Chapter 3 (Purpose and Powers) of the
MNCA Fourth Edition December 13, 2019 Exposure Draft

compared with

MNCA Third Edition Chapters 3 (Purpose and Powers)
(with amendments adopted through those published at 70 Bus. Law 467 (Spring 2015) and
also includes amendments approved on second reading
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Additions in Exposure Draft shown in blue with double underline]
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[CHAPTER] 3
PURPOSES AND POWERS

§ 3.01301. Purposes.
§ 3.02302. General powers.
§ 3.03303. Emergency powers.
§ 3.04304. Ultra vires.

§ 3.01301. PURPOSES

(a) Every nonprofit corporation has the purpose of engaging in any lawful activity
unless a more limited purpose is set forth in the articles of incorporation.

(b) If a corporation engaging in an activity that is subject to regulation
under another statute of this state, the corporation may incorporate under this [act] only if
incorporating under this [act] is not prohibited by, and subject to all limitations of, the other
statute. The corporation shall be subject to all the limitations of the other statute.

Substantially a reenactment of Revised Model Nonprofit Corporation Act (1987) § 3.01. (2016 Revision), § 3.01.
OFFICIAL COMMENT

Section 3.01301(a) provides that every nonprofit corporation automatically has the purpose of engaging in any lawful activity unless a narrower purpose is described in the articles of incorporation.

While Section 3.01301 does not impose any limitations on the purposes of a nonprofit corporation or the use of its assets, those forming a nonprofit corporation may limit the corporate purposes in the articles of incorporation. Such limitations may be added to obtain tax-exempt status, to attract significant contributions, or to provide a limited purpose for the corporation.

The limited scope of the ultra vires concept in litigation between the nonprofit corporation and outsiders means that a third person entering into a transaction that violates the restrictions in the purpose clause may be able to enforce the transaction in accordance with its terms if the person was unaware of the narrow purpose clause when entering the transaction. See the Official Comment to Section 3.04304.

Section 3.01301(b) is designed to tie in a nonprofit corporation with a limitless lawful purpose permitted by Section 3.01301(a) with the numerous state statutes that impose regulations or limitations on corporations engaging in certain activities. Many nonprofit corporations are subject to those types of regulations or limitations. Hospitals, colleges, secondary schools and health maintenance organizations, for example, are subject to extensive regulation.

Charitable corporations must comply with additional requirements imposed by under other provisions of law such as Section 501(c)(3) of the Internal Revenue Code such as the requirement that the charitable corporation be organized for one or more of the purposes listed in that section and the requirement that there be limitations on the distributions of assets upon dissolution.

§ 3.02302. GENERAL POWERS

Unless its articles of incorporation provide otherwise, every nonprofit corporation has perpetual duration and succession in its corporate name and has the same powers as an individual to do all things necessary or convenient to carry out its activities and affairs including, without limitation, power:

(1) to sue and be sued, complain and defend in its corporate name;
(2) to have a corporate seal, which may be altered at will, and to use it, or a facsimile of it, by impressing or affixing it or in any other manner reproducing it;

(3) to make and amend bylaws, not inconsistent with its articles of incorporation or with the laws of this state, for managing and regulating the activities and affairs of the corporation;

(4) to purchase, receive, lease, or otherwise acquire, and own, hold, improve, use, and otherwise deal with, real or personal property, or any legal or equitable interest in property, wherever located;

(5) to sell, convey, mortgage, pledge, lease, exchange, and otherwise dispose of all or any part of its property;

(6) to purchase, receive, subscribe for, or otherwise acquire, own, hold, vote, use, sell, mortgage, lend, pledge, or otherwise dispose of, and deal in and with shares or other interests in, or obligations of, any other entity;

(7) to make contracts and guarantees, incur liabilities, borrow money, issue its securities and obligations (which may be convertible into to include the option to purchase other securities of the corporation), and secure any of its obligations by mortgage or pledge of any of its property, franchises, or income;

(8) to lend money, invest and reinvest its funds, and receive and hold real and personal property as security for repayment[, except as limited by Section 8.32833 (loans to or guarantees for directors and officers)];

(9) to be a promoter, partner, member, associate, or manager of any partnership, joint venture, trust, or other entity;

(10) to conduct its activities, locate offices, and exercise the powers granted by this [actAct] within or without this state;

(11) to elect directors and appoint officers, employees, and agents of the corporation, define their duties, fix their compensation, and lend them money and credit[, except as limited by Section 8.32833];

(12) to pay pensions and establish pension plans, pension trusts, and benefit or incentive plans for any or all of its current or former directors, officers, employees, and agents;

(13) to make donations for charitable purposes;

(14) to impose dues, assessments, admission, and transfer fees on its members;
(15) to impose dues, assessments, admission, and transfer fees on its members;

(16) to carry on a business; and

(17) to make payments or donations, or do any other act, not inconsistent with law, that furthers the purposes, activities, and affairs of the corporation.


CROSS-REFERENCES

Bylaws, see §§ 2.06, 10.20 Subch. 9B.
Compensation of directors, see § 8.14811.
Debt and security interests, see § 6.43643.
Disposition of assets, see Ch. 1210.
“Employee” defined, see § 1.40102.
“Entity” defined, see § 1.40102.
Foreign corporations, see § 15.05 Ch. 13.
Indemnification, see Subch. 8E F.
“Members” defined, see § 1.40102.
“Membership” defined, see § 1.40102.
Ultra vires, see § 3.04304.

OFFICIAL COMMENT

The law of corporations has always proceeded on the fundamental assumption that corporations are creations with limited power; such an assumption was articulated by the United States Supreme Court as early as 1804, Head & Armory v. Providence Insurance Co., 6 U.S. (2 Cranch) 127, 169 (1804), and appears never to have been seriously questioned as a judicial matter.

It is clear that narrow and limited powers clauses are undesirable: they encourage litigation by bringing into question reasonable transactions that further the activities and interests of the corporation and to the extent transactions are unauthorized, may defeat valid and reasonable expectations. The history of many state statutes in this area is largely one ensuring that corporate powers are broad enough to cover all reasonable transactions. The issue of corporate powers must be distinguished from corporate purposes. A limitation on the purposes of a nonprofit corporation may be desirable, for example, to obtain tax-exempt status.

In developing Section 3.02, serious consideration was given to whether there was a continued need for a long list of corporate powers or whether a general provision granting every nonprofit corporation power to act to the same extent as an individual might be substituted. Because of the long history of these powers, it was feared that no matter how broadly-phrased a general provision might be, a court might conclude that some power might not exist because no
specific reference to it was made in the statute. It was also feared that cautious attorneys might begin to restore power clauses to articles of incorporation out of concern that a general clause of the type in question might not be interpreted literally. Hence, this section retains a general clause granting the corporation essentially the same powers as an individual, coupled with a nonexclusive listing of powers, including the traditional power clauses that appear in many state statutes.

The general philosophy of Section 302.302 is that nonprofit corporations formed under the act should be automatically authorized to engage in all acts and have all powers that an individual may have. Because broad grants of power of this nature may not be desired in some nonprofit corporations, Section 302.302 generally authorizes articles of incorporation to deny or limit specific powers to a specific corporation if that is felt desirable. Limitations may be imposed to obtain federal or state tax status, because a donor or grantor wishes to limit the activities of a corporation, or for some other reason. Illustrative of the powers that may be appropriate for limitation in specific corporations are the powers to make political contributions or to make expenditures to influence elections to the extent permitted by law.

The responsibility of the board of directors to manage the affairs of a nonprofit corporation includes both a decision-making function and an oversight function. See Section 8.01. In recent years the oversight function of the board of directors has become increasingly prominent. References throughout the act to the management of the affairs of a corporation, such as in Section 3.02(3), include the oversight function of the board.

The optional provisions of Section 302.302(8) and (11) should be used if loans to directors and officers are prohibited. The prior version of the act included as Section 8.32 an outright prohibition on loans to directors and officers. Section 8.32 has been made optional in the current version of the act because the approach to this issue varies among the states. Some states prohibit loans to directors and officers, while other states leave the wisdom and propriety of such loans to be evaluated on the basis of general fiduciary standards. A nonprofit corporation organized under the law of a state that does not prohibit loans to directors and officers should use particular care to ensure that any such loans serve a valid corporate purpose.

While Section 302.302(16) permits a nonprofit corporation to carry on any lawful business without restriction, nonprofit corporations need to be mindful that carrying on certain types of business can jeopardize the exempt status of charitable corporations.

Section 302.302(17) permits payments or donations or any other act “that further the purposes, activities, and affairs of the corporation.” This clause, which is in addition to and independent of the power to make charitable and similar donations under Section 302.302(13), permits contributions for purposes that may not be charitable, such as for political purposes or to influence elections. This power exists only to the extent consistent with law other than the act. For example, many states prohibit corporations of all types from making political contributions. It is the purpose of this section to authorize all corporate actions that are lawful or not against public policy.

The powers of a nonprofit corporation under the act exist independently of whether the corporation has a broad or narrow purpose clause. A corporation with a narrow purpose clause
nevertheless has the same powers as an individual to do all things necessary or convenient to
carry out its activities. Many actions are therefore intra vires even though they do not directly
affect the limited purpose for which the corporation is formed. In some instances, however, a
limited or narrow purpose clause may be considered to be a restriction on corporate powers as
well as a restriction on purposes. Since the same ultra vires rule is applicable to
corporations that exceed their purposes or powers (see the Official Comment to Section
3.04), it is not necessary to determine whether a narrow purpose clause also limits the powers
of the corporation but simply whether the purpose of the transaction in question is consistent
with the purpose clause. Of course, these issues cannot arise in corporations with an “any lawful
activity” purpose clause.

§ 3.03303. EMERGENCY POWERS

(a) In anticipation of or during an emergency, the board of directors of a nonprofit
corporation may:

(1) modify lines of succession to accommodate the incapacity of any director,
officer, employee, or agent; and

(2) relocate the principal office, designate alternative principal offices or
regional offices, or authorize the officers to do so.

(b) During an emergency, unless the articles of incorporation or bylaws provide
otherwise:

(1) notice of a meeting of the board of directors need be given only to those
directors it is practicable to reach and may be given in any practicable manner; and

(2) those directors who participate in a meeting of the board of directors shall
constitute a quorum; and

(23) one or more officers of the nonprofit corporation present at a meeting of
the board of directors may be deemed to be directors for the meeting, in order of rank and within
the same rank in order of seniority.

(c) Corporate action taken in good faith during an emergency to further the ordinary
activities and affairs of the nonprofit corporation:

(1) binds the corporation; and

(2) may not be used to impose liability on a director, officer, employee, or
agent.
An emergency exists for purposes of this section if a quorum of the board of directors cannot readily be assembled reasonably be convened because of some catastrophic event.


CROSS REFERENCES

Corporate powers, see § 3.02302.

“Notice” defined, see § 1.41102.

Notice of directors’ meeting, see § 8.22822.

“Principal office” defined, see § 1.40102.

OFFICIAL COMMENT

Section 3.03 grants every corporation limited powers to act in an emergency even though it has failed to adopt emergency bylaws. An “emergency” for purposes of Section 3.03 is defined in subsection (d) as any catastrophic event that makes it difficult or impossible to assemble a quorum of directors. In this situation, Section 3.03(b) dispenses with or relaxes notice requirements and permits corporate officers to serve as directors in order to achieve a quorum. The section also authorizes the board of directors, either before or during an emergency, to modify lines of succession and relocate the principal business office of the corporation. These actions may be taken only by the board of directors at a meeting at which a quorum is present after giving effect, if necessary, to Section 3.03(b).

These minimal provisions, it is believed, should permit a corporation to continue to function in the face of an emergency.

What constitutes notice in a practicable manner, as required by Section 3.03(b)(1), will depend on the nature of the emergency. In appropriate circumstances, practicable notice may involve the use of radio or publication, while in other circumstances more direct notice may be practicable.

§ 3.04304. ULTRA VIRES

(a) Except as provided in subsection (b), the validity of corporate action may not be challenged on the ground that the nonprofit corporation lacks or lacked power to act.

(b) The power of a nonprofit corporation to act may be challenged:

(1) in a derivative proceeding under [Chapter] 135 (derivative proceedings) by a member, director, or member of a designated body against the corporation to enjoin the act;
(2) in a proceeding by the corporation, directly, derivatively, or through a receiver, trustee, or other legal representative, against an incumbent or former director or member of a designated body, officer, employee, or agent of the corporation; or

(3) in a proceeding by the attorney general under Section 14.301312 (action by attorney general).

(c) In a proceeding by a member, director, or member of a designated body under subsection paragraph (b)(1) to enjoin an unauthorized corporate act as being outside the power of the nonprofit corporation, the court may enjoin or set aside the act, if equitable and if all affected persons are parties to the proceeding, and may award damages for loss (other than anticipated profits) suffered by the corporation or another party because of enjoining the unauthorized corporate act.


CROSS-REFERENCES

Corporate powers, see § 3.02302.
Corporate purposes, see § 3.01301.
Derivative proceedings, see Ch. 135.
Dissolution, see Ch. 141.
“Employee” defined, see § 1.40102.
“Proceeding” defined, see § 1.40102.

OFFICIAL COMMENT

The basic purpose of Section 3.04—as has been the purpose of all similar statutes during the 20th century—is to eliminate any vestiges of the doctrine of inherent incapacity of corporations. See Campbell, “The Model Business Corporation Act,” 11 BUS. LAW. 98, 102 (1956). Under this section it is unnecessary for purposes of dealing with a nonprofit corporation to inquire into limitation on its purpose or powers that may appear in its articles of incorporation. A person who is unaware of these limitations when dealing with the corporation is not bound by them. The phrase in Section 3.04(a) that the “validity of corporate action may not be challenged on the ground that the corporation lacks or lacked power to act” applies equally to the use of the doctrine as a sword or as a shield: a third person may no more avoid an undesired contract with a corporation on the ground the corporation was without authority to make the contract than a corporation may defend a suit on a contract on the ground that the contract is ultra vires.

The language of Section 3.04 extends beyond contracts and conveyances of property; “corporate action” of any kind cannot be challenged on the ground of ultra vires. For this reason it makes no difference whether a limitation in articles of incorporation is considered to be a
limitation on a purpose or a limitation on a power; both are equally subject to Section 3.04304.

Corporate action also includes inaction or refusal to act. The common law of ultra vires
distinguished between executory contracts, partially executed contracts, and fully executed ones;
Section 3.04304 treats all corporate action the same – except to the extent described in Section
3.04304(b) – and the same rules apply to all contracts no matter at what stage of performance.

Section 3.04304, however, does not validate corporate conduct that is made illegal or
unlawful by statute or common law decision. This conduct is subject to whatever sanction,
criminal or civil, that is provided by the statute or decision. Whether or not illegal corporate
conduct is voidable or rescindable depends on the applicable statute or substantive law and is not
affected by Section 3.04304.

Section 3.04304 also does not address the validity of essentially intra vires conduct that is
not approved by appropriate corporate action. It does not deal, for example, with the
enforceability of an executory contract to sell substantially all the assets of a corporation not in
the ordinary course of business that was not approved by the members as required by Section
12.02. This type of transaction is not beyond the purposes or powers of the corporation; it
simply has not been approved by the corporate authorities as required by law. Similarly, Section
3.04 does not deal with whether a nonprofit corporation is bound by the action of a corporate
agent if the action requires, but has not received, approval by the board of directors. Whether or
not the corporation is bound by this action depends on the law of agency, particularly the scope
of apparent authority and whether the third party knew or should have known of the defect in the
approval process. These actions may be ultra vires with respect to the agent’s authority
but they are not ultra vires with respect to the corporation and are not controlled by Section
3.04304.

Similarly, corporate action is not ultra vires under Section 3.04304 merely because it
constitutes a breach of fiduciary duty. For example, a misuse of corporate assets for personal
purposes by an officer or director is a breach of fiduciary duty and may be enjoined. Similarly, in
some circumstances a lien on corporate assets and a contract entered into by the nonprofit
corporation may be cancelled or enjoined if they constitute breaches of fiduciary duty and the
third person is charged with knowledge that they were improper. These transactions, however,
are not ultra vires with respect to the corporation, and cannot be attacked under Section 3.04304.
They may be enjoined because of the breach of fiduciary duty, not because the transaction
exceeds the powers or purposes of the corporation.

Section 3.04304(b) permits challenges to a lack of power by a nonprofit corporation in
three limited classes of cases:

(1) In suits by the attorney general under Section 14.301312. This provision does not
answer the question whether or not a corporation may be dissolved or enjoined by
the attorney general for committing an ultra vires act; it simply preserves the
power of the state to assert that certain corporate action was ultra vires.

(2) In a suit by the corporation, either directly or through a legal representative,
against incumbent or former directors, members of a designated body, or officers
for authorizing or causing the corporation to engage in an ultra vires act. Again, this section does not address whether or not there is liability for causing the corporation to enter into an ultra vires act; it simply preserves the power of the corporation to assert that certain corporate action was ultra vires.

(3) In a derivative suit by a member, director, or member of a designated body against the corporation to enjoin an ultra vires act, this derivative suit, however, is subject to the requirements of Section 3.04.304(c). Under this subsection an ultra vires act may be enjoined only if all “affected parties” are parties to the suit. The requirement that the action be “equitable” generally means that only third persons dealing with a corporation while specifically aware that the corporation’s action was ultra vires will be enjoined. The general phrase “if equitable” was included because of the possibility that other circumstances may exist that make it equitable to refuse to enjoin an ultra vires contract. Further, if enforcement of the contract is enjoined, either the third person or the corporation may in the discretion of the court be awarded damages from the other for loss (excluding anticipated profits).

Section 3.04.304(c) thus authorizes a court to enjoin or set aside an ultra vires act or grant other relief that may be necessary to protect the interests of all affected persons, including the interests of third persons who deal with the nonprofit corporation.
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**Summary report:**

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**Intelligent Table Comparison:** Active

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