8113 (perm. ed., rev. vol. 1995).

59. See ALA. CODE § 10-2B-14.02 (providing for voluntary dissolution upon approval by the board of directors); § 10-2B-14.03 (allowing a corporation to dissolve after filing articles of dissolution); § 10-2B-14.05 (noting that the "corporation continues [in] . . . existence but may not carry on any business except that appropriate to wind up and liquidate its business and affairs").

60. Under these circumstances, the corporation may only carry on the business affairs that are appropriate to winding up and liquidating the business, including collecting its assets, disposing of its properties, discharging its liabilities, and doing every other act necessary to wind up and liquidate its business and affairs. See § 10-2B-14.05(a).

61. Alabama's conversion statute is known as a "junction box" statute. *Disparate Business Entities*, *supra* note 1, at 381. In this type of statute, conversion provisions are located in a separate statute from the organic statute, such as the corporation act. *Id.* This approach is said to assure consistency and require fewer provisions than inserting cross-entity provisions into each organic statute. *Id.* Thus, we have to compare the relationship between the conversion statute, which exists on its own, and the corporation statute.

62. The moment when conversion becomes effective is particularly important, as it should govern which law to apply to a particular entity.

63. See *supra* note 21 and accompanying text.

64. See *supra* note 22 and accompanying text.

65. Such a law will of course be in another section of the Alabama Code, assuming the presence of filing requirements. The practitioner should consult the law of the new entity form to determine whether or not to file a formation document.

66. This would be the case where a corporation converts into a general partnership. However, conversion to an entity which requires a filing would also require filing a formation document. See § 10-15-3(b)(3).

tion.<sup>67</sup> While the Conversion Act does not specifically state this proposition, this has to be the desired outcome if the conversion of an entity is to be given the proper effect.<sup>68</sup>

However, there is a possible argument to the contrary based on the language of section 10-15-3(d)(1) of the Act, stating that the converted entity is “for all purposes the same business entity that existed before the conversion.”<sup>69</sup> It is easy to discern how this may confuse a practitioner; it seems that the new entity form, though now effective, may still be subject to some provisions of the law which applied to the converted entity form. Thus, the converted corporation may still be subject to the rules that applied after the filing of articles of dissolution, since those articles were indeed filed. However, the comments to this section state that the “principal purpose[ ] of using the conversion device is to change a business entity’s form of business organization without disturbing its ownership of property and without requiring a deed or other instrument of conveyance from the converting business entity to the converted business entity.”<sup>70</sup> Therefore, this “same business” provision was enacted to make the conversion process more efficient by circumventing the requirement that property be transferred; it likely does not mandate that any of the prior entity form’s law be applied.<sup>71</sup> Once the conversion takes effect, the law of the new entity form should trump the law of the prior entity form, and thus the fact that the articles of dissolution were filed should not mandate that the business be restricted to the section 10-2B-14.05 activities.<sup>72</sup>

There are other concerns regarding the Alabama system and its requirement of filing articles of dissolution as a termination document. One of the main concerns is the filing system in which the articles of dissolution (or “termination document” for these purposes) are located and indexed. Are these documents indexed in such a way that when one searches the files, the converting corporation is portrayed as having dissolved and thus ended its existence? This may have a number of implications, such as the triggering of default under certain notes.<sup>73</sup> The Act does require that the termination document include a statement that the converting entity was converted to another business entity, the name of the entity to which the converting entity

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67. See *supra* note 60.

68. The purpose of the conversion statutes is to allow an entity to forego the “long form” route of dissolving the converting entity and reforming as the new entity, which requires the transfer of assets. MARKS, *supra* note 9, at 1. Therefore, if the filing of articles of dissolution as a termination document does not “effect” the conversion and thus take the entity out of the realm of dissolution and into the law of the new entity form, the requirement of dissolution would remain.

69. § 10-15-3(d)(1) (providing the effects of conversion on the converted entity).

70. § 10-15-3, cmt. 7 (discussing the purposes of the conversion device and the intended consequences).

71. See *id.*

72. This result is not obvious, however, in the textual provisions of the statute. Therefore, Alabama could have circumvented most of this confusion by adopting a different method of conversion. For a discussion of this suggestion, see *infra* notes 95-99.

73. Parties may agree as to what events trigger a default, and this argument relies on the assumption that the filing of articles of dissolution frequently constitutes a default under such agreements.

was converted, and the office where the resulting business entity's formation document, if any, is filed.<sup>74</sup> However, since there is not a different filing system for articles of dissolution which are filed as termination documents, an inquiring person will search for articles of dissolution under the name of the entity. If these articles are present, and if one draws a conclusion from their presence without extensively reading the actual document, then confusion may occur.

### *B. An Analysis of Other Conversion Methods*

Notwithstanding the conclusion that the filing of articles of dissolution by a converting corporation does not detrimentally affect the transaction, a question remains: Did the Alabama legislature make the correct decision in requiring articles of dissolution to be filed, or is there a better method of allowing the conversion of a corporation to another entity form?

Even though the Alabama Business Entities Conversion and Merger Act requires that a converting corporation file articles of dissolution as a termination document, a lawyer involved in the conversion of a corporation for a client should not be concerned about the effects of dissolution.<sup>75</sup> However, an analysis of how other states have approached the entity conversion issue may be valuable in determining if the Alabama statute is the most efficient and effective method of allowing entity conversion.

Since Delaware is the corporate home to more than half of the country's corporations due to the flexibility offered in important corporate structural issues, an examination of their conversion provisions is a good place to start.<sup>76</sup> The Delaware Code specifically provides for the conversion of a domestic corporation to another entity by the adoption of a resolution approving conversion.<sup>77</sup> The critical difference, however, is in the subsequent filing requirements that Delaware mandates.<sup>78</sup> The Delaware conversion provision provides that "the corporation shall file with the Secretary of State a *certificate of conversion*" upon approval by the shareholders and the adoption of the resolution.<sup>79</sup> This "certificate of conversion" language is also used in California and Colorado.<sup>80</sup> The certificate must contain the name of the corporation, the date its original certificate of incorporation was filed, and the name of the business entity into which the corporation is being converted.<sup>81</sup> Additionally, the Delaware conversion provision states that the corporation shall "cease to exist as a corporation . . . at the time the certifi-

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74. See § 10-15-3(b)(3).

75. See *supra* notes 45-54 and accompanying text.

76. See John Reed & Frank Noyes, *Delaware Does It Best*, DIRECTORS & BOARDS 33-36 (Winter 2001), available at <http://www.bowne.com/newsletters/newsletter.asp?storyID=226>.

77. DEL. CODE ANN. tit. 8, § 266 (2001).

78. § 266(b) (2001) (requiring articles of conversion).

79. *Id.* (emphasis added).

80. See CAL. CORP. CODE § 1153 (West 1990) (using the "certificate of conversion"); COLO. REV. STAT. ANN. § 7-90-201 (West 1998).

81. See *supra* note 80.

cate of conversion becomes effective,” which in Delaware is the time of its filing.<sup>82</sup> Finally, the provision makes it clear that the conversion of the corporation does not result in the dissolution of the corporation by stating the following:

Unless otherwise provided in a resolution of conversion adopted in accordance with this section, the converting corporation shall not be required to wind up its affairs or pay its liabilities and distribute its assets, and the conversion shall not constitute a dissolution of such corporation and shall constitute a continuation of the existence of the converting corporation in the form of the applicable other entity of this State.<sup>83</sup>

Therefore, the Delaware provision does not require articles of dissolution to be filed by a converting corporation, and it expressly states that conversion does not result in the dissolution of the corporation.

Other states have used different language, but the effect is essentially the same as that of the Delaware provision—no articles of dissolution must be filed. Iowa and Oregon require “articles of conversion” to be filed upon the conversion of a corporation into another business entity.<sup>84</sup> North Carolina and Oklahoma use the “articles of conversion” language, and specifically state that the conversion of a corporation does not constitute dissolution of the converting corporation, and thus the corporation is not required to wind up and distribute its assets.<sup>85</sup>

Additionally, the National Conference of Commissioners on Uniform State Laws (NCCUSL) is drafting the Model Entity Transactions Act, which addresses entity conversion.<sup>86</sup> Section 505 of the Model Entity Transactions Act requires the filing of a statement of conversion.<sup>87</sup> The comments state that “[t]he filing of a statement of conversion makes the transaction a matter of public record. A separate public filing under the organic laws of the converting or surviving entity is not required.”<sup>88</sup> Furthermore, section 506(a) states that “[w]hen a conversion becomes effective . . . [t]he converted entity is deemed to . . . be organized under and subject to the organic law of the converted entity for all purposes; [and] be *the same entity without interruption or dissolution as the converting entity.*”<sup>89</sup> Finally, section 506(a)(6)

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82. DEL. CODE ANN. tit. 8, § 266(c) (2001).

83. § 266(f) (2001).

84. See IOWA CODE ANN. § 490A.304 (West 2001); OR. REV. STAT. § 70.515 (2001).

85. See N.C. GEN. STAT. § 55-11A-13 (2003); OKLA. STAT. ANN. tit. 18, § 2054.1 (West 1999).

86. NAT’L CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, MODEL ENTITY TRANSACTIONS ACT DRAFT, Feb. 2, 2004 [hereinafter ENTITY TRANSACTIONS ACT], available at <http://www.law.upenn.edu/bll/ulc/ueta/2004AnnMtgDraft.htm>. This statute has not been passed by the National Conference of Commissioners on Uniform State Laws, the American Bar Association, or the Drafting Committees acting for those organizations, it is merely a draft provided for discussion purposes.

87. ENTITY TRANSACTIONS ACT, *supra* note 86, at § 505.

88. *Id.* § 505(a).

89. *Id.* § 506(a)(1) (emphasis added).

specifically states that “[u]nless otherwise provided by the organic law of the converting entity, the conversion does not require the dissolution of the converting entity.”<sup>90</sup>

There are a number of benefits afforded by the “certificate” or “articles” of conversion approach that other states have taken. This approach provides the essential notice function and allows for efficient filings and effective tracking.<sup>91</sup> These states maintain a public record of every conversion and merger that occurs.<sup>92</sup> This allows creditors of businesses to track the disposition and location of assets and obligees.<sup>93</sup> Additionally, “[t]he procedure is as efficient and direct as possible, requiring only a single filing to report the exit of a business from one form of entity and the entrance to a new form.”<sup>94</sup>

In comparing the Alabama conversion provisions to those of other states, there are a number of significant differences. First, the Alabama statute does not require the filing of a separate certificate or articles of conversion, rather it provides for the notation of conversion on documents that would normally be filed when a new business entity is created or when an existing business entity is ending.<sup>95</sup> Second, the Alabama conversion provisions do not address the issue of dissolution and the effect of filing the required termination document (or articles of dissolution) on the converting entity.<sup>96</sup> We must now ask if the Alabama legislature made the correct decisions when they adopted this approach to entity conversion.

When analyzing the differences between the two approaches, it is easy to see that the clarity and brevity allowed by the “articles of conversion” method makes it the superior conversion statute. With the single filing of “articles of conversion,” there is a central location where only these articles are filed; an inquiring person can find out quickly and efficiently whether or not an entity has changed form just by searching for the entity name.<sup>97</sup> With the Alabama approach, the indication of conversion is placed on the articles of dissolution and filed with the other articles of dissolution from other corporations—a simple name search will not reveal whether the entity has actually been dissolved or whether it was merely converted to another entity form without the effects of dissolution. “Administrative procedures must allow the state to record and report on the current status of a business, without undue expense or complexity,” and the articles of conversion approach is obviously the best method of accomplishing this goal.<sup>98</sup> Additionally, with the Alabama approach, the effect of filing articles of dissolution when

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90. *Id.* § 506(a)(6).

91. *Disparate Business Entities*, *supra* note 1, at 387.

92. *Id.*

93. *Id.*

94. *Id.*

95. ALA. CODE § 10-15-3(b) (1975).

96. *See generally* § 10-15-3(d) (providing the effects of conversion, but not mentioning dissolution).

97. This argument assumes that there is some type of search method by which an inquiring party can determine whether or not a particular person has made a filing. This may be an electronic search, or it may simply require placing a call to the Secretary of State’s office.

98. *Disparate Business Entities*, *supra* note 1, at 353.

converting a corporate entity into another form is unclear. Alabama should consider following the approach of those states and NCCUSL. These conversion statutes clearly state that the conversion of a corporate entity does not result in the dissolution of the converting corporation and thus does not require it to wind up its business. These two minor differences in the construction of the statute would alleviate the concerns regarding the filing of articles of dissolution upon the conversion of an Alabama corporation into another entity form.

## VI. CONCLUSION

With the variety of business entities available to businesses and investors, the emergence of conversion statutes is a step forward in the process of allowing efficient transition from one entity form to another. However, in promoting such transition, there will undoubtedly be numerous issues and challenges to be addressed along the way. This Comment addresses only two issues particular to the Alabama statute—others may arise.

Although the Alabama Business Entities Merger and Conversion Act may have some flaws in the way it is drafted, it is commendable that the issue of entity conversion has been addressed in Alabama, and in such an expedient fashion. The option to convert from one entity form to another provides numerous advantages for those who opt to take advantage of the statute, and although the Act may need some reformation in order to operate flawlessly, the existence of the conversion act is important to the progression of business law in Alabama. As Alabama law continues to develop in this area, the legislature should consider improving the law's operation to ensure that Alabama provides the most efficient and effective method of entity conversion.

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