Gerald T. Noel, Jr. *Legislative Service Commission*

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123rd General Assembly
(As Reported by S. Judiciary)

Reps. Womer Benjamin, Callender, Mottley, Ford, Buchy, Willamowski, Salerno, Grendell

BILL SUMMARY

- Eliminates the requirement that the articles of incorporation ("articles") of an Ohio corporation for profit ("corporation") must set forth the purposes for which the corporation is formed but permits articles to include those purposes as well as the names of the individuals who are to serve as the corporation's initial directors.

- Modifies the General Corporation (GC) Law's provisions pertaining to the permissible adoption of amendments to a corporation's articles by its incorporators, directors, or shareholders.

- Permits the express terms of a corporation's shares to include a statement of the directors' right, subject to any stated limitations, to adopt amendments to the corporation's articles that determine the express terms of any class of shares before their issuance or the express terms of one or more series within a class before their issuance.

- Requires that each series of a class of shares be given a distinguishing designation and that all shares of a series have express terms identical with those of other shares of the same series.

- Subject to certain limitations, permits any of the express terms of any class or series of shares to be made dependent upon facts ascertainable outside a corporation's articles or an amendment to the articles.

- Permits incorporators to receive subscriptions for shares after a corporation's articles are filed with the Secretary of State, and prohibits incorporators from receiving subscriptions if the articles name the initial directors or after the meeting of the shareholders or incorporators at which the initial election of directors occurs.

- Specifies that the shareholders of certain corporations do not have a pre-emptive right to acquire the corporation's unissued shares except to the extent that the corporation's articles provide that right.

- Entitles the holders of fractional shares to exercise the rights of a shareholder, including the right to vote, to receive dividends, and to participate in the assets of the corporation upon liquidation.

- Modifies the GC Law's organizational meeting provisions to reflect instances in which initial directors are named in the articles and instances in which they are not so named, to permit organizational meetings to be held in or outside of Ohio, and to permit incorporators to take "organizational meeting action" without a meeting if the action is evidenced by specified written consents.

- Modifies the GC Law's general regulation provisions to reflect the ability of initial directors named in a corporation's articles or elected by the incorporators to generally adopt regulations within 90 days after the corporation is formed.

- Requires a corporation to pay expenses "as they are incurred" by a director in defending certain types of actions, suits, or proceedings if the corporation receives a specified undertaking and unless the corporation's articles or regulations declare in a specified manner that the payment requirement does not apply.

- Generally grants an immunity from personal liability to a shareholder or subscriber to a corporation's shares for any debts, obligations, or liabilities of the corporation in the absence of a written, enforceable agreement that is signed by the shareholder or subscriber and specifically undertakes liability for the debts, obligations, or liabilities.

- Specifies that subscribers for or purchasers of a corporation's shares must pay or deliver the requisite consideration for the shares but are not liable to the corporation or its creditors in any other amount.

- Places a corporation's indebtedness to a shareholder incurred by reason of a dividend or distribution "at parity with" the corporation's indebtedness to its general, unsecured creditors, except to the extent subordinated by agreement.

- Specifies dates for the measurement of the "effect" of a dividend or distribution, and provides that the "record date" for determining shareholders entitled to a dividend or distribution is the date the directors authorize the dividend or distribution if they otherwise fail to fix the record date for that purpose.

TABLE OF CONTENTS

Articles of incorporation provisions 4
Formation of a corporation 4
Amendments to articles by the incorporators or directors 5
Amendments to articles by the shareholders 6
Shares provisions 7
Express terms of shares 7
Subscriptions for shares 8
Pre-emptive right to purchase shares 9
Fractional shares 9
Organizational meetings 10
Existing law 10
Changes proposed by the bill 10
Regulations adoption and amendment: in general 12
Existing law 12
Changes proposed by the bill 12
Directors performance of duties and associated liabilities 12
Background: standard of care 12
Impermissible loans, dividends, distributions, etc. 13
Shareholders and subscriber liabilities 14
Background 14
Existing liabilities 14
Changes proposed by the bill 15
Dividends and distributions 15
Background 15
Changes proposed by the bill 15

CONTENT AND OPERATION

Articles of incorporation provisions

Formation of a corporation

Background. Under existing law (continued by the bill), an Ohio corporation *for profit* (hereafter, "corporation") may be formed under the General

Corporation (GC) Law for any purpose or combination of purposes for which individuals lawfully may associate themselves or for the purpose of carrying on any profession. One or more persons may form a corporation generally by filing a written appointment of a statutory agent and signed *articles of incorporation* (hereafter, "articles") with the Secretary of State (see **COMMENT** 1). The legal existence of the corporation begins upon the filing of the articles, and, unless the articles otherwise provide, the corporation's period of existence is perpetual. The articles must set forth certain specified items and may set forth other specified items (see below). (Sec. 1701.04; sec. 1701.03--not in the bill.)

Mandatory items. Similar to existing law, the bill requires that a corporation's articles set forth the following items: the name of the corporation; the place in Ohio where the corporation's principal office is to be located; the authorized number and the par value per share of shares with par value; the authorized number of shares without par value; the express terms (if any) of the shares; if the shares are classified, the designation of each class, the authorized number and par value per share (if any) of the shares of each class, and the express terms of the shares of each class; and, if applicable, the amount of the corporation's initial stated capital (sec. 1701.04(A)(1) to (4)). The bill also converts one of existing law's mandatory items into a permissive item (see (2) under "***Permissive items***" below).

Permissive items. The bill continues to permit the inclusion of certain items in a corporation's articles. The types of items that the bill permits incorporators to include in a corporation's articles are as follows (sec. 1701.04(B) and (C)):

(1) The names of the individuals who are to serve as *initial directors* of the corporation (added by the bill);

(2) The *purpose* or purposes for which the corporation is formed. In the absence of a statement of this nature and except as expressly set forth in a statement of this nature, the purpose for which a corporation is formed is "to engage in any lawful act or activity for which a corporation may be formed" under the GC Law, and all lawful acts and activities of the corporation are within the purposes of the corporation. (Added by the bill.)

This permissive item generally is similar to existing law's *mandatory requirement* that a corporation's articles set forth the purpose or purposes for which the corporation is formed. That requirement may be satisfied by a statement that the corporation's purpose, either alone or with other specified purposes, is to engage in any lawful act or activity for which corporations may be formed under the GC Law, and that statement has the effect of including within the corporation's purposes all lawful corporate acts and activities that conform to the conditions and

limitations (if any) specified in the corporation's articles (existing sec. 1701.04(A)(3)--repealed by the bill).

(3) Similar to existing law, (a) any lawful provision for the purpose of defining, limiting, or regulating the exercise of the authority of the corporation, the incorporators, the directors, the officers, the shareholders, or the holders of any class of shares, (b) any provision that may be set forth in the corporation's regulations, (c) a provision specifying the period of the corporation's existence if it is not perpetual, or (d) any additional provision permitted by the GC Law.

Related provisions. The bill continues a prohibition against the articles of a *banking, safe deposit, trust, or insurance* corporation authorizing shares without par value (sec. 1701.04(A)(3)). To reflect the bill's "***Mandatory items***" and "***Permissive items***," the bill also modifies cross-references in the "articles of incorporation" or "certificates of reorganization" provisions of two statutes *outside of the GC Law* that pertain to federal savings and loan associations that have a home office in Ohio and decide to convert or reorganize in a specified manner into an Ohio savings and loan association (see **COMMENT** 2) or to the reorganization of an Ohio savings and loan association in a specified manner (secs. 1151.38(D)(1) and 1151.61(D)(1).)

Amendments to articles by the incorporators or directors

Existing law. Under the existing GC Law, if an initial stated capital is set forth in a corporation's articles, the *incorporators* may adopt a written, signed amendment to the corporation's articles before subscriptions to shares are received "in the amount of that initial stated capital." If an initial stated capital is not set forth in the articles, the incorporators may adopt a written signed amendment to the corporation's articles before "the corporation begins business." The *directors* of a corporation are authorized to adopt an amendment to the corporation's articles in specified cases, one of which is as follows: when and to the extent that the articles authorize the directors to adopt an amendment with respect to any unissued or treasury shares of any class. (Sec. 1701.70(A) and (B)(1).)

Changes proposed by the bill. The bill modifies the latter provisions as follows (secs. 1701.70(A), (B)(1), and (C) and 1701.71(B)(4)):

(1) The bill replaces the *incorporators*-related provisions with two new provisions. First, if initial directors are *not named* in the articles, the incorporators may adopt written, signed amendments to the articles before subscriptions to shares have been received *and before the incorporators have elected directors*. The bill deletes the reference in existing law to "before the corporation begins business." Second, if initial directors *are named* in the articles or if the incorporators have elected directors and have not received subscriptions, the

directors may adopt amendments to the articles before subscriptions to shares have been received.

(2) The bill replaces existing law's *directors* amendment authority relative to *unissued or treasury shares of any class* with the following amendment authority: they may adopt an amendment to the articles when and to the extent that the articles authorize the directors to adopt an amendment determining, in whole or in part and within the limits set forth in the GC Law, *the express terms of any class of shares* before the issuance of any shares of that class or the express terms of *one or more series within a class* before the issuance of any shares of that series.

(3) The bill adds a new provision pertaining to *any type* of directors' amendment to a corporation's articles in accordance with continuing law (see **COMMENT** 3) or the bill's new amendment authority described in (2), above. Specifically, if a directors' amendment creates a *class or series of shares* the express terms of which provide for the *convertibility of the shares into shares of another class*, and if the GC Law requires a *shareholders' vote* on the adoption of that amendment because the amendment changes "the express terms of issued shares of any class senior to the particular class in any manner substantially prejudicial to the holders of shares of the particular class," the bill requires that the directors' amendment also be approved by the holders, voting as a class, of any issued and outstanding shares into which the shares may be converted.

Amendments to articles by the shareholders

Existing law. At a meeting held for the purpose, the shareholders of a corporation may adopt an amendment to the corporation's articles, including an amendment that the directors may adopt. The adoption of a shareholders' amendment *generally* requires (1) the affirmative vote of shareholders entitled to exercise two-thirds of the corporation's voting power on the proposal or, if the articles provide or permit, the affirmative vote of a greater or lesser proportion, but not less than a majority, of that voting power and (2) the affirmative vote of any particular class of shareholders that the articles require. (Sec. 1701.71(A)(1).)

The existing GC Law provides that, regardless of limitations or restrictions in a corporation's articles on the voting rights of the shares of any class, the holders of *shares of a particular class* and, in certain cases, the holders of shares of every class are entitled *to vote as a class* on the adoption of certain types of amendments to the articles (see **COMMENT** 4). One of those types of amendments is as follows: an amendment that authorizes shares of another class that are convertible into shares of the particular class, authorizes the conversion of shares of another class into shares of the particular class, or authorizes the directors to fix or alter conversion rights of shares of another class that are

convertible into shares of the particular class (hereafter, "a conversion shares amendment"). (Sec. 1701.71(A)(2) and (B).)

Changes proposed by the bill. Under the bill, if a *conversion shares amendment* is involved, the holders of the class of shares into which other shares may be converted *generally continue* to be entitled to vote as a class on the adoption of the amendment. However, the bill qualifies these voting provisions in two respects. First, the failure to obtain the shareholders' approval only prevents the conversion of the shares until the approval is obtained and otherwise does not affect the authorization or any other express terms of the shares. Second, the corporation's articles may provide that no vote of the holders of common shares, as a class, is required in connection with the authorization of shares of any class that are convertible into common shares. (Sec. 1701.71(B)(5).)

Shares provisions

Express terms of shares

Permissive statements. The existing GC Law *permits* the express terms of a corporation's shares to include certain types of statements. The bill continues most of those types of statements (see **COMMENT** 5) but modifies the nature of one of them. (Sec. 1701.06(A).)

Specifically, under existing law, the express terms of a corporation's shares may include a statement of the right of the directors, subject to any stated limitations, to adopt amendments to the corporation's articles *in respect of any unissued or treasury shares of any class* (see **COMMENT** 6) and, as a result of those amendments, to fix or change the following: (1) the division of the unissued or treasury shares into series and the designation and authorized number of shares of each series, (2) the dividend or distribution rate, (3) the dates of payment of dividends or distributions and the dates from which they are cumulative, (4) liquidation price, (5) redemption rights and price, (6) sinking fund requirements, (7) conversion rights, and (8) restrictions on the issuance of shares of any class or series. The bill repeals these provisions and instead authorizes the express terms of a corporation's shares to include a statement specifying the following: the right of the directors, subject to any stated limitations, to adopt amendments to the corporation's articles that determine, in whole or in part and within the limits set forth in the GC Law, the express terms *of any class of shares* before the issuance of any shares of that class or the express terms of *one or more series within a class* before the issuance of any shares of that series. (Sec. 1701.06(A)(12).)

Series of a class of shares. The existing GC Law generally requires the express terms of shares of *different* series of any particular class of shares to be

identical. However, under existing law, there may be variations with respect to items similar to those listed in (2) through (8) above. (Sec. 1701.06(B).)

The bill repeals the latter provisions and substitutes the following requirements (sec. 1701.06(B)):

(1) Each series of a class of shares (hereafter, "series") must be given a distinguishing designation.

(2) All shares of a series must have express terms identical with those of other shares of the *same series*.

(3) Any of the express terms of any class or series of shares *generally* may be made dependent upon facts ascertainable outside the corporation's articles or any amendment to the articles. However, the manner in which the facts operate upon the express terms must be set forth in the articles or an amendment to them.

Subscriptions for shares

The existing GC Law contains several provisions pertaining to incorporators and subscriptions for shares. The bill continues most of these provisions (see **COMMENT** 7) but modifies two of them as follows (sec. 1701.09(A) and (C)):

(1) Existing law provides that, after a corporation's articles are filed with the Secretary of State, the incorporators or a majority of them *must* receive subscriptions for shares at the time and place that they determine. The bill instead *permits* the incorporators or a majority of them to receive those subscriptions.

(2) Existing law prohibits incorporators from receiving subscriptions for shares after the election of directors. The bill instead provides that incorporators are prohibited from receiving subscriptions for shares (a) if the articles of incorporation name the initial directors or (b) after the meeting of the shareholders or incorporators at which the initial election of directors occurs.

Pre-emptive right to purchase shares

Existing law. Under the existing GC Law, the holders of shares of any class (other than shares that are limited as to dividend and distribution rate and liquidation price) *generally* have a statutory right to purchase shares of the same class that are offered or sold for cash. A purchase is authorized during a reasonable time and on reasonable terms fixed by the corporation's directors, in proportion to the respective holdings of shares of the same class, and at a price fixed in accordance with the GC Law. This *pre-emptive right* does not extend *to*

treasury shares, to shares issued as a share dividend or distribution, and to certain other types of shares. (Sec. 1701.15(A).)

Changes proposed by the bill. The bill modifies existing law's *pre-emptive right* provisions in two respects. First, it specifies that the shareholders of a corporation do not have a pre-emptive right to acquire the corporation's unissued shares *except to the extent that the corporation's articles provide that right*. Under the bill, if articles provide a pre-emptive right to the holders of shares of any class (other than shares that are limited as to dividend and distribution rate and liquidation price), existing law's pre-emptive right provisions apply to the shareholders. (Sec. 1701.15(A).)

Second, the bill provides that the statutory *pre-emptive right* provisions that existed prior to the effective date of the bill's modification of those provisions continue to apply to any corporation incorporated prior to that effective date, until the shareholders adopt an amendment to the articles expressly providing that the bill's pre-emptive right provisions taking effect on that date apply to the corporation or amended articles. (Sec. 1701.15(C).)

Fractional shares

Existing law. The existing GC Law provides that a corporation is not required to issue, but may issue, fractional shares. A corporation that issues fractional shares in connection with *certificated securities* may execute and deliver a certificate for or including a fractional share, or it may (1) pay cash to the person entitled to become a holder of the fractional share, (2) provide reasonable means to afford the person the opportunity, on specified terms and conditions, to purchase or sell fractional interests in shares to the exclusion of all other rights the person otherwise may have, or (3) execute and deliver registered or bearer scrip that is in a specified form and exchangeable for full shares. A corporation that issues fractional shares in connection with *uncertificated securities* has options (1) and (2), above. (Sec. 1701.24(C).)

Changes proposed by the bill. The bill continues the latter fractional shares provisions and additionally specifies that the holder of a fractional share is entitled to exercise the rights of a shareholder, including the right to vote, to receive dividends, and to participate in the assets of the corporation upon liquidation (sec. 1701.24(C)).

Organizational meetings

Existing law

The existing GC Law provides that, after subscriptions for shares have been received in cases in which an initial stated capital is not set forth in a corporation's articles *or* after subscriptions for shares have been received in an amount that "the stated capital of those shares is at least equal to the initial stated capital set forth in the articles," the incorporators or a majority of the incorporators generally must give at least ten days' notice by mail to the shareholders (unless the shareholders waive the notice) to meet at a specified time and place for the purpose of adopting regulations, electing directors, and transacting other business. The shareholders then must meet for those purposes at the time and place specified. (*Existing* sec. 1701.10.)

Changes proposed by the bill

The bill outright repeals the latter provisions of the GC Law (Section 2's repeal of existing sec. 1701.10) and substitutes the following "organizational meeting" provisions:

When initial directors named. If the initial directors *are named* in a corporation's articles, then, after incorporation, the initial directors must hold an organizational meeting, at the call of a majority of the directors, to complete the organization of the corporation by receiving subscriptions of shares, appointing officers, *adopting regulations*, and carrying on other business brought before the meeting. The regulation adoption authority appears to be qualified by the "***Exception and limitation***" described below. (New sec. 1701.10(A)(1).)

When initial directors not named. If initial directors *are not named* in a corporation's articles, then, after incorporation, the incorporator or incorporators must either (1) receive subscriptions of shares as described under "***Subscriptions for shares***," above, or (2) hold an organizational meeting at the call of a majority of the incorporators to elect directors. Those directors then must complete the organization of the corporation as described under "***When initial directors named***," above. The directors' regulation adoption authority appears to be qualified by the "***Exception and limitation***" described below. (New sec. 1701.10(A)(2).)

If subscriptions for shares are received by the incorporators, the incorporators or a majority of the incorporators must give at least *seven days'* written notice to the shareholders (unless the shareholders waive the notice) to meet at a specified time and place for the purposes of *adopting regulations*, electing directors, and transacting other business. The shareholders then must

meet for those purposes at the time and place specified. (New sec. 1701.10(A)(2).)

Exception and limitation. Notwithstanding the bill's "***When initial directors named***" provisions and its "***When initial directors not named***" provisions, if directors do not adopt regulations for a corporation within 90 days after the corporation's formation, only the shareholders may adopt the regulations. The shareholders must adopt the regulations in one of the following ways (new sec. 1701.10(A)(3)):

(1) *At a meeting* of the shareholders that the *directors call* for that purpose or, if directors are not named in the corporation's articles or have not been elected, at a *meeting* of the shareholders that at least a *majority of the incorporators* call for that purpose. The directors or incorporators must give not less than seven days' written notice to the shareholders (unless the shareholders waive the notice) to meet at a specified time and place for the purposes of adopting regulations and transacting other business.

(2) *Without a meeting* of the shareholders, by the written consent of the shareholders entitled to exercise two-thirds of the voting power on the proposal.

The bill also prohibits directors from taking any action to adopt or amend regulations after the shareholders have adopted regulations (sec. 1701.10(A)(4)).

Incorporators and organizational meetings. Under the bill, action that the GC Law requires or permits incorporators to take at an organizational meeting may be taken *without a meeting* if the action is evidenced by one or more written consents that describe the action and are signed by each incorporator (sec. 1701.10(B)).

Location of an organizational meeting. The bill permits an organizational meeting to be held in or outside of Ohio (sec. 1701.10(C)).

Regulations adoption and amendment: in general

Existing law

The existing GC Law's *general* regulations-related provisions authorize a corporation's *shareholders* to adopt and amend regulations for the government of the corporation, the conduct of its affairs, and the management of its property. This action must be undertaken consistent with Ohio law and the corporation's articles (see **COMMENT** 8). (Sec. 1701.11(A).)

Shareholders may *adopt* regulations of that nature (1) *at a meeting* held for that purpose and by the affirmative vote of the shareholders entitled to exercise a

majority of the voting power of the corporation on the proposal or (2) *without a meeting* and by the written consent of the shareholders entitled to exercise two-thirds of that voting power. Shareholders may *amend* existing regulations, or repeal existing regulations and adopt new regulations, in the same manners as described in (1) or (2), above, or, if the corporation's articles or regulations so provide or permit, by the affirmative vote or written consent of the shareholders entitled to exercise "a greater or lesser proportion but not less than a majority of" the corporation's voting power. (Sec. 1701.11(A).)

Changes proposed by the bill

The bill restructures the form of, but generally continues, the authority of shareholders to adopt and amend regulations in the manners described under "***Existing law***," above. The bill also specifies in the general regulations-related provisions that *initial directors* named in a corporation's articles or elected by the incorporators may adopt regulations within 90 days after the corporation is formed, as described under "***Organizational meetings***," above. (Sec. 1701.11(A)(1) and (2).)

Directors performance of duties and associated liabilities

Background: standard of care

The existing GC Law (continued by the bill) requires all authority of a corporation to be exercised by or under the direction of its directors except as "the law" or the articles or regulations require action to be authorized or taken by the shareholders. A director must perform the director's duties (including duties as a member of a committee) in good faith, in a manner the director reasonably believes to be in or not opposed to the best interests of the corporation, and with the care that an ordinarily prudent person in a like position would use under similar circumstances (hereafter, "the standard of care"). Other GC Law provisions relate to a director's fulfillment or *breach* of the standard of care, including a provision authorizing a finding that a director breached the standard of care only if the breach is established "by clear and convincing evidence" *in an action brought against the director*. (Sec. 1701.59(A), (B), (C), and (E).)

Impermissible loans, dividends, distributions, etc.

Existing law. The existing GC Law *generally renders* directors jointly and severally liable to the corporation in specified manners if they vote for or assent to (1) the payment of a dividend or distribution, the making of a distribution of assets to shareholders, or the purchase or redemption of the corporation's own shares contrary to law or the corporation's articles, (2) a distribution of assets to shareholders during the winding up of the affairs of the corporation, on dissolution

of the corporation, or otherwise without the payment of all known obligations of the corporation or without making adequate provision for their payment, or (3) the making of a loan, other than in the usual course of business and subject to certain exceptions, to an officer, director, or shareholder of the corporation. There are a few exceptions to these liability provisions. Under one of those exceptions, a director is not liable for voting for or assenting to the types of actions described in (1) or (2), above, if, in determining the amount available for any dividend, purchase, redemption, or distribution to shareholders, the director in good faith relied on a financial statement of the corporation prepared by an officer or employee of the corporation in charge of its accounts or certified by a public accountant or firm of public accountants, if the director in good faith considered the assets to be of their book value, or if the director followed what the director believed to be sound accounting and business practice. The existing GC Law establishes a "two years from the day on which the violation occurs" *statute of limitations* in connection with an action brought by or on behalf of a corporation upon a cause of action based on a director's voting for or assenting to the actions described in (1), (2), or (3), above. (Sec. 1701.95(A)(1), (B)(1), and (F).)

Changes proposed by the bill. The bill *possibly* may remove a cause of action based on a director's voting for or assenting to loans, other than in the usual course of business, to an officer, director, or shareholder from existing law's "two years from the day on which the violation occurs" *statute of limitations*. If the bill's amendments to the statute of limitations provisions result in that removal, there may not be any statute of limitations in connection with a director's voting for or assenting to a covered impermissible loan. (Sec. 1701.95(F).)

Shareholders and subscriber liabilities

Background

The existing GC Law generally requires shareholders to pay for their shares by money, other property or property interests transferred to the corporation, or labor or services rendered to the corporation, specifies that promissory notes, drafts, and other obligations of a subscriber or purchaser are impermissible forms of payment for shares, regulates the amount of the requisite consideration for treasury shares with par value and for other shares with par value, and sets forth other share payment and issuance provisions. The bill continues these provisions without change. (Sec. 1701.18(A) to (E).)

Existing liabilities

The existing GC Law contains the following *personal liability* or *immunity from personal liability* provisions that apply to shareholders and certain other persons (secs. 1701.18(F), (G), (H), and (I) and 1701.95(D)):

(1) Each person who subscribes for or purchases shares of a corporation is liable to the corporation to pay or deliver to the corporation the consideration agreed upon. If the shares are with par value, the person generally must pay the full par value of the shares in money or other property or services. (Hereafter, "consideration payment liability.")

(2) Every original or transferee holder of shares that have not been paid for in the manner described under "***Background***," above, who acquires the shares *with actual knowledge* of that nonpayment is personally liable to the corporation for the amount unpaid on the shares. Notwithstanding any transfer of the shares, this liability continues until the shares are paid in full.

(3) A pledgee or other holder of shares as collateral security is not personally liable as a shareholder.

(4) An executor, administrator, guardian, trustee, trustee of a voting trust, receiver, or other person who holds shares in a *fiduciary capacity* is not personally liable as a shareholder, but the estate or property in the hands of the fiduciary is so liable or the real or beneficial owner is so liable as equity may require.

(5) A shareholder who knowingly receives any dividend, distribution, or payment made contrary to law or the corporation's articles is liable to the corporation for the amount received by that shareholder that is in excess of the amount that could have been paid or distributed without violation of law or the articles.

Changes proposed by the bill

The bill supplements existing law's *consideration payment liability provisions* as described in (1), above, by providing that a subscriber or purchaser of shares is not liable to the corporation or its creditors *in any other* amount (i.e., any amount other than the requisite consideration owed for the shares). The bill also enacts the following immunity provision and exception relative to shareholders and subscribers: except as set forth in any provision in the Ohio tax laws (R.C. Title 57), neither a shareholder nor a subscriber to shares is personally liable for any debts, obligations, or liabilities of the corporation in the absence of a written, enforceable agreement that is signed by the shareholder or subscriber and that specifically undertakes liability for the corporation's debts, obligations, or liabilities. (Sec. 1701.18(F) and (J).)

Dividends and distributions

Background

The existing GC Law permits a corporation's directors to declare dividends and distributions on outstanding shares of the corporation subject to certain statutory limitations. A dividend or distribution may be paid in the form of cash, property, or shares of the corporation or in the form of treasury shares or authorized but unissued shares and cannot be paid to the shareholders of any class in violation of the rights of shareholders of another class, when the corporation is insolvent, or when there is reasonable ground to believe that the payment will render the corporation insolvent. (Sec. 1701.33(A) to (G).)

The existing GC Law permits directors to fix a *record date* for any "lawful purpose" in connection with their corporation. Among other lawful purposes, a record date may be necessary to determine *the shareholders who are entitled to receive payment of any dividend or distribution*. In the latter situation, unless the corporation's articles or regulations specify a shorter or a longer period for the purpose, the record date cannot be more than 60 days before the date fixed for the payment of any dividend or distribution. (Sec. 1701.45(A).)

Changes proposed by the bill

The bill continues the provisions described above and further specifies as follows in connection with dividends and distributions (secs. 1701.33(H) and (I) and 1701.45(G)):

(1) The effect of a dividend or distribution generally is measured as of the date the dividend or distribution is authorized if the payment occurs within 120 days after the date of authorization or as of the date the payment is made if it occurs more than 120 days after the date of authorization. If a corporation pays a dividend or distribution by delivering an obligation or other evidence of indebtedness, the date of the delivery is the date upon which the effect of the dividend or distribution is measured.

(2) A corporation's indebtedness to a shareholder incurred by reason of a dividend or distribution made in accordance with the GC Law is *at parity* with the corporation's indebtedness to its general, unsecured creditors, except to the extent subordinated by agreement.

(3) If a corporation's directors do not fix a record date for determining shareholders entitled to a dividend or distribution, the record date is the date that the directors authorize the dividend or distribution.

COMMENT

1. Section 1701.05(A) (not in the bill) generally requires the name of a corporation to end in a certain manner, to be distinguishable in the Secretary of State's records from the name of any other nonprofit or for profit corporation authorized to do business in Ohio and from certain registered trade names, and to not contain any language that indicates or implies that the corporation is connected with a state or federal government agency. Section 1701.07(A) (not in the bill) requires each corporation to have and maintain an agent upon whom any process, notice, or demand required or permitted by statute to be served upon a corporation may be served.

2. Section 1151.01(A) (not in the bill) specifies that statutory references to "building and loan associations" are interchangeable with and are to be construed to mean "savings and loan associations."

3. Under the existing GC Law, the directors of a corporation also may adopt amendments to the corporation's articles under certain circumstances relative to (a) shares or obligations convertible into shares of the corporation, (b) options to purchase shares of the corporation, (c) redeemed shares of a class, (d) shares of a class surrendered to or acquired by the corporation upon conversion, exchange, purchase, or otherwise, (e) amended articles and the taking effect of any change of issued or unissued shares provided for in the amendment or the amended articles, or (f) the taking effect of a merger or consolidation in which the surviving or new corporation is an Ohio corporation (sec. 1701.70(B)(2) to (5)).

4. The existing GC Law also provides that, regardless of limitations or restrictions in a corporation's articles on the voting rights of the shares of any class, the holders of shares of a particular class and, in certain cases, the holders of shares of every class are entitled *to vote as a class* on the adoption of amendments to a corporation's articles that do any of the following: (a) increase or decrease the par value of the issued shares of the particular class, (b) change issued shares of the particular class, whether with or without par value, into a lesser number of shares of the same class or into the same or a different number of shares of any other class, with or without par value, previously or then authorized, (c) change the express terms, or add express terms, of the shares of the particular class in any manner substantially prejudicial to the holders of the shares, (d) change the express terms of issued shares of any class senior to the particular class in any manner substantially prejudicial to the holders of shares of the particular class, (e) provide, in the case of certain amendments, that the stated capital of the corporation will be reduced or eliminated as a result of the amendment or upon the exercise of conversion rights, (f) change substantially the purposes of the corporation or provide that a future amendment to the articles may be adopted that

substantially changes those purposes, or (g) change a corporation into a nonprofit corporation (sec. 1701.71(B)).

5. The bill continues the following types of statements that may be included in the express terms of a corporation's shares (sec. 1701.06(A)(1) to (11) and (13)):

Description of permissive statement	***Qualifying provisions***
(1) Dividend or distribution rights	They may be: cumulative or noncumulative; at a specified rate, amount, or proportion; with or without further participation rights; and in preference to, junior to, or on a parity in whole or in part with dividend or distribution rights of shares of any other class.
(2) Liquidation rights, preferences, and price	None.
(3) Redemption rights and price	None.
(4) Sinking fund requirements	They may require the corporation to provide a sinking fund out of earnings or otherwise for the purchase or redemption of shares or for dividends or distributions on them.
(5) Voting rights	They may be full, limited, or denied, except as otherwise required by law.
(6) Pre-emptive rights, or the denial or limitation of them	None.
(7) Conversion rights	None.
(8) Restrictions on the issuance of shares	None.
(9) Rights of alteration of express terms	None.
(10) The division of any class of shares into series	None.

Description of permissive statement	***Qualifying provisions***
(11) The designation and authorized number of shares of each series	None.
(12) Any other relative, participating, optional, or other special rights and privileges of, and qualifications or restrictions on, the rights of holders of shares of any class or series	None.

6. The following are definitions of the GC Law that apply throughout the bill's provisions (sec. 1701.01(E), (F), (I), and (K)--not in the bill):

(a) "Incorporator" means a person who signed the original articles of incorporation.

(b) "Shareholder" means a person whose name appears on the books of a corporation as the owner of shares of the corporation. Unless the articles of incorporation, the regulations, or the contract of subscription otherwise provides, "shareholder" includes a subscriber to shares, whether the subscription is received by the incorporators or pursuant to authorization by the directors.

(c) The "express terms" of shares of a class are the statements expressed in the articles with respect to those shares.

(d) "Treasury shares" means shares that belong to a corporation, that are not retired, and that have been issued and thereafter acquired by the corporation or have been paid as a dividend or distribution in shares of the corporation on treasury shares of the same class. These shares are deemed to be issued, but they generally cannot be considered as an asset or a liability of the corporation or as outstanding for dividend or distribution, quorum, voting, or other purposes.

7. The bill continues existing law's requirements that, unless a corporation's articles fix the consideration for which subscriptions are to be received, (a) the incorporators must fix the consideration for subscriptions for shares without par value, (b) the consideration for subscriptions of shares with par value must be the par value or a greater consideration that the incorporators fix, and (c) the incorporators may determine the fair value to the corporation of the consideration for subscriptions of shares not payable in money (sec. 1701.09(B)).

8. The bill does not modify existing law's examples of *permissible* corporate regulations or the ability of shareholders to adopt or authorize the

directors to adopt *emergency regulations* that are operative only during an emergency (sec. 1701.11(B) and (C)).

9. Unless otherwise provided in a corporation's articles or regulations, if certain specified "disclosure, knowledge, directors' or shareholders' vote, and/or fairness" circumstances are involved, a contract, action, or transaction apparently is not void or voidable with respect to a corporation (a) *for the reason* that it is between or affects the corporation and one or more of its directors or officers or is between or affects the corporation and any other person in which one or more of its directors or officers are directors, trustees, or officers or have a financial or personal interest or (b) *for the reason* that one or more interested directors or officers participate in or vote at the meeting of the directors or a committee of the directors that authorizes the contract, action, or transaction. Apparently, if none of the specified circumstances applies, a contract, action, or transaction is void or voidable. (Sec. 1701.60--referred to in the bill.)

HISTORY

ACTION	DATE	JOURNAL ENTRY	
Introduced	01-22-99	p.	114
Reported, H. Civil & Commercial Law	03-03-99	p.	258
Passed House (94-1)	04-27-99	pp.	466-467
Reported, S. Judiciary	10-14-99	p.	1071

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