Draft Revision of the
Model Nonprofit Corporation Act

Including Proposed Changes to the MNCA –
(i) Reflecting the 2016 Revision of the MBCA,
(ii) Conforming the MNCA to the
Uniform Business Organizations Code, and
(iii) Making Other Substantive Revisions

Exposure Draft of December 13, 2019

Stand-alone Version of the MNCA
With Comments

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§ 101. SHORT TITLE AND APPLICATION OF [Act]

(a) This [Act] shall be known and may be cited as the “[name of state] Nonprofit Corporation Act.”

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
(2008), § 1.01. Cf. Model Business Corporation Act (2016 Revision), § 1.01.

(b) This [Act] applies to all domestic nonprofit corporations in existence on its effective date that were incorporated under any general statute of this state providing for incorporation of nonprofit corporations if power to amend or repeal the statute under which the corporation was incorporated was reserved.

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
(2008), § 17.01. Cf. Model Business Corporation Act (2016 Revision), § 17.01.
(c) A foreign nonprofit corporation registered or authorized to do business in this state on the effective date of this [Act] is subject to this [Act], is deemed to be registered to do business in this state, and is not required to file a foreign registration statement under this [Act].


CROSS-REFERENCES

Effective date of act, § 1405.
Reservation of power to amend or repeal the act, § 107.
Saving provisions, § 1401.

OFFICIAL COMMENT

The short title provided by Section 101(a) creates a convenient name for the enacting state’s nonprofit corporation act.

The act’s application to all domestic nonprofit corporations in existence on the effective date of the act, as well as to all new domestic corporations formed after that date, avoids a confusing coexistence of different and overlapping rules of corporation law.

Section 101(b) applies this basic principle in its broadest sense by making the act applicable as of its “effective date” (prescribed in Section 1405) to all domestic nonprofit corporations formed under general statutes for nonprofit corporations.

Section 101(b) applies the act to all corporations to which that application is constitutionally permissible. In view of the universal adoption of “reservation of power” provisions in all states for more than a century, there are very few active nonprofit corporations to which this act will not be applicable under this section. See Section 107 for the act’s “reservation of power” provision.

Section 101(c) makes the act applicable on its effective date to all foreign nonprofit corporations that are registered to transact business in the state on that date. But these corporations need not refile and obtain new certificates of registration under the act. While Chapter 13 represents a change in the rules applicable to foreign corporations in many states, these changes are not of a type that require a transition period. It is therefore recommended that only a single effective date be provided for the application of the act to foreign corporations and that delayed effective dates for specific provisions in this regard are unnecessary.

§ 102. [Act] DEFINITIONS

In this [Act], unless the context clearly indicates otherwise:
“Articles” or “articles of incorporation” means the original articles of incorporation, all amendments thereof, and any other records filed with the secretary of state with respect to a domestic nonprofit corporation under any provision of this [Act] except Section 421 (annual report for secretary of state). If any record filed under this [Act] restates the articles in their entirety, thenceforth the articles shall not include any prior filings. When used with respect to a foreign nonprofit corporation or a domestic or foreign business corporation, the “articles of incorporation” of the corporation means the document of the corporation that is equivalent to the articles of incorporation of a domestic nonprofit corporation.

“Board” or “board of directors” means the group of individuals responsible for the management of the activities and affairs of the nonprofit corporation, regardless of the name used to refer to the group. The term includes a designated body to the extent:

1. the powers, functions, or authority of the board have been vested in, or are exercised by, the designated body; and
2. the provision of this [Act] in which the term appears is relevant to the discharge by the designated body of its powers, functions, or authority.

“Business corporation” or “domestic business corporation” means a corporation incorporated under the laws of this state and subject to the provisions of the [Model Business Corporation Act].

“Bylaws” means the code or codes of rules (other than the articles of incorporation) adopted for the regulation and governance of the internal affairs of the nonprofit corporation, regardless of the name or names used to refer to those rules.

“Charitable asset” means property that is given, received, or held for a charitable purpose.

“Charitable corporation” means a domestic nonprofit corporation that is operated primarily or exclusively for one or more charitable purposes.

“Charitable purpose” means a purpose that:

1. would make a corporation operated exclusively for that purpose eligible to be exempt from taxation under Section 501(c)(3) of the Internal Revenue Code, or
2. is considered charitable under law other than this [Act] or the Internal Revenue Code.

“Delegate” means a person elected or appointed to vote in a representative assembly for the election of directors or on other matters.
“Deliver” or “delivery” means any method of delivery used in conventional commercial
practice, including delivery by hand, mail, commercial delivery, and electronic transmission,
except that delivery to the secretary of state means actual receipt by the secretary of state.

“Designated body” means a person or group, other than a committee of the board of
directors, that has been vested by the articles of incorporation or bylaws with powers that, if not
vested by the articles or bylaws in that person or group, would be required by this [Act] to be
exercised by the board or the members.

“Director” means an individual designated, elected, or appointed, by that or any other
name or title, to act as a member of the board of directors, while the individual is holding that
position. The term does not include a member of a designated body, as such.

“Domestic,” with respect to an entity, means an entity governed as to its internal affairs
by the law of this state.

“Effective date,” when referring to a record accepted for filing by the secretary of state,
means the date and time determined in accordance with Section 163 (effective time and date of
filing).

“Electronic” means relating to technology having electrical, digital, magnetic, wireless,
optical, electromagnetic, or similar capabilities.

“Eligible entity” means a domestic or foreign unincorporated entity or a domestic or
foreign business corporation.

“Employee” does not include an individual serving as an officer or director who is not
otherwise employed by the corporation. A director or officer may accept duties that make the
director also an employee.

“Entitled to vote” means entitled to vote on the matter under consideration pursuant to
the articles of incorporation or bylaws of the nonprofit corporation or any applicable controlling
provision of law.

“Entity” includes a domestic or foreign business corporation, domestic or foreign
nonprofit corporation, estate, trust, domestic or foreign unincorporated entity, and state, the
United States, foreign government, or governmental subdivision.

“Expenses” means reasonable expenses of any kind that are incurred in connection with a
matter.

“Filing entity” means an unincorporated entity whose formation requires the filing of a
public organic record. The term does not include a limited liability partnership.

“Foreign,” with respect to an entity, means an entity governed as to its internal affairs by
an organic law of a jurisdiction other than this state.
“Foreign business corporation” means a corporation for profit incorporated under a law other than the law of this state that would be a business corporation if incorporated under the law of this state.

“Foreign corporation” or “foreign nonprofit corporation” means a corporation incorporated under a law other than the law of this state that would be a nonprofit corporation if incorporated under the law of this state.

“Foreign registration statement” means the foreign registration statement described in Section 1303 (foreign registration statement).

“Foreign unincorporated entity” means an unincorporated entity whose internal affairs are governed by an organic law of a jurisdiction other than this state.

“Fundamental transaction” means an amendment of the articles of incorporation or bylaws, merger, interest exchange, sale of all or substantially all of the assets, domestication, conversion, or dissolution of a nonprofit corporation.

“Governing jurisdiction” means the jurisdiction the law of which includes the organic law governing a domestic or foreign nonprofit corporation or eligible entity.

“Governmental subdivision” includes an authority, county, district, and municipality.

“Governor” means a person by or under whose authority the powers of an entity are exercised and under whose direction the business, activities, or affairs of the entity are managed pursuant to the organic law and organic records of the entity.

“Includes” and “including” denote a partial definition or a nonexclusive list.

“Individual” means a natural person.

“Interest” means:

(1) a share;

(2) a membership; or

(3) either or both of the following rights under the organic law governing an unincorporated entity:

(i) the right to receive distributions from the entity either in the ordinary course or upon liquidation; or
the right to receive notice or vote on issues involving its internal
affairs, other than as an agent, assignee, proxy, or person responsible for managing its business,
activities, or affairs.

“Interest holder” means a person who holds of record an interest.

“Interest holder liability” means:

(1) personal liability for a liability of a domestic or foreign business or
nonprofit corporation or unincorporated entity that is imposed on a person:

(i) solely by reason of the status of the person as an interest holder; or

(ii) by a provision of the articles of incorporation, bylaws, or organic
rules that make one or more specified interest holders or categories of interest holders liable in
their capacity as interest holders for all or specified liabilities of the entity; or

(2) an obligation of an interest holder under the organic rules of an entity to
contribute to the entity.


“Material interest” means an actual or potential benefit or detriment, other than one that
would devolve on the nonprofit corporation or the members generally, that would reasonably be
expected to impair the objectivity of an individual’s judgment when participating in the action to
be taken.

“Material relationship” means a familial, financial, professional, employment, or other
relationship that would reasonably be expected to impair the objectivity of an individual’s
judgment when participating in the action to be taken.

“Means” denotes an exhaustive definition.

“Member” means a person in whose name a membership is registered on the records of
the corporation and who has the right, not solely as a delegate, to select or vote for the election of
directors or delegates or to vote on any type of fundamental transaction. See Section 602(d)
(admission).

“Membership” means the rights and any obligations of a member in a domestic or foreign
nonprofit corporation.

“Membership corporation” means a nonprofit corporation whose articles of incorporation
or bylaws provide that it shall have members.
“Nonfiling entity” means an unincorporated entity whose formation does not require the filing of a public organic record.

“Nonmembership corporation” means a nonprofit corporation whose articles of incorporation or bylaws do not provide that it shall have members.

“Nonprofit corporation,” “corporation,” “domestic corporation,” or “domestic nonprofit corporation,” means a corporation incorporated under or subject to the provisions of this [Act] that is not a foreign corporation.

“Nonqualified foreign corporation” means a foreign corporation that is not authorized to conduct activities in this state.

“Notice” is provided for in Section 103 (notice).

“Officer” includes:

1. a person who is an officer as provided in Section 840 (officers); and
2. if a nonprofit corporation is in the hands of a custodian, receiver, trustee or other court-appointed fiduciary, that fiduciary or any person appointed by that fiduciary to act as an officer for any purpose under this [Act].

“Organic law” means the law of the governing jurisdiction of an entity that governs the internal affairs of the entity.


“Person” includes an individual and an entity.

“Principal office” means the office (in or out of this state) so designated in the annual report or foreign registration statement where the principal executive office of a domestic or foreign nonprofit corporation are located.

“Private organic rules” means the rules, whether or not in a record, that govern the internal affairs of an entity, are binding on all its interest holders, and are not part of its public organic record, if any. Where the private organic rules have been amended or restated, the term means the private organic rules as last amended or restated.

“Proceeding” means any threatened, pending, or completed action, suit, or proceeding, whether civil, criminal, administrative, arbitrative, or investigative, and whether formal or informal.

“Public organic record” means the record the filing of which by the secretary of state is required to form an entity. Where a public organic record has been amended or restated, the term means the public organic record as last amended or restated.
“Record” means information that is inscribed on a tangible medium or that is stored in an electronic or other medium and is retrievable in perceivable form.

“Record date” means the date established under Section 707 (record date) on which a nonprofit corporation determines the identity of its members and the membership interests they hold for purposes of this [Act]. Unless another time is specified when the record date is fixed, the determination shall be made as of the close of business at the principal office of the nonprofit corporation on the date so fixed.

“Registered foreign corporation” means a foreign corporation registered to conduct activities in this state.

“Secretary” means the corporate officer to whom the articles of incorporation, bylaws, or board of directors has delegated responsibility under Section 840(c) to maintain the minutes of the meetings of the board of directors, any designated body, committees, and the members, and for authenticating records of the nonprofit corporation.

“Shareholder” means the person in whose name shares are registered in the records of a domestic or foreign business corporation or the beneficial owner of shares to the extent of the rights granted by a nominee certificate on file with such a corporation.

“Shares” means the units into which the proprietary interests in a domestic or foreign business corporation are divided.

“Sign” means, with present intent to authenticate or adopt a record:

(1) to execute or adopt a tangible symbol; or

(2) to attach to or logically associate with the record an electronic sound, symbol, or process.

“State,” when referring to a part of the United States, includes a state or commonwealth, the District of Columbia, the Commonwealth of Puerto Rico, a territory or insular possession of the United States, and any agency or governmental subdivision of any of the foregoing.

“Type of entity” means a generic form of entity:

(1) recognized at common law; or

(2) formed under an organic law, whether or not some entities formed under that law are subject to provisions of that law that create different categories of the form of entity.

“Unincorporated entity” means an organization or artificial legal person that either has a separate legal existence or has the power to acquire an estate in real property in its own name and that is not any of the following: a domestic or foreign business or nonprofit corporation, an
estate, a trust, a governmental subdivision, a state, the United States, or a foreign government.
The term includes a general partnership, limited liability company, limited partnership, business
or statutory trust, joint stock association, and unincorporated nonprofit association.

“United States” includes a district, authority, bureau, commission, department, and any
other agency of the United States.

“Vote,” “voting” or “casting a vote” includes the giving of consent in a record without a
meeting. The term does not include either recording the fact of abstention or failing to vote for a
candidate or for approval or disapproval of a matter, whether or not the person entitled to vote
characterizes such conduct as voting or casting a vote.

“Voting group” means one or more classes of members that under the articles of
incorporation, bylaws, or this [Act] are entitled to vote and be counted together collectively on a
matter at a meeting of members. All members entitled by the articles of incorporation, bylaws, or
this [Act] to vote generally on the matter are for that purpose a single voting group.

“Voting power” means the current power to vote in the election of directors or delegates,
or to vote on approval of any type of fundamental transaction.

Revision), § 1.40.

CROSS-REFERENCES

Notice, § 103.
Special definitions in other sections of the [Act]:
“corporate action,” § 110(a).
“corporation,” § 850.
“court,” § 110(b).
“derivative proceeding,” § 501.
“director,” § 850.
“disinterested director,” § 850.
“exchanging entity,” § 1201.
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“party to an interest exchange,” § 1201.
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“survivor,” § 1201.
1. **Board of Directors and Designated Body**

The concept of a “designated body” recognizes that it is sometimes desirable for a nonprofit corporation to depart from the traditional governance structure based on a board of directors and, in appropriate circumstances, members. There is no limitation in the act on the number of designated bodies that a corporation may create.

When a designated body is exercising a power that would otherwise be exercised by the board of directors, the members of the designated body have the duties and liabilities of directors. See Section 8.12. However, when a designated body is exercising a power that would otherwise be exercised by the members, the members of the designated body should be subject only to the duties and liabilities of members or delegates.

2. **Bylaws**

The “bylaws” are those rules that are intended to have the status of bylaws under this act regardless of how the nonprofit corporation chooses to refer to them. Some corporations, for example, adopt a “constitution” that serves as bylaws.

Many nonprofit corporations adopt codes of conduct and other policies that have an important place in the conduct of the corporation’s activities but are not intended to have the status of bylaws under the act. A code of conduct that is not intended to be part of the bylaws, for example, will not be subject to the provisions of the act governing the adoption and amendment of bylaws in Chapters 2 and 9B. On the other hand, a corporation could choose to include a code of conduct in its bylaws, in which case the code of conduct would be subject to the provisions of the act in the same manner as the other provisions of the bylaws.

3. **Charitable Corporation and Charitable Purposes**

There are certain areas in which public policy concerns are more sensitive with respect to some nonprofit corporations than others. The act accordingly provides different rules for charitable corporations with respect to certain subjects.

Rather than providing a specific list of purposes that are considered charitable for purposes of the act, Section 102 defines charitable purposes as including those purposes that are considered charitable under Section 501(c)(3) of the Internal Revenue Code or other law. The prior act also treated all nonprofit corporations that are exempt from taxation under Section 501(c)(4) as having a charitable purpose. While a corporation taxed under Section 501(c)(4) may have a charitable purpose, treating all such corporations as having a charitable purpose was overly broad.

4. **Corporation, Domestic Corporation, Domestic Nonprofit Corporation, Foreign Corporation, Foreign Nonprofit Corporation and Nonprofit Corporation**
The word “corporation” is used only after a more complete description of the corporation (“domestic corporation,” “domestic nonprofit corporation,” “foreign corporation,” “foreign nonprofit corporation,” or “nonprofit corporation”) has already been used in the same subsection. Notwithstanding that style convention, in a few instances, the phrase “domestic corporation” has been used in order to contrast it with a foreign corporation. In addition, the phrase “domestic nonprofit corporation” has been used on occasion to contrast it with a domestic business corporation.

5. Delegate

Professional associations, churches, political parties, and numerous other organizations hold representative assemblies from time to time at which major corporate and policy decisions are made. These representative assemblies may be called conventions, annual meetings, or some other name. A person elected or appointed to vote at a representative assembly is a “delegate” for purposes of the act even if the person is called by some other name.

6. Electronic

The definition of “electronic” is patterned after the definition of that term in Uniform Electronic Transactions Act § 2(5). While not all of the technologies listed are technically “electronic” in nature (e.g., optical fiber technology), the term was chosen in the Uniform Electronic Transactions Act as the most descriptive single term available to describe current technologies. The term should be construed broadly to include developing technologies arguably within any aspect of the definition. Because “delivery” is defined to include electronic transmission, the use of such means as email, fax, and telephone are permissible ways of delivering notices under the act. But the use of electronic technology will not always involve a “record” as defined in Section 102. A telephone conversation between two people will involve electronic technology, but will not create a “record” because the conversation will not later be “retrievable” as required to create a record. Leaving a message on voicemail, however, results in a record for as long as the voicemail message remains saved and thus retrievable and capable of reproduction in perceivable form.

7. Entity and Unincorporated Entity

The term “entity” appears in the definition of “person” and covers all types of artificial persons. Estates and trusts and general partnerships are included even though they may not, in some jurisdictions, be considered artificial persons. The term “trust” as used in the definition of “entity” means a nonbusiness trust, such as a traditional testamentary trust, inter vivos trust, or charitable trust.

The term “entity” is broader than the term “unincorporated entity” because the definition of “entity” includes several categories of persons that are excluded from the definition of “unincorporated entity.” The term “unincorporated entity” includes limited liability partnerships and limited liability limited partnerships because those entities are forms of general partnerships and limited partnerships, respectively, that have made the additional required election claiming that status.
The Uniform Unincorporated Nonprofit Association Act gives an unincorporated nonprofit association the power to acquire an estate in real property and thus an unincorporated nonprofit association organized in a state that has adopted that act will be an “unincorporated entity.” At common law, an unincorporated nonprofit association was not a legal entity and did not have the power to acquire real property. Most states that have not adopted the Uniform Act have nonetheless modified the common law rule, but states that have not adopted the Uniform Act should analyze whether they should modify the definition of “unincorporated entity” to add an express reference to unincorporated nonprofit associations.

“Business or statutory trust” includes any trust carrying on a business, such as a Massachusetts trust, real estate investment trust, or other common law or statutory business trust. The term “unincorporated entity” expressly excludes estates and trusts (i.e., trusts that are not business trusts), whether or not they would be considered artificial persons under the governing jurisdiction’s law, to make it clear that they are not eligible to participate in a merger, interest exchange, or conversion under Chapter 12. If a nonprofit corporation wishes to engage in a “merger,” as defined in Section 1201, with a charitable trust it will be necessary to first incorporate the trust.

A form of co-ownership of property or sharing of returns from property that is not a partnership under the Uniform Partnership Act (1997) will not be an “unincorporated entity.”

8. Expenses

The act provides in a number of contexts that expenses relating to a proceeding incurred by a person shall or may be paid by another, through indemnification or by court order in specific contexts. Other than the requirement that expenses must be reasonable in the circumstances, the type or character of the expenses is not limited. Examples include such things as fees and disbursements of counsel, experts of all kinds, and jury and similar litigation consultants; travel, lodging, transcription, reproduction, photographic, video recording, communication, and delivery costs, whether included in the disbursements of counsel, experts, or consultants, or directly incurred; court costs; and premiums for posting required bonds.

9. Interest Holder Liability

The term “interest holder liability” is used in the context of provisions in Chapter 12 that preserve the personal liability of interest holders when the entity in which they own interests is the subject of a transaction under that chapter. The term includes only liabilities that are imposed by or pursuant to statute on interest holders. Liabilities that an interest holder incurs by contract (other than a contract that is part of an entity’s organic rules, such as a partnership agreement) are not included. Thus, for example, if a state’s nonprofit corporation law were to make members personally liable for unpaid wages, that liability would be an “interest holder liability.” If, on the other hand, a member were to guarantee payment of an obligation of a corporation, that liability would not be an “interest holder liability.”

10. Member and Membership
“Member” and “Membership” are defined for purposes of the act to refer only to the rights of a member in a nonprofit corporation. Although the owners of a limited liability company are generally referred to as “members,” for purposes of the act they are referred to as “interest holders” and what they own in the limited liability company is referred to in the act as an “interest.”

A nonprofit corporation will sometimes refer to contributors or other persons interested in the activities of the corporation as “members” even though those persons do not fit within the definition of “member.” If a person does not have the right to vote for the election of directors or delegates or to vote on fundamental transactions, the person will not be a “member” for purposes of the act even though the person may be referred to by the corporation as a member.

A person who has the right to select or vote for the election of members of a designated body, but who does not have the right to vote for the election of directors or on approval of any type of fundamental transaction, is not within the definition of “member.”


The term “organic records” includes both public organic records and private organic rules. The term “public organic record” includes such filings as the certificate of limited partnership of a limited partnership, the articles of organization or certificate of formation of a limited liability company, the deed of trust of a business trust, and comparable documents, however denominated, that are publicly filed to create other forms of unincorporated entities. The term “private organic rules” includes a partnership agreement of a general or limited partnership, an operating agreement of a limited liability company, and comparable agreements, however denominated, of other forms of unincorporated entities.

12. Person

The term “person” is defined to include an individual or an entity. In the case of an individual, this act assumes that the person is competent to act in the matter under general state law independent of the corporation statute.

13. Principal Office

Many corporations maintain numerous offices, but there is usually one office, sometimes colloquially referred to as the home office, headquarters, or executive suite, where the principal corporate officers are located. The corporation must designate its principal office address in the annual report required by Section 421. In case of doubt as to which corporate office is the principal office, the designation by the corporation in its annual report should be accepted as establishing the principal office of the corporation.

14. Record
The definition of “record” is patterned after the definition of that term in Uniform Electronic Transactions Act § 2(13). That definition, in turn, was based on the same definition in section 106(9) of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7006(9). The term includes both communication systems that in the normal course produce paper documents, such as telegrams and facsimiles, as well as communication systems that transmit and permit the retention of data that is then subject to subsequent retrieval and reproduction in perceivable form. The term is intended to be broadly construed and include the evolving methods of electronic delivery.

15. Secretary

The term “secretary” is defined in Section 102 because the act does not require the corporation to maintain any specific or titled officers. See Section 840. However, some corporate officer, regardless of title, must perform the functions described in this definition, and that officer is referred to as the “secretary” in various sections of the act that impose a duty to perform those functions.

16. Sign

The definition of “sign” is patterned after the definition of that term in Uniform Electronic Transactions Act § 2(8) (“electronic signature”). That definition, in turn, was based on the definition of “electronic signature” in section 106(5) of the Electronic Signatures in Global and National Commerce Act, 15 U.S.C. § 7006(5). The term includes manual, facsimile, conformed, or electronic signatures, and any manifestation of an intention to execute or authenticate a record will be accepted. Electronic signatures encompass any methodology approved by the secretary of state for purposes of verification of the authenticity of the record. This could include a typewritten conformed signature or other electronic entry in the form of a computer data compilation of any characters or series of characters comprising a name intended to evidence authorization and execution of a record.

17. Voting Group

Section 102 defines “voting group” for purposes of the act as a matter of convenient reference. A “voting group” consists of all the members of one or more classes that under the act, articles of incorporation, or bylaws are entitled to vote and be counted together collectively on a matter. Members entitled to vote “generally” on a matter under the act, articles, or bylaws are for that purpose a single voting group. The word “generally” signifies all members entitled to vote on the matter by the act, articles, or bylaws that do not expressly have the right to be counted or tabulated separately. “Voting groups” are thus the basic units of collective voting at a members’ meeting, and voting by voting groups may provide essential protection to one or more classes of members against actions that are detrimental to the rights or interests of that class.

The determination of which members form part of a single voting group must be made from the provisions of the act, articles of incorporation and bylaws. In a few instances under the act, the board of directors or a designated body may establish the right to vote by voting groups. On most matters coming before members’ meetings, only a single voting group, consisting of a
class of voting members, will be involved, and action on such a matter is effective when approved by that voting group pursuant to Section 724. See Section 725(a). If a second class of members is also entitled to vote on the matter, then a further determination must be made as to whether that class is to vote as a separate voting group or whether it is to vote along with the other voting members as part of a single voting group.

Members of the board of directors are usually elected by the single voting group of members entitled to vote generally; in some circumstances, however, some directors may be selected by one voting group and other directors by one or more different voting groups. See Section 804.

18. Voting Power

The term “voting power” means the current power to vote in the election of directors or delegates, or on approval of a fundamental transaction. Application of this definition turns on whether the relevant members have the power to vote as of the time a vote is being conducted. If members have the power to vote in an election of directors only under a certain contingency, for example, those members would not have voting power unless the contingency has occurred, and then only during the period when the voting rights are in effect. Members that have the power to vote for any directors as of the time a vote is conducted have the current power to vote in the election of directors even if the members do not have the power to vote for all directors.

§ 103. NOTICE

(a) A notice under this [Act] must be given or delivered in accordance with this section. Notice must be in a record unless oral notice is authorized by this [Act] or is reasonable under the circumstances.

(b) Except as provided in subsection (c), notice may be communicated in person, by delivery, or in any other manner authorized by the articles of incorporation or bylaws. If these forms of communication are impracticable, notice may be given by means of a broad non-exclusionary distribution to the public (which may include a newspaper of general circulation in the area where published; radio, television, or other form of public broadcast communication; or other methods of distribution that the nonprofit corporation has previously identified to its members).

(c) Notice by a nonprofit corporation to a director, member of a designated body, or member must be given to the mailing or electronic address of the person shown in the records of the corporation or as provided in subsection (f) or (g).

(d) Notices or service of process may be delivered to a domestic nonprofit corporation or foreign nonprofit corporation registered to conduct activities in this state by delivery to its registered agent at its registered office. Notices may also be delivered to the secretary of the corporation at its principal office shown in its most recent annual report or, in the
case of a foreign corporation that has not yet delivered an annual report, in its foreign registration statement.

(e) Notice under this [Act] is effective at the earliest of the following:

(1) when received;
(2) when left at the recipient’s residence or usual place of business;
(3) five days after its deposit in the United States mail or with a commercial delivery service, if the postage or delivery charge is paid and the notice is correctly addressed;
(4) on the date shown on the return receipt, if sent by registered or certified mail, return receipt requested, or by commercial delivery service.

(f) Oral notice is effective when communicated, if communicated in a comprehensible manner.

(g) If this [Act] prescribes notice requirements for particular circumstances, those requirements govern. If the articles of incorporation or bylaws prescribe notice requirements, not inconsistent with this section or other provisions of this [Act], those requirements govern.

(h) With respect to electronic communications:

(1) Unless otherwise provided in the articles of incorporation or bylaws, or otherwise agreed between the sender and the recipient, an electronic communication is received when:

(i) it enters an information processing system that the recipient has designated or uses for the purpose of receiving electronic records or information of the type sent and from which the recipient is able to retrieve the electronic record; and
(ii) it is in a form capable of being processed by that system.

(2) An electronic communication is received under paragraph (h)(1) even if no individual is aware of its receipt.

(3) Receipt of an electronic acknowledgement from an information processing system described in paragraph (h)(1) establishes that a record was received but, by itself, does not establish that the content sent corresponds to the content received.

(i) Whenever notice would otherwise be required to be given under any provision of this [Act] to a member, the notice need not be given if notice of two consecutive annual meetings, and all notices of meetings during the period between such two consecutive annual meetings have been returned undeliverable or could not be delivered. If a member delivers to the
nonprofit corporation a notice setting forth the member’s then-current address, the requirement
that notice be given to that member is reinstated.  

Source Note: Model Nonprofit Corporation Act, 3rd Ed.

CROSS-REFERENCES

Annual meeting, § 701.
Annual report, § 421.
“Deliver” defined, § 102:
“Electronic” defined, § 102.
Meetings:
   board of directors, § 822.
   members, § 705.
“Principal office”:
   defined, § 102.
   designated in annual report, § 421.
“Record” defined, § 102.
Record of members, § 401.
Special notice requirements:
   attorney general, §§ 113 and 140.
   derivative proceedings, § 509.
   resignation of registered agent, §§ 222 and 1304.
   service on corporation, § 223.

OFFICIAL COMMENT

Section 103 establishes rules for determining how notice may be given and when notice
is effective for a variety of purposes under the act. Those rules permit many other sections of the
act to be phrased simply in terms of delivering notice without repeating details with respect to
how notice should be given and when it is effective in various circumstances.

Notice may be given to a nonprofit corporation by delivering a copy of the notice to the
corporation or to the secretary of the corporation at its principal office. This method of giving
notice to the corporation, however, is not exclusive, and notice may be given in other ways as
well.

Section 103(b) authorizes a variety of alternative forms of notice if the otherwise
applicable methods of delivery are impracticable, including notice by methods of distribution
that are not provided for in the articles of incorporation or bylaws, but which the nonprofit
corporation has previously identified to its members. Section 103(b) does not limit the methods
of notice that may be used and, if appropriately provided for in the articles or bylaws, or
identified to the members, notice may be given by posting on the corporation’s website or a
social media platform.
Section 103(f) recognizes that notice may be given orally which could include oral notice through voice mail or other similar means.

Section 103(g) recognizes that other sections of the act prescribe specific notice requirements for particular situations and provides that these specific requirements, rather than the general requirements of Section 103, control. The second sentence of Section 103(g) permits a nonprofit corporation’s articles of incorporation or bylaws to prescribe the corporation’s own notice requirements, if they are not inconsistent with the general requirements of this section or specific requirements of other sections of the act.

Section 103(h)(2) makes clear that receipt of an electronic communication is not dependent on a person having notice that the record is in the person’s system. Receipt occurs when the record reaches the designated system whether or not the recipient ever retrieves the record. The paper analog is the recipient who never reads a mail notice. Section 103(h)(3) provides legal certainty regarding the effect of an electronic acknowledgement. It only addresses the fact of receipt, not the quality of the content, nor whether the electronic record was read or “opened.”

Section 103(i) balances the requirement that the nonprofit corporation deliver notice to members regarding meetings and the practical need to allow corporations to cease providing notices where notices are being returned undelivered and it is clear that the member no longer is located at the address previously provided to the corporation. Absent such a provision, the corporation technically may be required to continue to attempt to deliver a notice to the member in order to satisfy a statutory requirement regarding notices to members or otherwise risk questions concerning the validity of the meeting for which the notice is required.

Under Section 103(i), a nonprofit corporation generally will be required to continue to provide notice unless undeliverable items are returned over a period that could not be less than twelve months and could extend for up to twenty-four months. For instance, if the first undeliverable communication were delivered to a member six months before the next notice of an annual meeting is required, the corporation would have to wait until the annual meeting notice proves to be undeliverable to commence the non-delivery period, and then would have to wait until the next annual meeting notice after that also proves to be undeliverable before suspending the notification requirement. This amounts to a non-delivery period of eighteen months which could extend to two years under the right circumstances.

§ 104. SIGNING OF FILED RECORDS

A record delivered to the secretary of state for filing pursuant to this [Act] must be signed as follows:

(1) if the entity delivering the record for filing is a domestic or foreign nonprofit corporation, by:

(i) a director, a member of a designated body, or an officer; or
(ii) if directors or members of a designated body have not been selected or the corporation has not been formed, an incorporator; or

(2) if the entity delivering the record for filing is not a domestic or foreign nonprofit corporation, by:

(i) a person with authority to sign for the entity; or

(ii) if the entity is in the hands of a custodian, receiver, trustee, or other court-appointed fiduciary, that person.


CROSS-REFERENCES

Penalty for signing false record, § 169.
“Sign” defined, § 102.

OFFICIAL COMMENT

A record delivered for filing must be signed by a corporate officer. No specific corporate officer is designated as the appropriate officer to sign, although the record must state the office or capacity in which the officer signs the record. The act does not require that documents be acknowledged or verified as a condition for filing. Requirements such as these serve little purpose in connection with documents filed under the act because Section 169 makes it a criminal offense for any person to sign a document for filing with knowledge that it contains false information. On the other hand, many organizations, like lenders or title companies, may desire that specific documents include acknowledgments, verifications, or seals. These additional forms of authentication do not affect the eligibility of a record for filing.

§ 105. EXTRANISIC FACTS IN FILED RECORD

Whenever a provision of this [Act] permits any of the terms of a plan or a filed record to be dependent on facts objectively ascertainable outside the plan or filed record, the following provisions apply:

(1) The manner in which the facts will operate upon the terms of the plan or filed record shall be set forth in the plan or filed record.

(2) The facts may include:

(i) any of the following that is available in a nationally recognized news or information medium either in print or electronically: statistical or market indices, market
prices of any security or group of securities, interest rates, currency exchange rates, or similar
economic or financial data;

(ii) a determination or action by any person or body, including the
nonprofit corporation or any other party to a plan or filed record; or

(iii) the terms of, or actions taken under, an agreement to which the
corporation is a party, or any other agreement or record.

(3) As used in this section:

(i) “filed record” means a record filed with the secretary of state under
any provision of this [Act] except [Chapter] 13 (foreign corporations) or Section 421 (annual
report for secretary of state); and

(ii) “plan’ means a plan of domestication, conversion, merger or
interest exchange.

(4) The following provisions of a plan or filed record may not be made
dependent on facts outside the plan or filed document:

(i) the name and address of any person required in a filed record;

(ii) the registered office of any entity required in a filed record;

(iii) the registered agent of any entity required in a filed record;

(iv) the number of authorized interests and designation of each class or
series of interests;

(v) the effective date of a filed record; and

(vi) any required statement in a filed record of the date on which the
underlying transaction was approved or the manner in which that approval was given.

(5) If a provision of a filed record is made dependent on a fact ascertainable
outside of the filed record, and that fact is not ascertainable by reference to a source described in
Section 105(2)(i) or a record that is a matter of public record, and the affected members have not
received notice of the fact from the corporation, then the corporation shall file with the secretary
of state an amendment to the filed record setting forth the fact promptly after the time when the
fact referred to is first ascertainable or thereafter changes. The amendment under this Section
105(5) is deemed to be authorized by the authorization of the original filed record to which it
relates and may be filed by the corporation without further action by the board of directors, a
designated body, or the members.
OFFICIAL COMMENT

Section 105 applies where the act permits any of the terms of a filed record or plan to be made dependent on facts outside the record or plan. A common example is a reference to an interest rate such as the federal funds rate. Section 105(2)(ii) also provides that the facts on which a filed record or plan may be made dependent include facts within the control of the nonprofit corporation in order to make clear that those facts do not need to occur independently. In addition to a determination or action by the corporation, references to extrinsic facts may also include references to determinations or actions by the board of directors; a designated body; a committee of the board or a designated body; an officer, employee, or agent of the corporation; or any other person.

The only limitations on referring to extrinsic facts in a filed record or plan are that the facts must be objectively ascertainable and that the filed record or plan must state the manner in which the facts will operate. These requirements will help to avoid disputes over whether an extrinsic fact has occurred or its effect.

If the terms of a filed record or plan are made dependent on an agreement or other record, care should be taken to identify the agreement or record appropriately. The agreement or record must be identified in a manner that satisfies the objectively ascertainable standard, and the manner in which the terms or events under it are to operate must be specified. Consideration should also be given to the intended effects of an amendment to the agreement or record. A simple reference to an agreement will presumably include subsequent amendments, while a reference to the same agreement as in effect on a specified date presumably will not.

Chapter 12 generally requires the board of directors to adopt a plan. If the terms of such a plan are determined by reference to extrinsic facts, the board should establish appropriately defined parameters for such terms in order to discharge its statutory duties.

§ 106. RELATIONSHIP OF [Act] TO OTHER LAWS

(a) Unless displaced by particular provisions of this [Act], the principles of law and equity supplement this [Act].

(b) This [Act] does not authorize an act prohibited by, and does not affect the application or requirements of, law other than this [Act].

OFFICIAL COMMENT
Section 106(a) is a standard provision in uniform and model acts and has been included to make clear that unless a particular provision of this act displaces “other law,” the principles of law and equity continue to apply, including with respect to the rights of creditors, transferees, assignees, or other similar parties.

Section 106(b) preserves regulatory jurisdiction over actions and fundamental transactions under the act, such as amendments of the articles, mergers, sales of assets, and dissolution. The provisions of the act must be read together with any applicable regulatory law and, to the extent they are irreconcilable, the provisions of the regulatory law will control.

Section 106 does not create an independent power of a court or regulatory agency to enjoin or reverse an action or fundamental transaction. The appropriate remedy for violation of a regulatory law will be determined under the regulatory law itself.

Charitable corporations also must comply with applicable provisions of the Internal Revenue Code.

§ 107. RESERVATION OF POWER TO AMEND OR REPEAL

The [name of state legislature] has power to amend or repeal all or part of this [Act] at any time and all domestic and foreign nonprofit corporations subject to this [Act] are governed by the amendment or repeal.


CROSS-REFERENCES

Application of act to existing domestic nonprofit corporation, § 101(b).
Application of act to existing registered foreign nonprofit corporation, § 101(c).
Effective date of act, § 1405.
Saving provisions, § 17.03.

OFFICIAL COMMENT

Provisions similar to Section 107 have their genesis in Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat) 518 (1819), which held that the impairment of contracts clause of the United States Constitution, Article I, Section 10, Clause 1, prohibited the application of newly enacted statutes to existing corporations while suggesting the efficacy of a reservation of power similar to Section 107. The purpose of Section 107 is to avoid any possible argument that a nonprofit corporation or a member, beneficiary, or any other person has contractual or vested rights in any specific statutory provision and to ensure that the state may in the future modify its corporation statutes as it deems appropriate and require existing corporations to comply with the statutes as modified.
All articles of incorporation and foreign registration statements filed under the act are subject to the reservation of power set forth in Section 107. Further, nonprofit corporations “governed” by the act – which includes all corporations formed or registered under earlier, general incorporation statutes that contain a reservation of power – are also subject to the reservation of power of Section 107 and bound by subsequent amendments to the act.

Many states have constitutional provisions mandating the reservation of power to amend or modify corporate statutes and charters. In those states, Section 107 is also supported by specific constitutional authorization.

[Subchapter] B
REVIEW OF CONTESTED CORPORATE ACTION

§ 110. [Subchapter] definitions.
§ 111. Proceedings prior to corporate action.
§ 112. Review of contested corporate action.
§ 113. Notice to attorney general. [Optional]

§ 110. [Subchapter] DEFINITIONS

(a) This [Subchapter] applies to, and the term “corporate action” in this [Subchapter] means any of the following actions:

(1) The election, appointment, designation or other selection and the suspension, removal or expulsion of members, delegates, directors, members of a designated body, or officers of a nonprofit corporation.

(2) The taking of action on any matter submitted for action to the members, delegates, directors, members of a designated body, or officers of a nonprofit corporation that is required or permitted to be submitted to them under this [Act], any other provision of law, or the articles of incorporation or bylaws.

(b) The “court” referred to in this [Subchapter] is the [name or describe] court [of the county where the corporation’s principal office (or, if none in this state, its registered office) is located] [of county].

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.50.

CROSS-REFERENCES

“Delegates” defined, § 102.
“Designated body” defined, § 102.
“Members” defined, § 102.
“Officers” defined, § 102.
The rights to seek judicial relief provided in Subchapter 1B are available for all types of nonprofit corporations. It is expected, however, that the courts will use their discretion to avoid becoming overly entangled in the affairs of religious corporations.

§ 111. PROCEEDINGS PRIOR TO CORPORATE ACTION

(a) Where under applicable law or the articles of incorporation or bylaws of a nonprofit corporation there has been a failure to hold a meeting to take corporate action under any circumstances other than those described in Section 703(a) (court-ordered meeting), and the failure has continued for 30 days after the date designated or appropriate therefor, the court may summarily order a meeting to be held upon the application of [the attorney general, in the case of a charitable corporation, or] any person entitled, either alone or in conjunction with other persons similarly seeking relief under this section, to call a meeting to consider the corporate action in issue.

(b) The court may determine the right to vote at the meeting of persons claiming that right, may appoint an individual to hold the meeting under such orders and powers as the court may deem proper, and may take such action as may be required to give due notice of the meeting and convene and conduct the meeting in the interests of justice.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.51.

CROSS-REFERENCES

“Corporate action” defined, § 110(a).

OFFICIAL COMMENT

Section 111 provides a way to conduct meetings or take corporate action when it is otherwise impractical or impossible to do so. For example, a nonprofit corporation may have a quorum requirement that effectively prevents it from holding a meeting of members because of the difficulty of securing the required attendance of members. Or a corporation may have inaccurate records and be unable to identify its members or directors.

The power of the court to order a meeting under Section 111 is discretionary. If the court decides to order a meeting, Section 111 allows the court to order a meeting and frame the manner in which it is to be conducted even if it is necessary to dispense with otherwise applicable requirements of the act, articles of incorporation, or bylaws.

§ 112. REVIEW OF CONTESTED CORPORATE ACTION
(a) Upon petition of a person whose status as, or whose rights or duties as, a member, delegate, director, member of a designated body, or officer of a corporation are or may be affected by any corporate action, the court may hear and determine the validity of the corporate action.

(b) The court may make such orders in any such case as may be just and proper, with power to enforce the production of any books, papers and records of the corporation and other evidence that may relate to the issue. The court shall provide for notice of the pendency of the proceedings under this section to all persons affected thereby. If it is determined that no valid corporate action has been taken, the court may order a meeting to be held in accordance with Section 111 (proceedings prior to corporate action).

(c) Subsection (a) shall not apply if a nonprofit corporation has provided in its articles of incorporation or bylaws for a means of resolving a challenge to a corporate action, but the court may enforce the articles or bylaws if appropriate.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.52.

CROSS-REFERENCES

“Corporate action” defined, § 110(a).

OFFICIAL COMMENT

Section 112 provides an expeditious way to secure judicial review of corporate elections, the filling of corporate positions in other fashions, or the taking of action on matters such as fundamental transactions. The court has broad powers to fashion relief in the manner it considers appropriate.

§ 113. NOTICE TO ATTORNEY GENERAL [Optional]

The plaintiff in a proceeding under this [Subchapter] must notify the attorney general within ten days after commencing the proceeding if it involves a charitable corporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.53.

CROSS-REFERENCES

“Charitable corporation” defined, § 102.

OFFICIAL COMMENT

Section 113 is marked optional for two reasons. As a general matter, an enacting state should consider whether the substance of Section 113 would be better placed with the other
provisions of its law relating to the powers and duties of the attorney general. See the Official Comment to Section 140. Even if an enacting state decides to retain a requirement of notice to the attorney general in the act, Section 113 will not be needed if Section 140 is included in the state’s version of the act.

Notice to the attorney general of a proceeding under Subchapter 1B involving a charitable corporation gives the attorney general an opportunity to learn of and evaluate the dispute. Section 113 does not require the attorney general to join an action under Subchapter 1B and does not detract from the jurisdiction the attorney general may otherwise have in states adopting the act.

[Subchapter] C
RATIFICATION OF DEFECTIVE CORPORATE ACTIONS

§ 120. [Subchapter] definitions.
§ 121. Defective corporate actions.
§ 122. Ratification of defective corporate actions.
§ 123. Action on ratification.
§ 124. Notice requirements.
§ 125. Effect of ratification.
§ 126. Filings.

§ 120. [SUBCHAPTER] DEFINITIONS

In this [Subchapter], unless the context clearly indicates otherwise:

“Corporate action” means any action taken by or on behalf of a nonprofit corporation, including an action taken by the incorporator, the board of directors, a committee of the board of directors, a designated body, an officer, an agent of the corporation, or the members.

“Date of the defective corporate action” means the date (or the approximate date, if the exact date is unknown) the defective corporate action was purported to have been taken.

“Defective corporate action” means a corporate action purportedly taken that is, and at the time the corporate action was purportedly taken would have been, within the power of the nonprofit corporation, but is void or voidable due to a failure of authorization.

“Failure of authorization” means the failure to authorize, approve, or otherwise effect a corporate action in compliance with the provisions of this [Act], the articles of incorporation, or bylaws, a corporate resolution or other action of the board of directors or members, or any plan or agreement to which a nonprofit corporation is a party, if and to the extent the failure would render the corporate action void or voidable.
“Validation effective time” with respect to a defective corporate action ratified under this subchapter means the later of the time at which:

(1) one of the following occurs:

(i) the ratification of the defective corporate action is approved by the members;

(ii) if approval of members is not required, the time at which a notice under Section 124 (notice requirements) becomes effective in accordance with Section 103 (notice);

(iii) if approval of members is not required and notice is not given under Section 124 (notice requirements), the ratification of the defective corporate action is approved by the board of directors; and

(2) any articles of validation filed in accordance with Section 126 (filings) become effective.

Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.45.

CROSS-REFERENCES

Corporate powers, § 302.
Lack of power to act, § 304.

OFFICIAL COMMENT

The definitions of “corporate action,” “defective corporate action,” and “failure of authorization” are intentionally broad and permit ratification of any corporate action purportedly taken that would have been within the power granted to a nonprofit corporation under the act but as to which there is a question of its proper authorization.

§ 121. DEFECTIVE CORPORATE ACTIONS

(a) A defective corporate action shall not be void or voidable if ratified or validated in accordance with this [Subchapter].

(b) Ratification or validation under this [Subchapter] is not the exclusive means of ratifying or validating a defective corporate action. The absence or failure of ratification or validation in accordance with this [Subchapter] shall not:

(1) affect the validity or effectiveness of a corporate action otherwise properly ratified; or
create a presumption that a corporate action is or was:

(i) a defective corporate action; or

(ii) void or voidable.

Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.46.

CROSS-REFERENCES

Amendment of articles of incorporation or bylaws, Chapter 9.
“Corporate action” defined, § 120.
Correcting a filed record, § 164.
“Defective corporate action” defined, § 120.

OFFICIAL COMMENT

Subchapter 1C provides a statutory ratification procedure for corporate actions that may not have been properly authorized. The statutory ratification procedure is designed to supplement common law ratification.

Examples of defective corporate actions subject to ratification include the failure of the incorporator to validly appoint an initial board of directors, corporate action taken in the absence of board resolutions or other action of the board or members authorizing the action, and the failure to obtain the requisite member approval of a corporate action. The ratification procedure is intended to be available only where there is objective evidence that a corporate action was defectively authorized.

Section 121(a) does not distinguish between void and voidable actions. Instead it provides that any defective corporate action that is ratified in accordance with Subchapter 1C shall not be void or voidable. Subchapter 1C is not the exclusive means by which a defective corporate action may be ratified. Thus, the general common law doctrine of ratification, as applied to a board of directors’ adoption of actions taken by officers who may not have had the actual authority to take such actions, continues to be an effective mode of ratification. Section 121(b) makes clear that the nonprofit corporation’s ratification of a defective corporate action that is voidable but not void using common law methods of ratification rather than under Subchapter 1C will not, standing alone, affect the validity of the action or create a presumption that the action is not valid. In addition, ratification under Subchapter 1C is distinct from correction of an already filed record under Section 164.

§ 122. RATIFICATION OF DEFECTIVE CORPORATE ACTIONS

(a) To ratify a defective corporate action other than the ratification of an election of the initial board of directors under subsection (b), the board of directors shall take action ratifying the action in accordance with Section 123 (action on ratification), stating:
the defective corporate action to be ratified;

(2) the date of the defective corporate action;

(3) the nature of the failure of authorization with respect to the defective corporate action to be ratified; and

(4) that the board of directors approves the ratification of the defective corporate action.

(b) In the event that a defective corporate action to be ratified relates to the election of the initial board of directors or a designated body of the nonprofit corporation under Section 205(a)(2) (organization of corporation), a majority of the persons who, at the time of the ratification, are exercising the powers of directors may take an action stating:

(1) the name of the person or persons who first took action in the name of the corporation;

(2) the earlier of the date on which such persons first took such action or were purported to have been elected; and

(3) that the ratification of the election of such person or persons is approved.

(c) If any provision of this [Act], the articles of incorporation, bylaws, action of the board or directors or a designated body, plan, or agreement to which the nonprofit corporation is a party in effect at the time action under subsection (a) is taken requires member approval or would have required member approval at the date of the occurrence of the defective corporate action, the ratification of the defective corporate action approved in the action taken by the directors under subsection (a) shall be submitted to the members for approval in accordance with Section 123.

(d) Unless otherwise provided in the action taken by the board of directors under subsection (a), after the action by the board of directors has been taken and, if required, approved by the members, the board of directors may abandon the ratification at any time before the validation effective time without further action of the members.

Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.47.

CROSS-REFERENCES

“Date of the defective corporate action” defined, § 120.

“Defective corporate action” defined, § 120.

“Designated body” defined, § 102.

“Failure of authorization” defined, § 120.

Organization of corporation, § 205.
OFFICIAL COMMENT

Section 122(b) permits the ratification of the initial election of the board of directors or a designated body by the persons who are acting as the current board of directors, recognizing that if the nonprofit corporation’s initial board of directors was defectively appointed, there may be no effective method of ratification because a duly elected board of directors does not exist.

§ 123. ACTION ON RATIFICATION

(a) The quorum and voting requirements applicable to a ratifying action by the board of directors under Section 122(a) (ratification of defective corporate actions) shall be the quorum and voting requirements applicable to the corporate action proposed to be ratified at the time the ratifying action is taken.

(b) If the ratification of the defective corporate action requires approval by the members under Section 122(c), and if the approval is to be given at a meeting, the nonprofit corporation shall notify each member entitled to vote as of the record date for notice of the meeting. The notice must state that the purpose, or one of the purposes, of the meeting, is to consider ratification of a defective corporate action and must be accompanied by:

(1) either a copy of the action taken by the board of directors in accordance with Section 122(a) or the information required by Sections 122(a)(1) through (a)(4); and

(2) a statement that any claim that the ratification of the defective corporate action should not be effective, or should be effective only on certain conditions, shall be brought within 120 days after the applicable validation effective time.

(c) Except as provided in subsection (d) with respect to the voting requirements to ratify the election of a director, the quorum and voting requirements applicable to the approval by the members required by Section 122(c) shall be the quorum and voting requirements applicable to the corporate action proposed to be ratified at the time of the member approval.

(d) The approval by members to ratify the election of a director requires a majority of the votes cast within a voting group in favor of ratification or such greater vote as is required to elect directors at the time of ratification.

Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.48.

CROSS-REFERENCES

“Corporate action” defined, § 120.
“Defective corporate action” defined, § 120.
For matters other than the election of directors or a designated body, the quorum and voting requirements applicable to member approval of ratification are the quorum and voting requirements applicable to the corporate action being ratified at the time of such approval. For example, if the defective corporate action being ratified is an amendment to the articles of incorporation, the vote required would be governed by Section 904.

### § 124. NOTICE REQUIREMENTS

(a) Unless member approval is required under Section 122(c) (ratification of defective corporate actions), notice of an action taken under Section 122 may be given to each member entitled to vote as of the date of the action by the board of directors.

(b) If notice is given pursuant to subsection (a), the notice must contain:

1. either a copy of the action taken by the board of directors in accordance with Section 122(a) or (b) or the information required by Sections 122(a)(1) through (a)(4) or Sections 122(b)(1) through (b)(3), as applicable; and

2. a statement that any claim that the ratification of the defective corporate action should not be effective, or should be effective only on certain conditions, shall be brought within 120 days after the notice is effective under Section 103 (notice).

(c) No notice under this section is required with respect to any action required to be submitted to members for approval under Section 122(c).

*Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.49.*

### CROSS REFERENCES

Corporate records, § 401.
“Defective corporate action” defined, § 120.
Notices and other communications, § 103.

### OFFICIAL COMMENT

If member approval is not required under Section 122(c), notice to the members of action taken under Section 122 is optional.
§ 125. EFFECT OF RATIFICATION

(a) From and after the validation effective time, and without regard to the 120-day period during which a claim may be brought under Section 127 (judicial proceedings regarding validity of corporate actions):

(1) Each defective corporate action ratified in accordance with Section 122 (ratification of defective corporate actions) shall not be void or voidable as a result of the failure of authorization identified in the action taken under Section 122(a) or (b) and shall be deemed a valid corporate action effective as of the date of the defective corporate action.

(2) Any corporate action taken subsequent to the defective corporate action ratified in accordance with this [Subchapter] in reliance on the defective corporate action having been validly effected and any subsequent defective corporate action resulting directly or indirectly from the original defective corporate action shall be valid as of the time taken.

(b) The validation effective time shall not be affected by the filing or pendency of a judicial proceeding under Section 127 or otherwise, unless otherwise ordered by the court.

Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.50.

CROSS-REFERENCES

“Corporate action” defined, § 120.
“Date of the defective corporate action” defined, § 120.
“Defective corporate action” defined, § 120.
“Failure of authorization” defined, § 120.
“Validation effective time” defined, § 120.

OFFICIAL COMMENT

Ratification is effective as of the validation effective time and is not dependent on the expiration of the 120-day time period under Section 127(d) in which an action challenging the ratification must be brought. The ratification of a defective corporate action has the additional effect of ratifying corporate actions that are defective as a result of the original defective corporate action.

§ 126. FILINGS

(a) If a defective corporate action ratified under this [Subchapter] would have required the delivery of a record to the secretary of state for filing, then, regardless of whether a filing was previously made in respect of the defective corporate action and in lieu of a filing otherwise required by this [Act], the corporation shall deliver to the secretary of state for filing articles of validation in accordance with this section. The articles of validation shall amend or
substitute for the filing of any other record with respect to the defective corporate action required by this [Act].

(b) The articles of validation must set forth:

1. the defective corporate action that is the subject of the articles of validation;

2. the date of the defective corporate action;

3. the nature of the failure of authorization in respect of the defective corporate action;

4. a statement that the defective corporate action was ratified in accordance with Section 122 (ratification of defective corporate actions), including the date on which the board of directors ratified the defective corporate action and the date, if any, on which the members approved the ratification of the defective corporate action; and

5. if a filing was previously made in respect of the defective corporate action and no changes to the filing are required to give effect to the ratification of the defective corporate action in accordance with Section 122, the name, title, and filing date of the filing previously made and any articles of correction to that filing;

6. if a filing was previously made in respect of the defective corporate action and the filing requires any change to give effect to the ratification of the defective corporate action in accordance with Section 122:
   (i) the name, title and filing date of the filing previously made and any articles of correction to that filing; and
   (ii) a statement that a filing containing all of the information required to be included by this [Act] to give effect to the defective corporate action is attached as an exhibit to the articles of validation; and
   (iii) the date and time that the original filing became effective; and

7. if a filing was not previously made in respect of the defective corporate action and the defective corporate action ratified under Section 122 would have required a filing under this [Act]:
   (i) a statement that a filing containing all of the information required to be included by this [Act] to give effect to the defective corporate action is attached as an exhibit to the articles of validation; and
   (ii) the date and time that such filing is deemed to have become effective.
CROSS-REFERENCES

Correcting filed records, § 164.
“Date of the defective corporate action” defined, § 120.
“Defective corporate action” defined, § 120.
Effective time and date of filing, § 163.
“Failure of authorization” defined, § 120.

OFFICIAL COMMENT

Section 126 requires that the articles of validation have attached as an exhibit: (i) any filing that is or would have been required under the act to effect the defective corporate action (if no filing was previously made), or (ii) a corrected filing (if correction to a previous filing is required). If a filing was previously made and does not need to be corrected, the articles of validation must identify the previous filing. These requirements are intended to provide a clear public record of the actions relating to the ratification.

§ 127. JUDICIAL PROCEEDINGS REGARDING VALIDITY OF CORPORATE ACTIONS

(a) Upon application by a nonprofit corporation, any successor entity to the nonprofit corporation, a director of the corporation, a member of a designated body, a member, or any other person claiming to be substantially and adversely affected by a ratification under Section 122 (ratification of defective corporate actions), the [name or describe court] may:

(1) determine the validity and effectiveness of the corporate action or defective corporate action;
(2) determine the validity and effectiveness of any ratification under Section 122; and
(3) modify or waive any of the procedures specified in Section 122 or 123 (action on ratification) to ratify a defective corporate action.

(b) In connection with an action under this section, the court may make such findings or orders, and take into account any factors or considerations, regarding such matters as it deems proper under the circumstances.

(c) No party other than the nonprofit corporation need be joined in order for the court to adjudicate the matter. In an action filed by the nonprofit corporation, the court may require notice of the action be provided to other persons specified by the court and permit such other persons to intervene in the action.
(d) Notwithstanding any other provision of this section or otherwise under applicable law, any action asserting that the ratification of a defective corporate action should not be effective, or should be effective only on certain conditions, shall be brought within 120 days after the validation effective time.

Source Note: Cf. Model Business Corporation Act (2016 Revision), § 1.52.

CROSS-REFERENCES

“Corporate action” defined, § 120.
“Defective corporate action” defined, § 120.
“Validation effective time” defined, § 120.

OFFICIAL COMMENT

Section 127 confers plenary jurisdiction on a designated court to hear and determine claims regarding the validity of any corporate action. The court’s jurisdiction is not limited to reviewing corporate actions ratified or purportedly ratified under Subchapter 1C, and includes the ability of a nonprofit corporation or other permitted person to obtain a declaration regarding the validity of any corporate action. In acting under Section 127, the court may consider any factors or considerations it deems proper under the circumstances. These might include whether the person originally taking the defective corporate action believed that the action complied with corporate requirements, whether the corporation and board of directors has treated the defective corporate action as a valid action, whether any person has acted in reliance on the public record that such defective corporate action was valid and whether any person will be or was harmed by the ratification of the defective corporate action or will be harmed by the failure to ratify or validate the defective corporate action.

[Subchapter] D

RELIGIOUS CORPORATIONS

§ 130. Subordination to religious doctrine or polity, or canon law.

§ 130. SUBORDINATION TO RELIGIOUS DOCTRINE OR POLITY, OR CANON LAW

If religious doctrine or polity, or canon law governing the affairs of a nonprofit corporation is inconsistent with the provisions of this [Act] on the same subject, the religious doctrine or polity, or canon law shall control to the extent required by the Constitution of the United States or the Constitution of [name of state] or both.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.60.
CROSS-REFERENCES

“Nonprofit corporation” defined, § 102.

OFFICIAL COMMENT

As a result of history, policy, and constitutional principles, religious corporations are entitled to protections not available to business or other nonprofit corporations. Courts have been reluctant to interfere with the internal affairs of religious organizations. They will not decide between conflicting religious doctrine or determine the “true” faith. However, courts have often decided internal property disputes by applying neutral principles of contract or corporate law to organizational documents of religious organizations.

This reluctance is based in part on the First Amendment to the United States Constitution which provides: “Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof … .” The establishment clause applies to states, as does the free exercise clause. The act attempts to walk the thin line between the establishment clause and the free exercise clause. It allows religious corporations to be formed and gives them the same rights and privileges as other corporations. The act avoids interfering with the free exercise of religion by negating or allowing religious corporations to negate provisions of the act that might result in excessive entanglement in religious activities by the state. By limiting state intrusion, the act uses the least restrictive means to provide an orderly structure in which religious corporations can be formed and operate.

Section 130 is based on the recognition that some provisions of the act may conflict with religious doctrines or polity, or canon law protected by the United States Constitution or state constitutions. The exact scope of constitutional limitations is less than clear and is subject to debate. Section 130 overcomes this difficulty by providing that, to the extent religious doctrine or polity, or canon law applicable to a religious corporation sets forth provisions inconsistent with provisions of the act, the religious doctrine or polity, or canon law controls, but only to the extent required by the United States Constitution or applicable state constitutions.

While in one sense Section 130 simply states the obvious, it is helpful to remind those dealing with religious corporations that they must consider constitutional mandates. The approach of Section 130 also allows a case-by-case determination of difficult questions and automatically conforms the act to the opinions of the United States Supreme Court and applicable state courts.

[Subchapter] E [Optional]

ATTORNEY GENERAL

§ 140. Notice to attorney general. [Optional]

§ 140. NOTICE TO ATTORNEY GENERAL [Optional]
(a) The attorney general must be given notice of the commencement of any proceeding that this [Act] authorizes the attorney general to bring but that has been commenced by another person.

(b) Whenever any provision of this [Act] requires that notice be given to the attorney general before or after commencing a proceeding or permits the attorney general to commence a proceeding:

(1) if no proceeding has been commenced, the attorney general may take appropriate action including, but not limited to, seeking injunctive relief; and

(2) if a proceeding has been commenced by a person other than the attorney general, the attorney general, as of right, may intervene in such proceeding.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.70.

CROSS-REFERENCES

Derivative proceedings, § 509.
Dissolution:
  Judicial, § 1120.
  Voluntary, § 1102(g).
Removal of directors, § 809.
Ultra-vires, § 304.

OFFICIAL COMMENT

Section 140 is marked optional because an enacting state should consider whether the substance of Section 140 would be better placed with the other provisions of its law relating to the powers and duties of the attorney general. If that approach is taken, the state should consider whether a cross reference to that other statute should be added to this act.

Section 140(a) requires that the attorney general be given notice of any proceeding that could have been brought by the attorney general, but is commenced by another person. Section 140(b)(1) grants the attorney general independent authority to act when notice is required under Section 140(a) or any other provision of the act. This carries out the policy implicit in such notice requirements by specifically empowering the attorney general to protect the public interest when it may be adversely affected. Section 140(b)(2) permits the attorney general to intervene in any proceeding that the attorney general could have commenced but that was brought by another person, such as a director or member. To protect the public interest, the attorney general may either commence a proceeding or intervene in a proceeding commenced by another person who is authorized to do so.

This section does not detract from the jurisdiction the attorney general may otherwise have in states adopting this act.
§ 150. POWERS

The secretary of state has the power reasonably necessary to perform the duties required of the secretary of state by this [Act].


CROSS-REFERENCES

Administrative dissolution, Subchapter 11D.
Administrative termination of registration of foreign nonprofit corporation, § 1311.
Secretary of state’s filing duty, § 165.

OFFICIAL COMMENT

Section 150 is intended to grant the secretary of state the authority necessary for the efficient performance of the filing and other duties imposed by the act but is not intended to give the secretary of state general authority to establish public policy. The most important aspects of a modern nonprofit corporation statute relate to the creation and maintenance of relationships among persons interested in or involved with a corporation. These relationships should be a matter of concern to the parties involved and not subject to regulation or interpretation by the secretary of state. Further, even in situations where it is claimed that the corporation has been formed or is being operated for purposes that may violate the public policies of the state, the secretary of state generally should not be the governmental official that determines the scope of public policy through administration of the filing responsibilities under the act. Rather, the attorney general may seek to enjoin the illegal conduct or to dissolve involuntarily the offending corporation.

§ 151. RULES AND PROCEDURES

The secretary of state may:

(1) adopt rules to administer this [Act] in accordance with [this state’s administrative procedure act]; and
(2) prescribe procedures that are reasonably necessary to perform the duties required of the secretary of state under this [Act] and are not required by [this state’s administrative procedure act] to be adopted as rules.


OFFICIAL COMMENT

Section 151 grants the secretary of state the authority necessary for the efficient performance of the filing and other duties imposed by the act but is not intended as a grant of general authority to establish public policy. See Section 165(a) which makes clear that the duty of the secretary of state under the act is “ministerial.”

[Subchapter] G

FILING DOCUMENTS

§ 160. Filing requirements.
§ 161. Forms.
§ 162. Filing, service, and copying fees.
§ 163. Effective time and date of filing.
§ 164. Correcting a filed record.
§ 165. Filing duty of secretary of state.
§ 166. Refusal of secretary of state to file record.
§ 167. Evidentiary effect of certified copy of filed record.
§ 168. Certificate of existence or registration.
§ 169. Penalty for signing false record.

§ 160. FILING REQUIREMENTS

(a) To be filed by the secretary of state pursuant to this [Act], a record must be received by the secretary of state, comply with this [Act], and satisfy the following:

(1) The record must be required or permitted by this [Act].

(2) The record must be physically delivered in written form unless and to the extent the secretary of state permits electronic delivery of records.

(3) The words in the record must be in English, and numbers must be in Arabic or Roman numerals, but the name of the entity need not be in English if written in English letters or Arabic or Roman numerals.

(4) The record must be signed by or on behalf of a person authorized or required under this [Act] to sign the record.
(5) The record must state the name and capacity, if any, of each individual who signed it, either on behalf of the individual or the person authorized or required to sign the record, but need not contain a seal, attestation, acknowledgment, or verification.

(b) If law other than this [Act] prohibits the disclosure by the secretary of state of information contained in a record, the secretary of state shall file the record if the record otherwise complies with this [Act]. The secretary of state may redact the information, and shall do so at the request of the person delivering the record for filing.

(c) When a record is delivered to the secretary of state for filing, any fee required under this [Act] and any fee, tax, interest, or penalty required to be paid under this [Act] or law other than this [Act] must be paid in a manner permitted by the secretary of state or by that law.

(d) The secretary of state may require that a record delivered in written form be accompanied by an identical or conformed copy.


CROSS REFERENCES

“Electronic” defined, § 102.
“Record” defined, § 102.
“Sign” defined, § 102.

OFFICIAL COMMENT

A record must be in typewritten or printed form unless the secretary of state permits electronic delivery. The types of electronic delivery that may be used will be determined by the secretary of state. The text of the record must be in the English language, (except to the limited extent permitted by Section 160(a)(3).

The secretary of state is not authorized to prescribe forms (except to the extent permitted by Section 161) and as a result may not reject a record on the basis of form if it contains the information called for by the specific statutory requirement and meets the minimal formal requirements of this section.

To be filed a record must be signed by the appropriate person. Who is an appropriate person is specified in Section 104.

A record is not required to be acknowledged or verified as a condition for filing. On the other hand, many organizations, like lenders or title companies, may desire that specific records include acknowledgements, verifications, or seals. Section 160(a)(4) does not prohibit the addition of these forms of execution and their use is not intended to affect the eligibility of the record for filing.
A record must be filed by the secretary of state if it contains the information required by the act. In view of the very limited discretion granted to the secretary of state under Section 165(a), which defines the role of the secretary of state as “ministerial,” Section 167(d) provides that no presumption arises from the fact that the secretary of state has accepted or rejected a record for filing.

§ 161. FORMS

(a) The secretary of state may prescribe forms for:

1. an application for a certificate of existence or certificate of registration;
2. a registration statement for a foreign nonprofit corporation;
3. a statement of withdrawal by a foreign corporation; and
4. a transfer of registration statement by a foreign corporation.

(b) The secretary of state may require that use of the forms prescribed under subsection (a) is mandatory.

(c) The secretary of state may prescribe forms for records required or permitted to be delivered for filing under this [Act] in addition to those listed in subsection (a), but the use of those forms is not mandatory.


CROSS-REFERENCES

Annual report, § 421.
Certificate of existence or registration, § 168.
Filing requirements, § 160.
Foreign registration statement, § 1303.
Statement of withdrawal, § 1307.
Transfer of foreign registration statement, § 1310.

OFFICIAL COMMENT

The act does not vest the secretary of state with general authority to establish mandatory forms for use under the act. However, certain types of reports and requests for records may be processed efficiently only if uniform forms are used. The processing of applications for certificates of existence or registration, for example, may be handled more easily if specific information is located at specific places on the form. Similarly, processing of large-volume, largely routine filings is expedited if standardized forms are required. Also, the disclosure
requirements of the annual report may be administered on a systematic basis if a standardized form is mandated. Section 161(a) recognizes that these considerations may exist in limited cases.

§ 162. FILING, SERVICE, AND COPYING FEES

Alternative A

(a) The secretary of state shall collect the following fees when the records described in this subsection are delivered to the secretary of state for filing:

<table>
<thead>
<tr>
<th>DOCUMENT</th>
<th>FEE</th>
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<tbody>
<tr>
<td>(1) Articles of incorporation</td>
<td>$___.</td>
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<tr>
<td>(2) Application for use of indistinguishable name</td>
<td>$___.</td>
</tr>
<tr>
<td>(3) Application for reserved name</td>
<td>$___.</td>
</tr>
<tr>
<td>(4) Notice of transfer of reserved name</td>
<td>$___.</td>
</tr>
<tr>
<td>(5) Application for registered name</td>
<td>$___.</td>
</tr>
<tr>
<td>(6) Application for renewal of registered name</td>
<td>$___.</td>
</tr>
<tr>
<td>(7) Corporation’s statement of change of registered agent or</td>
<td>$___.</td>
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<tr>
<td>registered office or both</td>
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<tr>
<td>(8) Agent’s statement of change of registered office for each</td>
<td>$___.</td>
</tr>
<tr>
<td>affected corporation, not to exceed a total of $_____</td>
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</tr>
<tr>
<td>(9) Agent’s statement of resignation</td>
<td>No fee.</td>
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<tr>
<td>(10) Articles of domestication</td>
<td>$___.</td>
</tr>
<tr>
<td>(11) Articles of conversion</td>
<td>$___.</td>
</tr>
<tr>
<td>(12) Amendment of articles of incorporation</td>
<td>$___.</td>
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<tr>
<td>(13) Restatement of articles of incorporation with amendment</td>
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<tr>
<td>of articles</td>
<td></td>
</tr>
<tr>
<td>(14) Articles of merger or interest exchange</td>
<td>$___.</td>
</tr>
<tr>
<td>(15) Articles of dissolution</td>
<td>$___.</td>
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</tbody>
</table>
Articles of revocation of dissolution
Certificate of administrative dissolution
No fee.
Application for reinstatement following administrative dissolution
Certificate of reinstatement
No fee.
Certificate of judicial dissolution
No fee.
Foreign registration statement
$___.
Amendment of foreign registration statement
authority
$___.
Statement of withdrawal
$___.
Transfer of registration statement
$___.
Annual report
$___.
Articles of correction
$___.
Application for certificate of existence or authorization
$___.
Any other document required or permitted to be filed by this [Act]
$___.
(b) The secretary of state shall collect a fee of $______ each time process is served on the secretary of state under this [Act]. The party to a proceeding causing service of process may recover this fee as costs if that party prevails in the proceeding.
(c) The secretary of state shall collect the following fees for copying and certifying the copy of any record filed under this [Act]:
(1) $______ a page for copying; and
(2) $______ for the certificate.

Alternative B

The secretary of state shall promulgate rules, in accordance with the [state’s administrative procedure act], setting fees for filings and services by the secretary of state under this [Act].
OFFICIAL COMMENT

Alternative A

Section 162 establishes in a single section the filing fees for all records that may be filed under the act. The dollar amounts for each record should be inserted by each state as it adopts the act.

The list of records in Section 162(a) includes all records that are authorized to be filed with the secretary of state under the act. The catch-all in the last item of the list will apply to any record for which a state does not establish a specific filing fee.

Section 162(a)(8) relating to a registered agent’s statement of change of registered office contains a maximum fee for filing a change of address of a registered agent. Since corporation service companies serve as registered agents for thousands of corporations in many jurisdictions, their change of address may require a very large number of filings. The fee is broadly based on the number of corporations affected but a maximum fee is specified to reflect that as the number of changes increases the cost per change should decrease.

Alternative B

As an alternative to having the legislature establish the fee schedule for filings under the act, Alternative B gives the secretary of state the authority to set those fees.

§ 163. EFFECTIVE TIME AND DATE OF FILING

Except as provided in Section 164(c) (correcting filed record) or [Subchapter] C (ratification of defective corporate actions), a record accepted for filing is effective:

(1) on the date and at the time of filing, as provided in Section 165(b) (filing duty of secretary of state);

(2) on the date of filing and at the time specified in the record as its effective time if later than the time specified in paragraph (1);

(3) at a specified delayed effective date and time which may not be more than 90 days after the date of filing; or

(4) if a delayed effective date is specified, but no time is specified, at 12:01 a.m. on the date specified, which may not be more than 90 days after the date of filing.
CROSS-REFERENCES

“Effective date” defined, § 102.
Filing requirements, § 160.

OFFICIAL COMMENT

Section 163 provides definitive rules governing when a filed record becomes effective. The definition of effective date in Section 102 ties in with this section so that throughout the act the term “effective date” of a filed record means the effective date and time determined pursuant to Section 163. The act does not generally distinguish between the effective date of a filed record and the effectiveness of the transaction that is the subject of the record. However, in a few instances where filings in more than one jurisdiction are required, the act distinguishes between the effective date of the record and the effectiveness of the transaction that is the subject of the record. See Sections 1225, 1243, and 1253 regarding certain mergers, domestications, and conversions.

Section 103 deals with the effectiveness of notices and other communications and does not use or define the term “effective date.”

Section 163 does not authorize or contemplate the establishment of a retroactive effective date that is prior to the date of filing.

§ 164. CORRECTING FILED RECORD

(a) A record filed by the secretary of state under this [Act] may be corrected if:

(1) the record at the time of filing was inaccurate;
(2) the record was defectively signed; or
(3) the electronic transmission of the record to the secretary of state was defective.

(b) To correct a filed record, a person on whose behalf the record was delivered to the secretary of state must deliver articles of correction to the secretary of state for filing.

(c) Articles of correction:

(1) may not state a delayed effective date;
(2) must be signed by the person correcting the filed record;
must identify the filed record to be corrected;

(4) must specify the inaccuracy or defect to be corrected; and

(5) must correct the inaccuracy or defect.

(d) Articles of correction are effective on the effective date of the filing they correct except as to persons relying on the uncorrected filing and adversely affected by the correction. As to those persons, articles of correction are effective when filed.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.24. Cf. Model Business Corporation Act (2016 Revision), § 1.24. Subsections (b) and (c) patterned after Uniform Business Organizations Code (2011) (Last Amended 2013) § 1-205(b) and (c).

CROSS-REFERENCES

Delivery defined, § 103.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing requirements, § 160.

OFFICIAL COMMENT

Section 164 permits making corrections in filed records without refiling the entire record or submitting formal articles of amendment. This correction procedure has the advantage that articles of correction do not alter the effective date of the underlying filing being corrected. Indeed, under Section 164(d), the correction relates back to the original effective date of the filing except as to persons relying on the original filing and adversely affected by the correction. As to these persons, the effective date of articles of correction is the date the articles are filed.

A provision in a filing setting an effective date under Section 163 may be corrected under this section, but the corrected effective date must comply with Section 163 measured from the date of the original filing being corrected, i.e., it cannot be before the date of the original filing or more than 90 days thereafter.

§ 165. FILING DUTY OF SECRETARY OF STATE

(a) If a record delivered to the secretary of state for filing satisfies the requirements of Section 160 (filing requirements), the secretary of state must file it. The duty of the secretary of state to file records under this section is ministerial.
(b) The secretary of state files a record by recording it as filed on the date and time of receipt. After filing a record, the secretary of state shall return to the person who delivered the record for filing a copy of the record with an acknowledgement of the date and time of filing.

(c) If the secretary of state refuses to file a record, it shall be returned to the person who delivered the record for filing within five days after the record was delivered, together with a brief explanation in a record of the reason for the refusal.

(d) The filing or refusal to file a record by the secretary of state does not create a presumption that:

1. the record does or does not conform to the requirements of this [Act]; or
2. that information contained in the record is correct or incorrect.


CROSS-REFERENCES

Appeal from refusal to file document, § 166.
Effective time and date of filing, § 163.
Filing requirements, § 160.
Powers of secretary of state, § 150.

OFFICIAL COMMENT

Section 165 limits the secretary of state to a ministerial role in reviewing the contents of records. If the record submitted contains the information required by Section 160 and the applicable provision of the act (and if a mandatory form has been prescribed under Section 161(a), the record is in that form), the secretary of state under Section 165 must file it even though it contains additional provisions the secretary of state may believe are irrelevant or not authorized by the act or by general legal principles. Persons adversely affected by provisions in a record may test their validity in a proceeding appropriate for that purpose. Similarly, the attorney general of the state may also question the validity of provisions of records accepted for filing by the secretary of state in an independent suit brought for that purpose. In neither case should any presumption or inference be drawn about the validity of a provision from the fact that the secretary of state accepted the document for filing.

§ 166. RESPONSE TO REFUSAL OF SECRETARY OF STATE TO FILE RECORD

(a) If the secretary of state refuses to file a record delivered for filing, the record may be resubmitted accompanied by an opinion in a record from a lawyer admitted to practice in this state stating why the record conforms to law and the authorities upon which the opinion is based.
The secretary of state may rely with respect to any disputed point of law upon the opinion in determining whether the record conforms to law.

(b) If the secretary of state refuses to file a record delivered for filing, and as an alternative to resubmitting the record under subsection (a), or following a refusal to file the record after it is resubmitted under subsection (a), the person on whose behalf the record was delivered to the secretary of state may petition the [name or describe] court [of the county where the entity’s principal office (or, if none in this state, its registered office) is or will be located] [of county] to compel its filing. The record and the explanation of the secretary of state of the refusal to file must be attached to the petition. The court may:

(1) decide the matter in a summary proceeding; and

(2) order the secretary of state to file the record or take other action the court considers appropriate.

(c) The final decision of the court may be appealed as in other civil proceedings.


CROSS-REFERENCES

“Delivery” defined, § 102.
Filing fees, § 162.
Filing requirements, § 160.
Secretary of state’s filing duty, § 165.

OFFICIAL COMMENT

The identity of the specific court with jurisdiction to hear appeals from the secretary of state under Section 166(b) must be supplied by each state when enacting this section. The court may be one of general civil jurisdiction or relevant specialized jurisdiction. Other sections of the act also contemplate that the court with jurisdiction over substantive corporate matters will be designated in the statute. See, for example, Section 703, relating to the ordering of a members meeting after the corporation fails to hold such a meeting.

The phrase “summary proceeding” in Section 166(b)(1) refers to a class of cases where the court takes action on an expedited basis and decides the case on a limited record given the narrowness of the issues involved. See Section 165.

The act does not address either the burden of proof or the standard for review in judicial proceedings challenging action of the secretary of state. It is contemplated that these matters will be governed by general principles of judicial review of agency action.
§ 167. EVIDENTIARY EFFECT OF CERTIFIED COPY OF FILED RECORD

A certificate from the secretary of state delivered with a copy of a record filed by the secretary of state is conclusive evidence that the original record is on file with the secretary of state.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 1.27. Cf. Model Business Corporation Act (2016 Revision), § 1.27.

CROSS-REFERENCES

Certifying fee, § 162.

OFFICIAL COMMENT

The secretary of state may be requested to certify that a specific record has been filed with the secretary of state upon payment of the fee under Section 162. The limited effect of the certificate is consistent with the ministerial filing obligation imposed on the secretary of state under the act.

§ 168. CERTIFICATE OF EXISTENCE OR REGISTRATION

(a) Any person may apply to the secretary of state to furnish a certificate of existence for a domestic nonprofit corporation or a certificate of registration for a registered foreign nonprofit corporation.

(b) A certificate of existence shall set forth:

1. the corporate name of the domestic nonprofit corporation;
2. that the domestic corporation is duly incorporated under the law of this state, the date of its incorporation, and the period of its duration if less than perpetual;
3. that all fees, taxes, and penalties owed to this state have been paid, if:
   i. payment is reflected in the records of the secretary of state, and
   ii. nonpayment affects the existence of the domestic corporation;
4. that the most recent annual report of the domestic corporation required by Section 16.21 has been filed with the secretary of state;
5. that articles of dissolution have not been filed;
that the domestic corporation is not administratively dissolved and a proceeding is not pending under Section 1141 (procedure for administrative dissolution); and

other facts of record in the office of the secretary of state that may be requested by the applicant.

(c) A certificate of registration shall set forth:

(1) the name under which the foreign nonprofit corporation is registered in this state;

(2) that the foreign corporation is registered to do business in this state;

(3) that all fees, taxes, and penalties owed to this state have been paid, if

(i) payment is reflected in the records of the secretary of state, and

(ii) nonpayment affects the registration of the foreign corporation;

(4) that the most recent annual report of the foreign corporation required by Section 421 (annual report for secretary of state) has been filed with the secretary of state; and

(5) other facts of record in the office of the secretary of state that may be requested by the applicant.

(c) Subject to any qualification stated in the certificate, a certificate of existence or registration issued by the secretary of state may be relied upon as conclusive evidence of the facts stated in the certificate.


CROSS-REFERENCES

Fees, § 162.
Forms, § 161.

OFFICIAL COMMENT

Section 168 establishes a procedure by which anyone may obtain a conclusive certificate from the secretary of state that a particular domestic or foreign nonprofit corporation is in existence or is registered to conduct activities in the state. The secretary of state is to make the judgment whether or not the corporation is in existence or is registered to conduct activities from public records only and is not expected to make a more extensive investigation. In appropriate cases, the secretary of state may issue a certificate subject to specified qualifications.
Section 168(b)(3) refers only to fees, taxes, or penalties the payment of which is reflected in the records of the secretary of state. Those fees, taxes, and penalties include those collected by the secretary of state or collected by other agencies and reported to the secretary of state. In some states the secretary of state may ascertain from other agencies that other fees, taxes, or penalties have been paid and include this information in the certificate. In states where this procedure does not unduly delay the issuance of certificates, Section 168 may be revised appropriately. Section 168(b)(3) relates only to fees, taxes, or penalties to the extent their nonpayment affects the existence or authorization to conduct activities of the corporation.

§ 169. PENALTY FOR SIGNING FALSE RECORD

(a) Signing a record delivered to the secretary of state for filing is an affirmation under the penalties of perjury that the facts stated in the filing are true in all material respects.

(b) A record filed under this [Act] may be signed by an agent. Whenever this [Act] requires a particular individual to sign a record and the individual is deceased or incompetent, the filing may be signed by a legal representative of the individual.

(c) A person that signs a record as an agent or legal representative affirms as a fact that the person is authorized to sign the record.

Source Note:
Subsections (b) and (c): Uniform Business Organizations Code (2011) (Last Amended 2013), § 1-209(b) and (c).

CROSS-REFERENCES

“Sign” defined, § 102.

OFFICIAL COMMENT

The secretary of state should not check the bona fides of a person purporting to have signed a record in a representative capacity. Section 169 expressly authorizes taking action through an agent so as to provide context for Section 169(c) and for the avoidance of doubt. No negative inference should be drawn about using agents to take other action under the act.

[CHAPTER] 2
INCORPORATION

Subchapter
A. Incorporation Generally
B. Name
C. Registered Office and Agent

[Subchapter] A

INCORPORATION GENERALLY

§ 201. Incorporators.

One or more persons may act as the incorporator or incorporators of a nonprofit corporation by delivering articles of incorporation to the secretary of state for filing.


CROSS-REFERENCES

Articles of incorporation, § 202.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing and signature requirements, § 160.
Organization of corporation by incorporators, § 205.
“Person” defined, § 102.

OFFICIAL COMMENT

The only functions of incorporators under the act are (i) to sign the articles of incorporation, (ii) to deliver them to the secretary of state for filing, and (iii) to complete the formation of the nonprofit corporation to the extent set forth in Section 205. “Person” is defined in Section 102 and includes both individuals and entities.

The act does not require that articles of incorporation be acknowledged or verified. See the Official Comment to Section 160 with respect to execution and filing requirements.

§ 202. ARTICLES OF INCORPORATION

(a) The articles of incorporation must set forth:
(1) a name for the nonprofit corporation that satisfies the requirements of Section 210 (corporate name);

(2) the street address of the corporation’s initial registered office and the name of its initial registered agent at that office;

(3) that the corporation is incorporated under this [Act]; and

(4) the name of each incorporator.

(b) The articles of incorporation may set forth:

(1) the names of the individuals who are to serve as the initial directors;

(2) provisions creating one or more designated bodies;

(3) the names of the initial members of a designated body;

(4) whether the corporation will have members;

(5) the names of the initial members, if any;

(6) provisions not inconsistent with law regarding:

(i) the purpose or purposes for which the nonprofit corporation is organized;

(ii) managing the activities and regulating the affairs of the corporation;

(iii) defining, limiting, and regulating the powers of the corporation, its board of directors, any designated body, and the members, if any;

(iv) the characteristics, qualifications, rights, limitations, and obligations attaching to each or any class of members;

(v) abolishing or limiting a member’s right to inspect and copy the records of the corporation under Section 402(b) (inspection rights of members); or

(vi) the distribution of assets on dissolution;

(7) any provision that this [Act] requires or permits to be set forth in the bylaws;
(8) a provision permitting or making obligatory indemnification of a director for liability (as defined in Section 850 ([Subchapter] definitions)) to any person for any action taken, or any failure to take any action, as a director, except liability for:

(i) receipt of a financial benefit to which the director is not entitled;

(ii) an intentional infliction of harm;

(iii) a violation of Section 832 (directors’ liability for unlawful distributions); or

(iv) an intentional violation of criminal law;

(9) provisions required if the corporation is to be exempt from taxation under federal, state, or local law; and

(10) a provision limiting or eliminating any duty of a director or any other person to offer the corporation the right to have or participate in any, or one or more classes or categories of, business opportunities, before the pursuit or taking of the opportunity by the director or other person; but the application of such a provision to an officer or affiliate of that officer:

(i) also requires approval of that application by the board of directors, subsequent to the effective date of the provision, by action of the disinterested directors; and

(ii) may be limited by the authorizing action of the board.

(c) The liability of a director of a nonprofit corporation that is not a charitable corporation may be eliminated or limited by a provision of the articles of incorporation that a director shall not be liable to the corporation or its members for money damages for any action taken, or any failure to take any action, as a director, except liability for:

(1) the amount of a financial benefit received by the director to which the director is not entitled;

(2) an intentional infliction of harm;

(3) a violation of Section 832; or

(4) an intentional violation of criminal law.

(d) The articles of incorporation need not set forth any of the corporate powers enumerated in this [Act].
(e) Provisions of the articles of incorporation may be made dependent upon facts objectively ascertainable outside the articles of incorporation in accordance with Section 105 (extrinsic facts in filed record).

(f) See Sections 301(a) (purposes), 831(d) (standards of liability for directors) and 858(c) (variation of indemnification).


CROSS-REFERENCES

Amendment of articles, Ch. 9A.
Bylaws, § 206 and Ch. 9B.
Duration of corporate existence, § 302.
Filing fees, § 162.
Filing and signature requirements, § 160.
Incorporators, § 201.
Indemnification, Subch. 8E.
Powers, § 302.
Purposes, § 301.
Restated articles, § 907.

OFFICIAL COMMENT

1. Introduction

A nonprofit corporation will have perpetual duration unless a provision is included in its articles of incorporation providing for a shorter period. See Section 302. Similarly, a corporation with articles of incorporation which do not contain a purpose clause will have the purpose of engaging in any lawful business under Section 301(a). The option of providing a narrower purpose clause is also preserved in Sections 202(b)(2)(i) and 301, with the effect described in the Official Comment to Section 301.

2. Requirements

The nonprofit corporation’s initial registered office and agent must be included, and a mailing address alone, such as a post office box, is not sufficient because the registered office is the designated location for service of process. See Section 223.

No reference need be made to a variety of other matters. Generally, no substantive effect should be given to the absence of a specific reference to such matters in Section 202 because these matters are referred to in other sections of the act that usually provide an “opt in” privilege.

Nonprofit corporations may be required to comply with requirements outside the act. For example, charitable corporations must comply with additional requirements imposed under other
provisions of law such as Section 501(c)(3) of the Internal Revenue Code which requires that a 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.


Section 202(b) allows the articles of incorporation to contain optional provisions deemed sufficiently important to be of public record or subject to amendment only by the processes applicable to amendments of articles of incorporation.

A. CORPORATE POWERS

Section 202(b) makes it unnecessary to set forth any corporate powers in the articles of incorporation in view of the broad grant of power in Section 302. This grant of power, however, may be overbroad for particular nonprofit corporations; if so, it may be qualified or narrowed by appropriate provisions in the articles of incorporation.

B. PURPOSE CLAUSE

Under Section 202(b)(6)(i), a nonprofit corporation may elect a limited purpose clause or provide for specific purposes without limiting the broad purposes provided in Section 301. Specific purposes may be needed, among other reasons, for registration in certain foreign jurisdictions, to obtain tax-exempt status, or to obtain licenses.

C. MANAGEMENT OF THE CORPORATION GENERALLY

Under Section 202(b)(6)(ii) and (iii) a nonprofit corporation may include any provision not inconsistent with law for “managing the business and regulating the affairs of the corporation” and “defining, limiting, and regulating the powers of the corporation, its board of directors, any designated body, and the members.” This language is designed to allow the corporation to place in the articles any number of miscellaneous provisions that it considers sufficiently important to be of public record or, in the case of a membership corporation, subject to amendment only by the processes applicable to amendments of articles of incorporation which generally require member approval.

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 801. In recent years the oversight function of the board has become increasingly prominent. References throughout the act to the management of the affairs of a corporation, such as in Section 202(b)(6)(ii), include the oversight function of the board.

E. DIRECTOR LIABILITY

Section 202(c) authorizes the inclusion of a provision in the articles of incorporation of a nonprofit corporation that is not a charitable corporation eliminating or limiting, with certain exceptions, the liability of the directors to the corporation or its members for money damages.
Section 202(c) is optional rather than self-executing and does not apply to equitable relief.
Likewise, nothing in Section 202(c) in any way affects the right of the members to remove
directors, under Section 808(a), with or without cause. The phrase “as a director” emphasizes
that Section 202(c) applies to a director’s actions or failures to take action in the director’s
capacity as a director and not in any other capacity, such as officer, employee, or controlling
member. However, it is not intended to exclude coverage of conduct by individuals, even though
they are also officers, employees, or controlling members, to the extent they are acting in their
capacity as directors.

Section 202(c) only applies to nonprofit corporations that are not charitable corporations.
Inclusion of the type of provision authorized by Section 202(c) in the articles of incorporation of
a charitable corporation is not necessary because the same liability shield is provided for
directors of a charitable corporation by Section 831(d).

The statutory exceptions to permitted limitations of director liability are few and narrow
and are discussed below.

Financial Benefit

Transactions from which a director could benefit personally are subject to special
scrutiny. The financial benefits exception under Section 202(c) is limited to the amount of the
benefit actually received. Thus, liability for punitive damages could be eliminated, except in
cases of intentional infliction of harm or for violation of criminal law (as described below)
where, in a particular case (for example, theft), punitive damages may be available. The benefit
must be financial rather than in less easily measured and more conjectural forms, such as
business goodwill, personal reputation, or social ingratiation. The phrase “received by a director”
is not intended to be a “bright line.” As a director’s conduct moves toward the edge of what may
be exculpated, the director should bear the risk of miscalculation. Depending upon the
circumstances, a director may be deemed to have received a benefit that the director caused to be
directed to another person, for example, a relative, friend, or affiliate.

What constitutes a financial benefit “to which the director is not entitled” is left to
judicial development. For example, a director may receive reasonable compensation for the
performance of services; on the other hand, a director is not entitled to the profits from a
corporate opportunity improperly taken by the director. See section 870 as to procedures for
disclaiming the nonprofit corporation’s interest in a business opportunity by action of
disinterested directors or members.

Intentional Infliction of Harm

There may be situations in which a director intentionally causes harm to the nonprofit
corporation even though the director does not receive any improper benefit. The use of the word
“intentional,” rather than “knowing,” is meant to refer to the specific intent to perform, or fail to
perform, the acts with actual knowledge that the director’s action, or failure to act, will cause
harm, rather than a general intent to perform the acts which cause the harm.
Unlawful Distributions

Section 832(a) indicates a strong policy in favor of liability for unlawful distributions approved by directors who have not complied with the standards of conduct of Section 830. Accordingly, the exception in Section 202(c)(iii) prohibits the members and directors from eliminating or limiting the liability of directors for a violation of Section 832.

Intentional Violation of Criminal Law

Even though a director committing a crime may intend to benefit the nonprofit corporation, the members and directors should not be permitted to exculpate the director for any harm caused by an intentional violation of criminal law, including, for example, fines and legal expenses of the corporation in defending a criminal prosecution. The use of the word "intentional," rather than "knowing," is meant to refer to the specific intent to perform, or fail to perform, the acts with actual knowledge that the director’s action, or failure to act, constitutes a violation of criminal law.

F. DIRECTOR INDEMNIFICATION

Section 202(b)(8) specifically prohibits provisions for indemnification of director liability arising out of improper financial benefit received by a director, an intentional infliction of harm on the nonprofit corporation or the members, an unlawful distribution or an intentional violation of criminal law. These excepted liabilities parallel those a corporation is not permitted to limit or eliminate under Section 202(c). Officers are not included in the language of Section 202(b)(5) because the expansion of indemnification for directors that section permits must be set forth in the articles of incorporation as required by Section 851(a)(2). Section 856 allows a similar expansion of indemnification for officers to be set forth also in the bylaws, an action of the board of directors or members, or contracts.

Unlike the liability shield provided automatically for directors of a charitable corporation by Section 831(d), the act does not automatically provide for indemnification of directors of a charitable corporation. Thus, the option of taking advantage of Section 202(b)(8) should be evaluated by both charitable corporations and other nonprofit corporations.

G. BUSINESS OPPORTUNITIES

Section 202(b)(10) authorizes the inclusion of a provision in the articles of incorporation to limit or eliminate, in advance, the duty of a director or other person to bring a business opportunity to the nonprofit corporation. The limitation or elimination may be blanket in nature and apply to any business opportunities, or it may extend only to one or more specified classes or categories of business opportunities. The adoption of such a provision constitutes a curtailment of the duty of loyalty which includes the doctrine of corporate opportunity. If such a provision is included in the articles, taking advantage of a business opportunity covered by the provision of the articles without offering it to the corporation will not expose the director or other person to whom it is made applicable either to monetary damages or to equitable or any other relief in favor of the corporation upon compliance with the requirements of Section 202(b)(10).
Section 202(b)(10) also permits extension of the limitation or elimination of the duty to any other persons who might be deemed to have a duty to offer business opportunities to the nonprofit corporation. For example, courts have held that the corporate opportunity doctrine extends to officers of the corporation. Although officers may be included in a provision under this Section 202(b)(10), the limitation or elimination of corporate opportunity obligations of officers must be addressed by the board of directors in specific cases or by the directors’ authorizing provisions in employment agreements or other contractual arrangements with such officers. Accordingly, Section 202(b)(10) requires that the application of an advance limitation or elimination of the duty to offer a business opportunity to the corporation to any person who is an officer of the corporation or a related person of an officer also requires action by the board of directors acting through disinterested directors. This action must be taken subsequent to the inclusion of the provision in the articles of incorporation and may limit the application. This means that if the advance limitation or elimination of the duty of an officer to offer business opportunities to the corporation is included in the articles by an amendment recommended by the directors and approved by the members, if any, that recommendation of the directors does not serve as the required authorization by disinterested directors; rather, separate authorization by disinterested directors after the amendment is included in the articles is necessary to apply the provision to a particular officer or any related person of that officer.

Whether a provision for advance limitation or elimination of duty in the articles of incorporation should be a broad “blanket” provision or one more tailored to specific categories or classes of transactions deserves careful consideration given the particular circumstances of the nonprofit corporation.

4. Provisions That May Be Elected Only in the Articles of Incorporation

Unlike the pattern of many business corporation laws which provide that provisions on certain subjects can be placed either in the articles of incorporation or bylaws while provisions on other subjects can be placed only in the articles, the act permits most subjects to be addressed in either the articles or bylaws of a nonprofit corporation. The only subjects that may be addressed only in the articles and not in the bylaws are as follows:

- Limitation and elimination of liability of a director of nonprofit corporation that is not a charitable corporation. See Section 202(c).
- Limitations on the purposes of a nonprofit corporation. See Section 301.
- Limitations on the powers of a nonprofit corporation. See Section 302.
- Relinquishment by a nonprofit corporation of its rights to business opportunities. See Section 870.

§ 203. INCORPORATION
(a) Unless a delayed effective date is specified, the corporate existence begins when the articles of incorporation are filed.

(b) The filing of the articles of incorporation by the secretary of state is conclusive proof that the incorporators satisfied all conditions precedent to incorporation except in a proceeding by the state to cancel or revoke the incorporation or involuntarily dissolve the nonprofit corporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 2.03. Cf. Model Business Corporation Act (2016 Revision), § 2.03.

CROSS-REFERENCES

Duration, § 302.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing requirements, § 160.
Secretary of state’s filing duty, § 165.

OFFICIAL COMMENT

Section 203(a) fixes the beginning of corporate existence as the date and time the articles of incorporation are filed by the secretary of state, as provided in Section 163, unless the articles provide that the nonprofit corporation’s existence will begin at a time later than the time of filing, to the extent permitted by Section 163.

Under Section 203(b) the filing of the articles of incorporation is conclusive proof that all conditions precedent to incorporation have been met, except in specified proceedings brought by the state.

See Chapter 1, which contains rules for the filing and effective dates of documents, all of which are applicable to articles of incorporation and other documents.

§ 204. LIABILITY FOR PREINCORPORATION TRANSACTIONS

All persons purporting to act as or on behalf of a nonprofit corporation, knowing there was no incorporation under this [Act], are jointly and severally liable for all liabilities created while so acting.


CROSS-REFERENCES
OFFICIAL COMMENT

The filing of articles of incorporation establishes that a nonprofit corporation has been formed with its attendant liability protections.

The act imposes liability only on persons who act as or on behalf of a nonprofit corporation “knowing” that no corporation exists. In addition, Section 204 does not foreclose the possibility that persons who urge defendants to execute contracts in the corporate name knowing that no steps to incorporate have been taken may be estopped to impose personal liability on individual defendants. This estoppel may be based on the inequity perceived when persons, unwilling or reluctant to enter into a commitment under their own name, are persuaded to use the name of a nonexistent corporation, and then are sought to be held personally liable under Section 204 by the party advocating execution in the name of the corporation.

§ 205. ORGANIZATION OF CORPORATION

(a) After incorporation:

(1) if initial directors or members of a designated body are named in the articles of incorporation, those persons shall hold an organizational meeting, as appropriate, to complete the organization of the nonprofit corporation by electing directors (when the organization of the corporation is to be completed by a designated body), appointing officers, adopting bylaws, and carrying on any other business brought before the meeting;

(2) if initial directors or members of a designated body are not named in the articles, the incorporator or incorporators shall hold an organizational meeting to:

   (i) elect directors and, when appropriate, a designated body, and complete the organization of the nonprofit corporation; or

   (ii) elect a board of directors and, when appropriate, a designated body, who shall complete the organization of the corporation.

(b) Action required or permitted by this [Act] to be taken by incorporators at an organizational meeting may be taken without a meeting if the action taken is evidenced by one or more consents in a record describing the action taken and signed by each incorporator.

(c) An organizational meeting may be held in or out of this state.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 2.05. Cf: Model Business Corporation Act (2016 Revision), § 2.05.
OFFICIAL COMMENT

Following incorporation, the organization of a new nonprofit corporation must be completed so that it may engage in its activities. This usually requires adoption of bylaws, the appointment of officers and agents, the election of a board of directors, and, when appropriate, a designated body.

Section 205 allows alternative methods of completing the organization of the nonprofit corporation. First, Section 205(a)(1) contemplates that if initial directors or members of a designated body are named in the articles of incorporation, the persons so named will organize the corporation. It is expected that these persons will be named only if they will remain in office and there is no objection to the disclosure of their identity in the articles of incorporation. Second, Section 205(a)(2) provides that the incorporators may themselves complete the organization, or they may simply meet to elect a board of directors and, when appropriate, a designated body who are then to complete the organization.

Section 205(b) and (c) is limited to meetings of incorporators. Sections 821 and 822 permit organizational actions to be taken by the board of directors. If a meeting of members is necessary, Sections 701 and 704 give them the same flexibility that is given incorporators under Sections 205(b) and (c).

The provisions of Section 205(a)(2) also apply to a designated body under Section 812. Thus if neither directors nor members of a designated body are named in the articles of incorporation, Section 205(a)(2) will permit a designated body to hold an organizational meeting to complete whatever steps in the organization of the nonprofit corporation require action by the designated body.

An organizational action by the incorporators, the board of directors, or a designated body may be taken without a meeting, if the action taken is evidenced by one or more signed consents in a record describing the action taken.

§ 206. BYLAWS

(a) The incorporator or incorporators or the board of directors of a nonprofit corporation may adopt initial bylaws for the corporation.
(b) The bylaws of a nonprofit corporation may contain any provision for managing the activities and regulating the affairs of the corporation that is not inconsistent with law or the articles of incorporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 2.06. Cf. Model Business Corporation Act (2016 Revision), § 2.06(a) and (b).

CROSS-REFERENCES

Amendment of bylaws, Subch. 9B.
Organizing corporation, § 205.

OFFICIAL COMMENT

The responsibility for adopting the original bylaws is placed on the person or persons completing the organization of the nonprofit corporation. The powers of the board of directors under this section may be exercised by a designated body pursuant to Section 812.

The power to amend or repeal bylaws, or adopt new bylaws after the organization of the nonprofit corporation is completed, is addressed in Sections 920, 921, and 922.

[Subchapter] B
NAME

§ 210. Corporate name.
§ 211. Reserved name.
§ 212. Registered name.

§ 210. CORPORATE NAME

(a) Except as authorized by subsection (c) or (d), the name of a nonprofit corporation must be distinguishable upon the records of the secretary of state from:

(1) the name of a nonprofit or business corporation incorporated in this state that is not dissolved;

(2) the name of a foreign nonprofit or business corporation under which it is registered to conduct activities in this state, or an alternate name adopted by a foreign nonprofit or business corporation registered in this state because its real name is unavailable;

(3) the name of a filing entity other than a nonprofit or business corporation organized under the law of this state that is not dissolved;

(4) the name of a foreign entity other than a foreign nonprofit or business corporation under which it is registered to do business in this state, or an alternate name adopted
by such a foreign filing entity registered to do business in this state because its real name is unavailable;

(5) a name reserved or registered under Section 211 (reserved name) or 212 (registered name);

[(6) a name reserved or registered under [cite provisions of the state’s business corporation and other entity laws corresponding to Sections 211 and 212].]

[(7) the name of a limited liability partnership organized under the laws of this state;]

[(8) the name of a foreign limited liability partnership under which it is registered to do business in this state, or an alternate name adopted by a foreign limited liability partnership registered to do business in this state because its real name is unavailable; and]

[(9) an assumed name registered under [cite state’s assumed name statute].]

(b) A nonprofit corporation may apply for authorization to use a name that is not distinguishable upon the records of the secretary of state from one or more of the names described in subsection (b). The secretary of state shall authorize use of the name applied for if:

(1) the other entity consents to the use in writing and submits an undertaking in form satisfactory to the secretary of state to change its name to a name that is distinguishable upon the records of the secretary of state from the name of the applying corporation; or

(2) the applicant delivers to the secretary of state a certified copy of a final judgment of a court of competent jurisdiction establishing the applicant’s right to use the name applied for in this state.

(c) A name may not contain a word where the use of that word:

(1) requires the approval of an agency of this state, unless the approval of that agency has been obtained; or

(2) is prohibited by the law of this state.

(d) A name is distinguishable upon the records of the secretary of state only if the name differs from every other name of record in a way other than:

(1) use of punctuation marks;

(2) use of a definite or indefinite article; and

(3) use of any of the following terms, or an abbreviation thereof, in any language to designate the status of an entity: corporation, company, incorporated, limited,
association, fund, syndicate, limited partnership, limited liability company, limited liability partnership, limited liability limited partnership, trust, statutory trust, or business trust.


CROSS-REFERENCES

Appeal from refusal of secretary of state to file a document, § 166.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing requirements, § 160.
Foreign corporations, Ch. 13.
Registered name, § 212.
Reserved name, § 211.
Statement of name in articles, § 202.

OFFICIAL COMMENT

1. No Required Indication of Corporate Status

While the Model Business Corporation Act requires business corporations to include in their names an indication that they are corporations, the Model Nonprofit Corporation Act has never included such a requirement. Imposition of such a requirement for nonprofit corporations would be contrary to the practice of nonprofit corporations, would not materially protect the public, and would entail considerable effort and cost. Hospitals, colleges, museums, trade associations, and other nonprofit institutions typically do not include in their names an indication of corporate status. A nonprofit corporation, however, may include a corporate designator in its name if it so chooses.

2. Names That Are “Distinguishable upon the Records of the Secretary of State”

The provisions of Subchapter 2B are based on the fundamental premise that the name provisions in the act should only ensure that each nonprofit corporation has a sufficiently distinctive name so that it may be distinguished from other entities upon the records of the secretary of state. A nonprofit corporation statute should not be a partial substitute for a general assumed name, unfair competition, or antifraud statute. As a result, the act does not restrict the power of a corporation to adopt or use an assumed or fictitious name with the same freedom as an individual. Principles of unfair competition, not entity organic laws, provide the limits on the competitive use of similar names.

The phrase “distinguishable upon the records of the secretary of state” has become the generally accepted standard used in entity organic laws for name availability. The principal justifications for requiring a distinguishable official name are (i) to prevent confusion within the
secretary of state’s office and the tax office, and (ii) to permit accuracy in naming and serving
corporate defendants in litigation. In addition, having separate names will avoid confusion
regarding the proper recipient of contributions, bequests, and deferred gifts. Thus, confusion in
an absolute or linguistic sense is the appropriate test under the act, not the competitive
relationship between the entities, which is the test for fraud or unfair competition. Section 210(d)
provides guidance for the secretary of state in applying the standard of “distinguishable upon the
records.”

3. Unavailable Names

If an entity is administratively dissolved under its organic law, its name becomes
available for use by another entity. See Section 210(a)(1) and (3). If another entity appropriates
the name of a dissolved entity, upon reinstatement the dissolved entity must adopt a new name as
required by Section 1142. If a dissolved entity is reinstated before its name has been appropriated
by another entity, the dissolved entity resumes having the exclusive right to its name.

Under the laws of some states, registering as a limited liability partnership blocks the use
of the partnership’s name by other entities. In states where that is the case, optional Section
210(a)(7) and (8) should be used. Similarly, in some states registering a fictitious name blocks its
use by other entities and in states where that is the case, optional Section 210(a)(9) should be
used.

4. Consent to Use

Section 210(b)(1) authorizes the secretary of state to accept a name that is
indistinguishable from the name of another entity if that entity files an undertaking in a form
satisfactory to the secretary of state that it will thereafter change its name to a name that is
distinguishable upon the records of the secretary of state. This privilege may be important in
acquisition transactions where a nonprofit corporation is to take over the activities of an existing
entity without a change in name. The secretary of state may require the undertaking to specify
the new name that the corporation will adopt and the time period within which the change will be
made. The requirements imposed on the undertaking should be consistent with the limited role of
the secretary of state in the administration of Section 210.

§ 211. RESERVED NAME

(a) A person may reserve the exclusive use of a name, including an alternate name
for a foreign nonprofit corporation whose name is not available, by delivering an application to
the secretary of state for filing. The application must set forth the name and address of the
applicant and the name proposed to be reserved. If the secretary of state finds that the name
applied for is available, the secretary of state shall reserve the name for the exclusive use of the
applicant for a nonrenewable period of 120 days.
(b) The owner of a reserved name may transfer the reservation to another person by delivering to the secretary of state a signed notice of the transfer that states the name and address of the transferee.


CROSS-REFERENCES

Appeal from refusal of secretary of state to file a document, § 166.
Availability of names, § 210.
Consent to use corporate name, § 210.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing requirements, § 160.
Foreign corporation, Ch. 13.
“Person” defined, § 102.
Registered name, § 212.

OFFICIAL COMMENT

The “reservation” of a corporate name is basically a device to simplify the formation of a new nonprofit corporation or the registration of a foreign nonprofit corporation. By reserving a name, the persons considering such formation or registration can order stationery, prepare documents, etc., on the assumption that the reserved name will be available. Reference to a specific intent to form a new corporation is not required by the statute because the secretary of state is not equipped and should not be asked to determine whether the requisite intent actually exists. For the same reason, “any person” is permitted to reserve a corporate name without reference to specific classes of persons who might wish to reserve a corporate name for various purposes. To use the name to register to do business under Section 1306 or incorporate, the name must comply with Section 210.

Only a single, one-time 120-day reservation is provided for in Section 211, although after that period expires, the name becomes available again and anyone may reserve the name including a person who previously reserved the name. Nothing prevents the formation of an inactive nonprofit corporation specifically to hold a desired name if a longer period of reservation is desired than the 120-day period specified by Section 211.

§ 212. REGISTERED NAME

(a) A foreign corporation may register its name, or an alternate name adopted pursuant to Section 1306 (noncomplying name of foreign corporation), if the name is distinguishable upon the records of the secretary of state from the names that are not available under Section 210(b) (corporate name).
A foreign corporation registers its name, or an alternate name, by delivering to the secretary of state for filing an application setting forth:

1. its name, or an alternate name; and
2. the date and state or other jurisdiction of its incorporation.

The registration of a name under this section is effective for [one year] after the date of registration plus the remainder of the calendar year in which the registration expires.

A foreign corporation whose name registration is effective may renew it for successive [one year] periods by delivering to the secretary of state for filing a renewal application, which complies with the requirements of subsection (b), between October 1 and December 31 of the year before the renewal year. The renewal application when filed renews the registration for the following calendar year.

A foreign corporation whose name registration is effective may thereafter:

1. register to conduct activities in this state as a foreign corporation under the registered name;
2. consent in a record to the use of the registered name by:
   i. a corporation thereafter incorporated under this [Act]; or
   ii. another foreign corporation thereafter registered to conduct activities in this state.


CROSS-REFERENCES

- Appeal from refusal of secretary of state to file a document, § 166.
- Certificate of existence, § 168.
- Consent to use corporate name, § 210.
- “Deliver” defined, § 102.
- Effective time and date of filing, § 163.
- Filing fees, § 162.
- Filing and signature requirements, § 160.
- Foreign corporations, Ch. 13.
- Reserved name, § 211.
- “State” defined, § 102.
OFFICIAL COMMENT

The “registration” of a corporate name is basically a device by which a foreign nonprofit corporation, not registered to do business in the state, can preserve the right to use its unique corporate name if it decides later to register in the state. In effect, registration ensures corporate name availability in areas of potential future expansion.

Section 212 is limited to this purpose and is not for the preservation of trademarks, trade names, or possible assumed names. For this reason, generally only corporate names of foreign nonprofit corporations may be registered (with the exception described below). A broader approach would create issues better resolved under a trademark or similar statute, or by litigation under unfair competition principles, and might impose duties on secretaries of state that they are generally not equipped to handle, or could handle only at increased cost.

Confusion sometimes exists between “reservation” of names under section 211 and “registration” of names under section 212. A foreign nonprofit corporation that is planning to register as a foreign nonprofit corporation and finds that its name is available in the state may either reserve or register the name. Often a foreign nonprofit corporation will have to decide whether to register in the state or to create a domestic subsidiary. This may be decided after the exclusive right to use the corporate name in the state is obtained either by reservation or by registration. If the foreign nonprofit corporation reserves its name, that name will be kept for 120 days and then become available again; if the foreign nonprofit corporation registers its name, that name will be kept for the remainder of the calendar year, unless renewed. That is the foreign nonprofit corporation’s choice. If a foreign nonprofit corporation registers its name and then elects to form a domestic or foreign subsidiary, the written consent procedure of Section 212(e) allows the secretary of state to ascertain that the domestic subsidiary is related to the foreign nonprofit corporation and that use of the registered name by that subsidiary is acceptable to the foreign parent.

If a foreign nonprofit corporation’s corporate name is unavailable, a foreign nonprofit corporation may reserve any available name—including one that is assumed or fictitious rather than the corporation’s corporate name—for 120 days under Section 211, but it may not register this type of name in light of the policy against allowing the name provisions of the act to be used for purposes broader than the “unique name” issue. Nevertheless, a foreign nonprofit corporation that wishes to be certain that a particular fictitious or assumed name will be available in the future may create an inactive domestic subsidiary with the desired name to preserve its future availability.

[Subchapter] C

REGISTERED OFFICE AND AGENT

§ 220. Requirement of registered office and registered agent.

§ 221. Change of registered office or registered agent.

§ 222. Resignation of registered agent.
§ 22. Service on domestic and foreign nonprofit corporations.

§ 220. REQUIREMENT OF REGISTERED OFFICE AND REGISTERED AGENT

Every domestic nonprofit corporation or registered foreign nonprofit corporation must continuously maintain in this state:

(1) a registered office, which may be the same as any of its places of business; and

(2) a registered agent, which may be:

(i) an individual who resides in this state and whose business office is identical with the registered office; or

(ii) a domestic or foreign nonprofit corporation, domestic or foreign business corporation, or domestic or foreign unincorporated entity whose business office is identical with its registered office and, in the case of a foreign nonprofit corporation, foreign business corporation, or foreign unincorporated entity, is registered to do business in this state.


CROSS-REFERENCES

Annual report disclosure, § 421.
Changing registered office or agent, § 221.
“Domestic nonprofit corporation” defined, §102.
Effect of dissolution of corporation, § 1105.
“Filing entity” defined, § 102.
“Foreign nonprofit corporation” defined, §102.
Foreign corporations, Ch. 13.
Involuntary dissolution for failure to appoint and maintain registered agent and office, § 1140.
Naming registered agent and office in articles of incorporation, § 202.
“Principal office”: defined, §102.
designated in annual report, § 421.
Resignation of registered agent, § 222.
Service on corporation, § 223.

OFFICIAL COMMENT

The requirements that a nonprofit corporation incorporated under the act or a registered foreign nonprofit corporation continuously maintain a registered office and a registered agent at that office are based on the premises that at all times such a corporation should have an office
where it may be found and a registered agent at that office to receive any notice or process required or permitted by law to be served. The street and mailing addresses of the registered office must appear in the public records maintained by the secretary of state. A mailing address alone, such as a post office box, is not sufficient since the registered office is the designated location for service of process. See Section 202. The registered office may be a “legal” rather than a “business” office.

A domestic or registered foreign nonprofit corporations may designate a business office of the corporation to be its registered office and a corporate officer at that office to be the registered agent. Because most of the communication to the registered agent at the registered office deals with legal matters, however, corporations sometimes designate their regular legal counsel or the counsel’s nominee as their registered agent and the counsel’s office as the registered office of the corporation.

The registered agent need not be an individual. Corporation service businesses often provide, as a commercial service, registered offices and registered agents at the office of the corporation service business.

§ 221. CHANGE OF REGISTERED OFFICE OR REGISTERED AGENT

(a) A domestic nonprofit corporation or registered foreign nonprofit corporation may change its registered office or registered agent by delivering to the secretary of state for filing a statement of change that sets forth:

1. the name of the corporation;
2. the street address of its current registered office;
3. if the current registered office is to be changed, the street address of the new registered office;
4. the name of its current registered agent;
5. if the current registered agent is to be changed, the name of the new registered agent and the new agent’s signed consent in a record (either as part of the statement or accompanying it) to the appointment; and
6. that after the change or changes are made, the street addresses of its registered office and the business office of its registered agent will be identical.

(b) If the street address of a registered agent’s business office is changed, the agent shall change the street address of the registered office of any corporation for which the agent is the registered agent by notifying the domestic nonprofit corporation or registered foreign nonprofit corporation in a record of the change and signing and delivering to the secretary of state...
state for filing a statement that complies with the requirements of subsection (a) and states that
the corporation has been notified of the change.


CROSS-REFERENCES

Deletion of initial agent and office from articles of incorporation, § 903.
“Deliver” defined, § 102.
Effect of dissolution of corporation, § 1105.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing requirements, § 160.
Involuntary dissolution for failure to file notice of change of registered agent or office, § 1140.
Notice, § 103.
Resignation of registered agent, § 222.

OFFICIAL COMMENT

Changes of registered office or registered agent are routine matters. The purpose of Section 221 is to permit these changes without an amendment of the articles of incorporation or approval of the board of directors or the members.

§ 222. RESIGNATION OF REGISTERED AGENT

(a) A registered agent may resign as agent for a domestic nonprofit corporation or registered foreign nonprofit corporation by delivering to the secretary of state for filing a statement of resignation signed by the agent which states:

(1) the name of the corporation;

(2) the name of the agent;

(3) that the agent resigns from serving as registered agent for the corporation; and

(4) the address of the corporation to which the agent will deliver the notice required by subsection (c).

(b) A statement of resignation takes effect on the earlier of:

(1) 12:01 a.m. on the 31st day after the day on which it is filed by the secretary of state; or
(2) the designation of a new registered agent for the domestic nonprofit corporation or registered foreign nonprofit corporation.

(c) A registered agent promptly shall deliver to the domestic nonprofit corporation or registered foreign nonprofit corporation notice in a record of the date on which a statement of resignation was delivered to the secretary of state for filing.

(d) When a statement of resignation takes effect, the person that resigned ceases to have responsibility under this [Act] for any matter thereafter tendered to it as agent for the domestic nonprofit corporation or registered foreign nonprofit corporation. The resignation does not affect any contractual rights the corporation has against the agent or that the agent has against the corporation.

(e) A registered agent may resign with respect to a domestic nonprofit corporation or registered foreign nonprofit corporation regardless of whether the corporation is in good standing.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 5.03. Cf. Model Business Corporation Act (2016 Revision), § 5.03.

CROSS REFERENCES

Change of registered agent, § 221.
“Deliver” defined, § 102.
Filing fees, § 162.
Filing requirements, § 160.

OFFICIAL COMMENT

Section 222 permits the discontinuation of the registered office as well as the resignation of the agent and sets forth procedures for doing so.

§ 223. SERVICE ON DOMESTIC AND REGISTERED FOREIGN NONPROFIT CORPORATIONS

(a) The registered agent of a domestic nonprofit corporation or registered foreign nonprofit corporation is the corporation’s agent for service of process, notice, or demand required or permitted by law to be served on the corporation.

(b) If a domestic nonprofit corporation or registered foreign nonprofit corporation has no registered agent, or the agent cannot with reasonable diligence be served, the corporation may be served by delivery of the process in record form to the secretary of the corporation at its principal office. The address of the principal office of the corporation must be as shown in the...
corporation’s most recent annual report filed by the secretary of state. Service is effected under this subsection on the earliest of:

1. the date the corporation receives the mail or delivery by the commercial delivery service;
2. the date shown on the return receipt, if signed by the corporation; or
3. five days after its deposit with the United States Postal Service or commercial delivery service, if correctly addressed and with sufficient postage or payment.

(c) If process, notice, or demand cannot be served on a domestic nonprofit corporation or registered foreign nonprofit corporation pursuant to subsection (a) or (b), service may be made by handing a copy to the individual in charge of any regular place of activity of the corporation if the individual served is not a plaintiff in the action.

(d) If process, notice, or demand cannot be served on a domestic nonprofit corporation or registered foreign nonprofit corporation pursuant to subsection (a), (b), or (c), the secretary of state shall be an agent of the corporation upon whom process, notice, or demand may be served. Service of any process, notice, or demand on the secretary of state as agent for a corporation may be made by delivering to the secretary of state duplicate copies of the process, notice, or demand. If process, notice, or demand is served on the secretary of state, the secretary of state shall forward one of the copies by registered or certified mail, return receipt requested, to the corporation at the last address shown in the records of the secretary of state. Service is effected under this subsection (c) at the earliest of:

1. the date the corporation receives the process, notice, or demand;
2. the date shown on the return receipt, if signed on behalf of the corporation; or
3. five days after the process, notice, or demand is deposited with the United States mail by the secretary of state.

(e) This section does not prescribe the only means, or necessarily the required means, of serving a domestic nonprofit corporation or registered foreign nonprofit corporation.


CROSS-REFERENCES

Foreign corporations, Ch. 13.
Notice, § 103.
“Principal office”:
Section 223(b) offers three alternative methods for establishing the date service is
effected. Under Section 223(b)(1), service is effected on the date of receipt by the entity of the
mail or commercial delivery. Under Section 223(b)(2), service is effected on the date shown on
the return receipt, if signed on behalf of the entity. Under Section 223(b)(3), service is effected
five days after it is deposited with the Postal Service or with a commercial delivery service, if
correctly addressed and with correct postage or payment. Service is effected at the earliest of the
three listed circumstances. But for the party effecting service there are difficulties of proof under
the first two circumstances. Under Section 223(b)(1) the exact date of the receipt by the
nonprofit corporation of mail or commercial delivery is peculiarly within the knowledge of the
corporation. Under Section 223(b)(2) the return receipt must be signed on behalf of the
corporation. That requirement is designed to assure that the service is actually received by the
corporation. The problem is that the signature on the return receipt may not always show
unambiguously that the signer was acting for the corporation and was authorized to do so. As a
practical matter, therefore, parties effecting service under Section 223(b) may find it most
convenient to rely on Section 223(b)(3) and to maintain their own records so that the date of
deposit in the mails or with a commercial delivery service can easily be established.

Section 223(c) provides a means for serving process on a nonprofit corporation that
cannot be served under Section 223(a) or (b). Some entity organic laws require that service of
process in that circumstance be made on the secretary of state, but that leaves unanswered the
question of what the secretary of state should do with the process. Section 223(c) permits service
in that situation to be made on an officer or managing or general agent of the corporation.

[CHAPTER] 3
PURPOSES AND POWERS

§ 301. Purposes.
§ 302. General powers.
§ 303. Emergency powers.
§ 304. Ultra vires.

§ 301. 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 will engage in an activity that is subject to regulation under
another statute of this state, the corporation may incorporate under this [Act] only if not
prohibited by, and subject to all limitations of, the other statute.

Revision), § 3.01.

CROSS-REFERENCES

“Articles” or “articles of incorporation” defined, § 102.

OFFICIAL COMMENT

Section 301(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 301 does not impose any limitations on the purposes of a nonprofit
corporation or the use of its assets, those forming a 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 304.

Section 301(b) is designed to tie in a nonprofit corporation with a limitless lawful
purpose permitted by Section 301(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 under other
provisions of law such as Section 501(c)(3) of the Internal Revenue Code which requires that a
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.

§ 302. 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
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 notes, bonds, and other 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 833 (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 [Act] 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 833];
(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 establish conditions for admission of members, admit members, and issue memberships;
(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, § 206, Subch. 9B.
Compensation of directors, § 811.
Debt and security interests, § 643.
Disposition of assets, Ch. 10.
“Employee” defined, § 102.
“Entity” defined, § 102.
Foreign corporations, Ch. 13.
Indemnification, Subch. 8F.
“Member” defined, § 102.
“Membership” defined, § 102.
Ultra vires, § 304.

OFFICIAL COMMENT

The general philosophy of Section 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 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 optional provisions of Section 302(8) and (11) should be used if loans to directors and officers are prohibited. While some states prohibit loans to directors and officers, 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(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(17) permits payments or donations or any other act “that furthers 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(13), permits contributions for purposes that may not be charitable. This power exists only to the extent consistent with law other than the act.

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. Because the same ultra vires rule is applicable to corporations that exceed their purposes or powers (see the Official Comment to Section 304), 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.

§ 303.  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;
2. those directors who participate in a meeting of the board of directors shall constitute a quorum; and
(3) 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.

(d) An emergency exists for purposes of this section if a quorum of the board of directors cannot reasonably be convened because of some catastrophic event.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 3.03. Cf. Model Business Corporation Act (2016 Revision), § 3.03.

CROSS REFERENCES

Corporate powers, § 302.
“Notice” defined, § 102.
Notice of directors’ meeting, § 822.
“Principal office” defined, § 102.

OFFICIAL COMMENT

Section 303 grants every corporation limited powers to act in an emergency even though it has failed to adopt emergency bylaws. These minimal provisions 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 303(b)(1), will depend on the nature of the emergency.

§ 304. ULTRA VIRE

(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] 5 (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

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(3) in a proceeding by the attorney general under Section 1312 (action by attorney general).

(c) In a proceeding by a member, director, or member of a designated body under paragraph (b)(1) to enjoin a 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 corporate act.


CROSS-REFERENCES

Corporate powers, § 302.
Corporate purposes, § 301.
Derivative proceedings, Ch. 5.
Dissolution, Ch. 11.
“Employee” defined, § 102.
“Proceeding” defined, § 102.

OFFICIAL COMMENT

Under Section 304 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 304(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 304 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 purpose or a limitation on a power; both are equally subject to Section 304. 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 304 treats all corporate action the same – except to the extent described in Section 304(b) – and the same rules apply to all contracts no matter at what stage of performance.

Section 304, 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, 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 304.

Section 304 also does not address the validity of essentially intra vires conduct that is not approved by appropriate corporate action. Nor does it 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 corporate 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 304.

Similarly, corporate action is not ultra vires under Section 304 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 304. They may be enjoined because of the breach of fiduciary duty, not because the transaction exceeds the powers or purposes of the corporation.

Section 304(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 1312. 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, Section 304 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. A derivative suit, however, is subject to the requirements of Section 304(c). Under Section 304(c) 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 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.

[Chapter] 4
RECORDS AND REPORTS

Subchapter
A. Records
B. Reports

[Subchapter] A
RECORDS

§ 401. Corporate records.
§ 402. Inspection rights of members.
§ 403. Scope of inspection right.
§ 404. Court-ordered inspection.
§ 405. Inspection rights of directors.
§ 406. Limitations on use of membership list.

§ 401. CORPORATE RECORDS

(a) A nonprofit corporation must maintain the following records:

(1) its articles of incorporation as currently in effect;
(2) its bylaws as currently in effect;
(3) any notices to members referred to in Section 105 (extrinsic facts in filed
record) specifying facts on which a filed document is dependent if those facts are not included in a
document on file with the secretary of state;
(4) all communications in a record to members generally within the past
three years;
(5) minutes of all meetings of, and records of all actions taken without a
meeting by, its members, board of directors, board committees established under Section 825
(board and advisory committees), and any designated body;
(6) a list of the names and business addresses of its current directors and officers; and

(7) its most recent annual report delivered to the secretary of state under Section 421 (annual report for secretary of state).

(b) A nonprofit corporation must maintain appropriate accounting records in a form that permits preparation of the financial statements required by Section 420 (financial statements for members).

(c) A nonprofit corporation must maintain all annual financial statements prepared for the corporation for its last five fiscal years (or such shorter period of existence) and any audit or other reports with respect to those financial statements.

(d) A nonprofit corporation must maintain a record of its current members by class of membership showing an address for each member, which may be an email address or other electronic contact information of the member.

(e) A nonprofit corporation must maintain the records specified in this section in a manner that permits them to be made available for inspection within a reasonable time.


CROSS-REFERENCES

Action by members without meeting, § 704.
Board of directors’ meeting, § 820.
Committees of board of directors, § 825.
“Deliver” defined, § 102.
Directors’ action without meeting, § 821.
Inspection of corporate records, §§ 402 and 405.
Meetings of members, Ch. 7.
Officers, Subch. 8D.
“Principal office”: defined, § 102.
designated in annual report, § 421.

OFFICIAL COMMENT

1. Records to be Maintained

Section 401(a) requires certain basic records to be maintained by the nonprofit corporation. The act does not generally specify how records must be maintained (other than in a manner so that they may be made available for inspection within a reasonable time) or where they must be located.
2. Minutes and Related Documents

Section 401(a)(5) does not address the amount of detail that should appear in minutes or records of actions without a meeting. Minutes of meetings customarily include the formalities of notice, the time and place of the meeting, those in attendance, and the results of any votes. Minutes of meetings and records of actions without a meeting show formal action taken. The extent to which further detail is included is a matter of judgment which may depend on the circumstances or other applicable law. Section 704, which addresses written actions taken by members, requires that consents by members be delivered to the corporation for filing with the corporate records.

3. Financial Statements and Accounting Records

The act does not provide normative standards for the financial statements and accounting records to be prepared or maintained. The word “appropriate” is used to indicate that the nature of the financial records to be kept is dependent to some extent on the nature of the nonprofit corporation’s activities. The act does not require that the corporation prepare and maintain accounting records or financial statements on the basis of generally accepted accounting principles (“GAAP”) if it is not otherwise required to prepare GAAP financial statements. “Appropriate” records are generally records that permit financial statements to be prepared which fairly present the financial position and transactions of the corporation. In some very small corporations operating on a cash basis, however, “appropriate” accounting records may consist only of a check register, vouchers, and receipts.

§ 402. INSPECTION RIGHTS OF MEMBERS

(a) A member of a nonprofit corporation is entitled to inspect and copy, during regular business hours at the corporation’s principal office, any of the records of the corporation described in Section 401(a) (corporate records), excluding minutes of meetings of, and records of actions taken without a meeting by, the board of directors, board committees established under Section 825 (board and advisory committees) and any designated body, if the member gives the corporation a signed notice in a record of the member’s demand at least five business days before the date on which the member wishes to inspect and copy.

(b) A member of a nonprofit corporation is entitled to inspect and copy, during regular business hours at a reasonable location specified by the corporation, any of the following records of the corporation if the member meets the requirements of subsection (c) and gives the corporation a signed notice in a record of the member’s demand at least five business days before the date on which the member wishes to inspect and copy:

(1) financial statements prepared by or for the corporation;
(2) accounting records of the corporation; and
(3) excerpts from minutes of any meeting of, or records of any actions taken without a meeting by, the board of directors, board committees maintained in accordance with Section 401(a); and

(4) subject to Section 407 (limitations on use of membership list), the membership list.

(c) A member may inspect and copy the records described in subsection (b) only if:

1. the member’s demand is made in good faith and for a proper purpose;

2. the member describes with reasonable particularity the member’s purpose and the records the member desires to inspect; and

3. the records are directly connected with the member’s purpose.

(d) The nonprofit corporation may impose reasonable restrictions on the confidentiality, use, or distribution of records described in subsection (b).

(e) The right of inspection granted by subsection (b) may be abolished or limited by a nonprofit corporation’s articles of incorporation.

(f) This section does not affect:

1. the right of a member to inspect records under Section 720 (members list for meeting) or, if the member is in litigation with the corporation, to the same extent as any other litigant; or

2. the power of a court, independently of this [Act], to compel the production of corporate records for examination and to impose reasonable restrictions as provided in Section 404(c) (court-ordered inspection).


CROSS-REFERENCES

Board of directors meeting, § 820.
Committees of board of directors, § 825.
Corporate records required, § 401.
Court-ordered inspection, § 404.
“Deliver” defined, § 102.
Directors’ action without meeting, § 821.
“Principal office”: defined, § 102.
Designated in annual report, § 421.
OFFICIAL COMMENT

1. Scope of inspection right.

Section 402(b) grants a member who meets the requirements of Section 402(c) the right to inspect only excerpts of meetings of, and records of actions taken by, the board of directors and board committees related to the purpose of the inspection. A member is entitled to inspect the record of members under section 402(b) without regard to the nature or class of membership. This right is independent of the right to inspect a membership list immediately before a meeting under Section 720.

2. Proper purpose requirement.

A “proper purpose” under Section 402(c) means a purpose that is reasonably relevant to the demanding member’s interest as a member. Although some statutes do not use the phrase “proper purpose,” the act continues to use it because it is traditional and well understood language defining the scope of the member’s right of inspection and its use ensures that the very substantial case law that has developed under it will continue to be applicable.

As a practical matter, a member who alleges a purpose in general terms, such as to communicate with fellow members, or to determine whether improper transactions have occurred, has been held to allege a “proper purpose.” Section 402(c) thus attempts to require more meaningful statements of purpose, if feasible, by requiring that a member designate “with reasonable particularity” the purpose and the records sought to be inspected; the records demanded must also be “directly connected” with that purpose. If disputed by the nonprofit corporation, the “connection” of the records to the member’s purpose may be determined by a court’s in camera examination of the records.

3. Reasonable restrictions permitted.

The reasonable restrictions on the confidentiality, use, or distribution of financial statements and records permitted by Section 402(d) allow for the protection of confidential or proprietary information in the nonprofit corporation’s records or sensitive matters that might be disclosed in a member’s inspection. Such restrictions might include, for example, requiring the demanding member to sign a confidentiality and use agreement.

4. Limitations on inspection rights.

No inference of any kind should be drawn from Section 402(e) as to whether other sections of the act may be modified by provisions in the articles of incorporation or bylaws.

Section 402(f) provides that the right of inspection granted by Section 402 is an independent right of inspection that is not a substitute for or in derogation of rights of inspection that may exist (i) under Section 720, to inspect the membership list following the establishment of a record date for a meeting; (ii) as part of a right of discovery that exists in connection with
litigation; and (iii) as a “common law” right of inspection, if any is found to exist by a court, to
examine corporate records. Section 402(f) simply preserves whatever independent right of
inspection exists under these sources and does not create or recognize any rights, either expressly
or by implication.

§ 403. SCOPE OF INSPECTION RIGHT

(a) A member may appoint an agent or attorney to exercise the member’s inspection
and copying rights under Section 402 (inspection rights of members).

(b) The nonprofit corporation may, if reasonable, satisfy the right of a member to
copy records under Section 402 by furnishing to the member copies by such means as are chosen
by the corporation, including furnishing copies through electronic delivery.

(c) The nonprofit corporation may comply at its expense with a member’s demand to
inspect the record of members under Section 402(b)(4) by providing the member with a list of
members that was compiled no earlier than the date of the member’s demand.

(d) The nonprofit corporation may impose a reasonable charge to cover the costs of
providing copies of documents to the member, which may be based on an estimate of those costs.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 16.03. Cf. Model Business Corporation Act
(2016 Revision), § 16.03.

CROSS-REFERENCES

Corporate records, § 401.
Court-ordered inspection, § 404.
Inspection right generally, § 402.
Membership list inspection, § 720.

OFFICIAL COMMENT

The right of inspection set forth in Section 402 includes the general right to copy the
records inspected. Section 403 follows precedent established under earlier statutes and extends
the right of inspection to an agent or attorney of a member as well as the member. The right to
copy means more than a right to copy by longhand and extends to the right to receive copies
made by copying machines or through an electronic delivery with the cost of reproduction and
electronic copies being paid by the member.

Section 403(c) is designed to give the nonprofit corporation the option of providing a
reasonably current list of its members instead of granting the right of inspection. A “reasonably
current” list is defined in Section 403(c) as one compiled no earlier than the date of the demand,
which under Section 402(b) must provide at least five days’ notice.
Many nonprofit corporations make available to members without charge some or all of the basic records described in Section 401(a). Section 403(d) authorizes the corporation to charge a reasonable fee based on reproduction costs (including labor and materials) for providing a copy of any record.

Section 720 creates a right of members to inspect a list of members in advance of and at a meeting that is independent of the rights of members to inspect corporate records under Section 402.

§ 404. COURT-ORDERED INSPECTION

(a) If a nonprofit corporation does not allow a member who complies with Section 402 (inspection rights of members) to inspect and copy any records required by that section to be available for inspection, the [name or describe court] of the county where the corporation’s principal office (or, if none in this state, its registered office) is located may summarily order inspection and copying of the records demanded at the corporation’s expense upon application of the member.

(b) If a nonprofit corporation does not within a reasonable time allow a member that complies with Section 402 to inspect and copy the records as required by that section, the member who complies with Section 402 may apply to the [name or describe court] in the county where the corporation’s principal office (or, if none in this state, its registered office) is located for an order to permit inspection and copying of the records demanded. The court shall dispose of an application under this subsection on an expedited basis.

(c) If the court orders inspection and copying of the records demanded under Section 402, it may impose reasonable restrictions on their confidentiality, use or distribution by the demanding member and it shall also order the nonprofit corporation to pay the member’s expenses incurred to obtain the order unless the corporation establishes that it refused inspection in good faith because the corporation had:

(1) a reasonable basis for doubt about the right of the member to inspect the records demanded; or

(2) required reasonable restrictions on the confidentiality, use or distribution of the records demanded to which the demanding member was unwilling to agree.


CROSS-REFERENCES

Corporate records, § 16.01.
Inspection rights of members, § 402.
“Principal office”:
Section 404 provides a judicial remedy if a nonprofit corporation refuses to grant the right of inspection provided by Section 402.

If the right of inspection under Section 402(a) is invoked and the nonprofit corporation refuses to grant inspection, the member may seek a summary order compelling inspection. A summary order is appropriate since the right of inspection under Section 402(a) is either automatic or subject only to a determination that the person is in fact a member of the corporation. By contrast, if inspection is demanded under Section 402(b), the member’s good faith and purpose may be in issue. In that situation Section 404(b) directs the court to handle the proceeding “on an expedited basis.” The purpose of this phrase is to discourage dilatory tactics to avoid or delay inspection without requiring the court to resolve these issues on a summary basis. This language does not mandate any specific procedure by which these issues are to be resolved.

If a court enters a summary order directing inspection under Section 402(a), the cost of reproducing the records, if any, is placed on the nonprofit corporation. Section 404 does not address who should bear the cost of reproducing other records ordered by the court, which is a matter for the courts to decide in light of the policy of the act that costs of reproduction are generally the responsibility of the requesting member and should be assessed against the member.

The principal sanction against unreasonable delay or refusal to grant inspection is provided by Section 404(c), which imposes on the nonprofit corporation the plaintiff’s costs, including attorneys’ fees, unless the corporation can establish that it acted reasonably. The corporation may avoid these costs by showing that the corporation refused inspection in good faith because it had a reasonable basis for doubt about the right of the member to inspect the records demanded. This normally will involve reasonable doubt whether the member had the necessary good faith and proper purpose or whether the records demanded are directly connected to the member’s purpose. The phrase “in good faith because the corporation had a reasonable basis for doubt” establishes a partially objective standard, in that the corporation must be able to point to some objective basis for its doubt that the member was acting in good faith or had a purpose that was proper. For example, a corporation may point to earlier conduct of the member involving improper use of information obtained from the corporation in the past as indicating that reasonable doubt existed as to his present purpose. A corporation may not avoid the imposition of costs under this section merely by showing it had no information one way or the other about the issues in controversy.
§ 405. INSPECTION RIGHTS OF DIRECTORS

(a) A director of a nonprofit corporation is entitled to inspect and copy the books, records, and documents of the corporation at any reasonable time to the extent reasonably related to the performance of the director’s duties as a director, including duties as a member of a board committee, but not for any other purpose or in any manner that would violate any duty to the corporation or law other than this [Act].

(b) The [name or describe the court] of the county where the nonprofit corporation’s principal office (or if none in this state, its registered office) is located may order inspection and copying of the books, records, and documents at the corporation’s expense, upon application of a director who has been refused such inspection rights, unless the corporation establishes that the director is not entitled to such inspection rights. The court must dispose of an application under this subsection on an expedited basis.

(c) If an order is issued, the court may include provisions protecting the nonprofit corporation from undue burden or expense, and prohibiting the director from using information obtained upon exercise of the inspection rights in a manner that would violate a duty to the corporation, and may also order the corporation to reimburse the director for the director’s expenses incurred in connection with the application.


CROSS-REFERENCES

Corporate records, § 401.
Court-ordered inspection, § 404.
Duties of board of directors, § 801.
Director standards of conduct, § 830.

OFFICIAL COMMENT

The purpose of Section 405(a) is to confirm the principle that a director always is entitled to inspect books, records, and documents to the extent reasonably related to the performance of the director’s oversight or decisional duties so long as the requested inspection is not for an improper purpose and the director’s use of the information obtained would not violate any duty to the nonprofit corporation. Section 405(a) provide a director a nearly “absolute” right to information, subject only to limitation if it can be shown that the director has an improper motive or intent in asking for the information or would violate law by receiving the information. In addition, the statutory provision sets forth a remedy for the director in circumstances where the corporation improperly denies the right of inspection.

Under Section 405(a), a director is entitled to review books, records, and documents relating to matters such as (i) compliance by a nonprofit corporation with applicable law, (ii) adequacy of the corporation’s system of internal controls to provide accurate and timely financial
statements and disclosure documents, or (iii) the proper operation, maintenance and protection of
the corporation’s assets. In addition, a director would be entitled to review books and records to
the extent required to consider and make decisions with respect to matters placed before the
board. Inspection by a director may be limited, however, by applicable privacy laws.

Section 405(b) provides for a court order on an expedited basis because there is a
presumption that significant latitude and discretion should be granted to a director, and the
nonprofit corporation has the burden of establishing that the director is not entitled to inspection
of the documents requested. Circumstances where the director’s inspection rights might be
denied include requests that (i) are not reasonably related to performance of a director’s duties
(e.g., seeking a specified confidential document not necessary for the performance of a director’s
duties), (ii) impose an unreasonable burden and expense on the corporation (e.g., compliance
with the request would be duplicative of information already provided or would be unreasonably
expensive and time-consuming), (iii) violate the director’s duty to the corporation (e.g., the
director could reasonably be expected to use or exploit confidential information in personal or
third-party transactions), or (iv) violate any applicable law (e.g., the director does not have the
necessary governmental security clearance to see the requested classified information).

Section 405 does not directly deal with the ability of a director to inspect records of a
subsidiary of which he or she is not also a director. A director’s ability to inspect records of a
subsidiary generally should be exercised through the parent’s rights or power and subsection (a)
does not independently provide that right or power to a director of the parent. In the case of
wholly-owned subsidiaries, a director’s ability to inspect should approximate his or her rights
with respect to the parent. In the case of a partially-owned subsidiary, the ability of the director
to inspect is likely to be influenced by the level of ownership of the parent (this ability can be
expected to be greater for a subsidiary which is part of a consolidated group than for a minority-
owned subsidiary). In any case, the inspection by a director of the parent will be subject to the
parent’s fiduciary obligation to the subsidiary’s other members.

Section 405(c) provides that the court may place limitations on the use of information
obtained by the director and may include in its order other provisions protecting the nonprofit
corporation from undue burden or expense. Further, the court may order the corporation to
reimburse the director for costs (including reasonable counsel fees) incurred in connection with
the application. The amount of any reimbursement is left in the court’s discretion, since it must
consider the reasonableness of the expenses incurred, as well as the fact that a director may be
only partially successful in the application.

The rights granted by this section are also available to members of a designated body. See
Section 812.

§ 406. LIMITATIONS ON USE OF MEMBERSHIP LIST

(a) Without consent of the board of directors, a membership list or any part thereof
may not be obtained or used by any person for any purpose unrelated to a member’s interest as a
member. Without limiting the generality of the foregoing, without the consent of the board a membership list or any part thereof may not be:

(1) used to solicit money or property unless the money or property will be used solely to solicit the votes of the members in an election to be held by the nonprofit corporation;

(2) used for any commercial purpose; or

(3) sold to or purchased by any person.

(b) Instead of making a membership list available for inspection and copying under this [Subchapter], a nonprofit corporation may elect to proceed under the procedures set forth in Section 720(f) (members list for meeting).


CROSS-REFERENCES

Court-ordered inspection, § 404.
Inspection rights, § 402.
“Member” defined, § 102.
Required corporate records, § 401.
Voting lists, § 720.

OFFICIAL COMMENT

A nonprofit corporation’s membership list is a valuable asset. In many cases, the membership list may represent a list of contributors. Section 407 sets forth the basic premise that a membership list may not be obtained or used by any person for any purpose unrelated to a member’s interest as a member. Section 407 then provides that a membership list may not be used in any of the following three purposes without the board’s consent:

(1) The solicitation of money or property unless the money or property will be used solely to solicit the votes of members in an election held by the corporation. A membership list therefore cannot be used by members who in good faith believe the organization has strayed from its purposes and want to solicit the members to contribute to a competitive organization that is carrying out the true purposes of the corporation whose membership list is sought. Nor can members use a membership list to solicit contributions for a non-competitive organization, even if the non-competitive organization has laudable purposes.

(2) Used for any commercial purpose. Commercial organizations frequently desire to use membership lists of nonprofit organizations to contact members. That use is only allowed if approved by the board of directors of the corporation.
(3) Sold to or purchased by any person. Members of a nonprofit organization do not have the right to sell a membership list to any person. Nor may a person seeking a membership list purchase it except from the corporation with the approval of the board of directors.

A nonprofit corporation must have some factual basis for believing that the member seeking the membership list will violate the provisions of Section 407 to deny inspection rights pursuant to Section 407. If a corporation has a legitimate doubt as to the purposes for which a member seeks a membership list, the matter can be heard by a court pursuant to Section 404. The court should closely scrutinize the transaction to determine whether a member has a legitimate purpose or whether the corporation was simply using Section 407 as a ruse to prevent and frustrate a member’s rights. See the Official Comment to Section 404 for the circumstances in which a court may order the corporation to pay attorney fees and costs.

[Subchapter] B
REPORTS

§ 420. Financial statements for members.

§ 421. Annual report for secretary of state.

§ 420. FINANCIAL STATEMENTS FOR MEMBERS

(a) On demand in a record from a member, a nonprofit corporation must furnish that member with financial statements for its latest completed fiscal year within a reasonable time after receipt of the demand. The financial statements may be consolidated or combined statements of the corporation and one or more of its subsidiaries, as appropriate, that include a balance sheet as of the end of the fiscal year and a statement of operations for the year. If financial statements are prepared for the corporation on the basis of generally accepted accounting principles, the annual financial statements must also be prepared on that basis.

(b) If the annual financial statements are reported upon by a certified public accountant, the accountant’s report must accompany them. If not, the statements must be accompanied by a statement of the president or the person responsible for the nonprofit corporation’s accounting records:

(1) stating the reasonable belief of the president or other person as to whether the statements were prepared on the basis of generally accepted accounting principles and, if not, describing the basis of preparation; and

(2) describing any respects in which the statements were not prepared on a basis of accounting consistent with the statements prepared for the preceding year.

Section 420 requires every nonprofit corporation to provide to a member that so requests annual financial statements consisting of a balance sheet as of the end of the fiscal year and a statement of operations for the year. A nonprofit corporation is not otherwise required by this act to provide financial statements to its members, but the articles of incorporation or bylaws may require the preparation and distribution of annual financial statements. A member who is entitled to request a financial statement is defined in Section 102 as a person with the right to vote on a specified matter or a designated body under certain circumstances.

Consolidated statements of the corporation and any subsidiary, or subsidiaries, or combined statements for corporations under common control, may be used. Section 420 does not require financial statements to be prepared on the basis of generally accepted accounting principles (“GAAP”). Many small nonprofit corporations have never prepared financial statements on the basis of GAAP. “Cash basis” financial statements (often used in preparing the tax returns of small corporations) do not comply with GAAP. Even small corporations that keep accrual basis records frequently do not make the adjustments that may be required to present their financial statements on a GAAP basis. In light of these considerations, it would be too burdensome on some small corporations to require GAAP statements. Accordingly, internally or externally prepared financial statements prepared on the basis of other accounting practices and principles that are reasonable in the circumstances will suffice for these types of corporations. If a corporation does prepare financial statements on a GAAP basis for any purpose for the particular year, however, it must send those statements to the members upon demand to meet the requirements of the last sentence of Section 420(a).

Section 420(b) requires an accompanying report or statement in one of two forms: (1) if the financial statements have been reported upon by a public accountant, that report must be furnished; or (2) in other cases, a statement of the president or the person responsible for the corporation’s accounting records must be furnished (i) stating the person’s reasonable belief as to whether the financial statements were prepared on the basis of generally accepted accounting principles, and, if not, describing the basis on which they were prepared, and (ii) describing any respects in which the financial statements were not prepared on a basis of accounting consistent with those prepared for the previous year.

In requiring a statement by the president or person responsible for the corporation’s financial affairs, it is recognized that in many cases this person will not be a professionally trained accountant and should not be held to the standard required of a professional. To emphasize this difference, Section 420 requires a “statement” (rather than a “report” or “certificate”) and calls for the person to express a “reasonable belief” (rather than “opinion”) about whether or not the statements are prepared on the basis of GAAP or, if not, to describe the basis of presentation and any inconsistencies in the basis of the presentation as compared with the previous year. The person is not required to describe any inconsistencies between the basis of
presentation and GAAP. For example, the description might state, with respect to a cash basis statement of receipts and disbursements, that the statement was prepared on that basis and that it presents the cash receipts and disbursements of the entity for the period but does not purport to present the results of operations on the accrual basis of accounting.

This section does not prescribe a set period of time in which the financial statements must be delivered to the members. Failure to comply with the requirements of Section 16.20 does not adversely affect the existence or good standing of the nonprofit corporation. Rather, failure to comply gives an aggrieved member rights to compel compliance or to obtain damages, if they can be established, under general principles of law.

§ 421. ANNUAL REPORT FOR SECRETARY OF STATE

(a) Each domestic nonprofit corporation must deliver to the secretary of state for filing an annual report that sets forth:

(3) the name of the corporation;

(4) the street and mailing addresses of its registered office and the name of its registered agent at that office in this state;

(5) the street and mailing addresses of its principal office; and

(6) the names and business addresses of its directors and principal officers.

(b) Each foreign nonprofit corporation registered to do business in this state must deliver to the secretary of state for filing an annual report that sets forth:

(1) the name of the foreign corporation and, if the name does not comply with Section 210 (corporate name), an alternate name as required by Section 1306 (noncomplying name of foreign corporation);

(2) the foreign corporation’s governing jurisdiction;

(3) the street and mailing addresses of the foreign corporation’s principal office and, if the law of the foreign corporation’s governing jurisdiction requires the foreign corporation to maintain an office in that jurisdiction, the street and mailing addresses of that office;

(4) the street and mailing address of the foreign corporation’s registered office in this state and the name of its registered agent at that office;

(5) the names and business addresses of its directors and principal officers.
(c) Information in the annual report must be current as of the date the annual report is signed on behalf of the nonprofit corporation.

(d) The first annual report must be delivered to the secretary of state between January 1 and April 1 of the year following the calendar year in which a domestic nonprofit corporation was incorporated or a foreign nonprofit corporation was registered to do business. Subsequent annual reports must be delivered to the secretary of state between January 1 and April 1 of the following calendar years.

(e) If an annual report does not contain the information required by this section, the secretary of state shall deliver a notice in a record to the reporting domestic or foreign nonprofit corporation and return the report to it for correction. If the report is corrected to contain the information required by this section and delivered to the secretary of state within 30 days after the notice from the secretary of state becomes effective as determined in accordance with Section 103 (notice), it is deemed to be timely filed.

(f) See Sections 1140 (grounds for administrative dissolution) and 1.311(a)(2) (administrative termination of registration).


CROSS-REFERENCES

Annual report form prescribed by secretary of state, § 421.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Filing fees, § 162.
Grounds for administrative dissolution, §1140
Notice, § 103.
Officers, § 840.
“Principal office” defined, § 102.
Registered agent, Subch. 2B.
Registered office, Subch. 2b.

OFFICIAL COMMENT

The annual report that each nonprofit corporation must submit to the secretary of state is a limited information document for use by the secretary of state, members of the general public, and members. The purpose of the annual report is to show the location of the principal office of the corporation, the names and business addresses of its directors and principal officers, the general nature of the corporation’s activities. It permits members of the general public to ascertain the identity of the corporation and communicate directly with it. It also establishes the alternative to the registered office for service of process and related matters. The “principal office” of the corporation is defined as the location of its executive office in Section 1.40.
The reference to “principal officers” in Section 421(a)(4) is intended to simplify reporting requirements of nonprofit corporations with very large numbers of employees who have some managerial responsibility and who, for business reasons, are designed as officers. The “principal officers” of a corporation include at least the chair of the board of directors, the chief executive officer, and the officers performing the traditional functions performed by the corporate secretary and treasurer, no matter what their designation.

The annual report is required of both domestic nonprofit corporations and foreign nonprofit corporations qualified to conduct activities in the state. The failure to file the annual report, like the failure to satisfy other mandatory requirements of the act, is a ground for administrative dissolution or revocation of the certificate of authority to conduct activities.

[CHAPTER] 5
DERIVATIVE PROCEEDINGS

§ 501. SCOPE OF [Chapter]

In this [Chapter], “derivative proceeding” means a civil suit in the right of a domestic nonprofit corporation or, to the extent provided in Section 508 (applicability to foreign corporations), in the right of a foreign nonprofit corporation.


OFFICIAL COMMENT

The definition of “derivative proceeding” makes it clear that the chapter applies to foreign corporations only to the extent provided in Section 508, which provides that the law of the jurisdiction of incorporation governs except for Sections 504 (stay of proceedings), 506 (discontinuance or settlement) and 507 (payment of expenses). See the Official Comment to Section 508.

§ 502. STANDING
(a) A derivative proceeding may be brought by:

(1) a member or members:

   (i) having 5% or more of the voting power, or by 50 members, whichever is less; or

   (ii) that do not satisfy the requirements of subparagraph (a)(1)(i), but can fairly and adequately represent the interests of the nonprofit corporation in enforcing the rights of the corporation; or

(2) any director or member of a designated body.

(b) The plaintiff in a derivative proceeding must be a member, director, or member of a designated body at the time of bringing the proceeding. A plaintiff who is a member must also have been a member at the time of any action complained of in the derivative proceeding.


CROSS-REFERENCES

“Derivative proceeding” defined, § 501.

OFFICIAL COMMENT

The act and the statutes of many states have long required that a plaintiff must have been a member at the time of the transaction in question. This rule has been criticized as being unduly narrow and technical and unnecessary to prevent the transfer or purchase of lawsuits.

The decision to retain the rule of contemporaneous status as a member in Section 502(b) was based primarily on the view that it was simple, clear, and easy to apply. Further, there has been no persuasive showing that the contemporaneous membership rule has prevented the litigation of substantial suits. Where the plaintiff is a director or member of a designated body, however, the plaintiff need only have that status at the time the proceeding is commenced.

Section 502 does not permit a creditor to commence a derivative proceeding.

§ 503. DEMAND

No person may commence a derivative proceeding until:

(1) a demand in a record has been made upon the nonprofit corporation to take suitable action; and
(2) 90 days have expired from the date delivery of the demand was made unless the person has earlier been notified that the demand has been rejected by the corporation or unless irreparable injury to the corporation would result by waiting for the expiration of the 90-day period.


CROSS-REFERENCES

“Derivative proceeding” defined, § 501.

OFFICIAL COMMENT

Section 503 requires a demand on the nonprofit corporation in all cases. The demand must be made at least 90 days before commencement of suit unless irreparable injury to the corporation would result. This approach has been adopted for two reasons. First, even though no director may be independent, the demand will give the board of directors the opportunity to re-examine the act complained of in the light of a potential lawsuit and take corrective action. Secondly, the provision eliminates the time and expense of the litigants and the court involved in litigating the question whether demand is required. It is believed that requiring a demand in all cases does not impose an onerous burden since a relatively short waiting period of 90 days is provided and this period may be shortened if irreparable injury to the corporation would result by waiting for the expiration of the 90-day period. Moreover, the cases in which demand is excused are relatively rare. Many plaintiffs’ counsel as a matter of practice make a demand in all cases rather than litigate the issue whether demand is excused.

1. Form Of Demand

Section 503 specifies only that the demand must be in a record. The demand should, however, set forth the facts concerning membership and be sufficiently specific to apprise the nonprofit corporation of the action sought to be taken and the ground for that action so that the demand can be evaluated. Detailed pleading is not required since the corporation can contact the member for clarification if there are any questions. In keeping with the spirit of this section, the specificity of the demand should not become a new source of dilatory motions.

2. Upon Whom Demand Should Be Made

Section 503 states that demand shall be made upon the nonprofit corporation. Reference is not made specifically to the board of directors since there may be instances such as a decision to sue a third party for an injury to the corporation, in which the taking of, or refusal to take, action would fall within the authority of an officer of the corporation. Nevertheless, it is expected that in most cases the board of directors will be the appropriate body to review the demand and only in relatively rare cases will a designated body have been given the role of reviewing a demand.
To ensure that the demand reaches the appropriate person for review, it is recommended that the demand be addressed to the board of directors, chief executive officer, or corporate secretary of the nonprofit corporation at its principal office.

3. The 90-Day Period

Section 503(2) provides that a derivative proceeding may not be commenced until 90 days after demand has been made. Ninety days has been chosen as a reasonable minimum time within which the board of directors can meet, direct the necessary inquiry into the charges, receive the results of the inquiry and make its decision. A fixed time period eliminates litigation over what is not a reasonable time. The nonprofit corporation may request counsel for the plaintiff to delay filing suit until the inquiry is completed or, if suit is commenced, the corporation can apply to the court for a stay under Section 504.

Two exceptions are provided to the 90-day waiting period. The first exception is the situation where the plaintiff has been notified of the rejection of the demand prior to the end of the 90 days. The second exception is where irreparable injury to the nonprofit corporation would otherwise result if the commencement of the proceeding is delayed for the 90-day period.

It should be noted that the person bringing suit does not necessarily have to be the person making the demand. Only one demand need be made in order for the nonprofit corporation to consider whether to take corrective action.

4. Response by the Corporation

There is no obligation on the part of the nonprofit corporation to respond to the demand. However, if the corporation, after receiving the demand, decides to institute litigation or, after a derivative proceeding has commenced, decides to assume control of the litigation, the plaintiff’s right to commence or control the proceeding normally ends unless it can be shown that the corporation will not adequately pursue the matter.

§ 504. STAY OF PROCEEDINGS

(a) If the nonprofit corporation commences an inquiry into the allegations made in the demand or complaint, the court may stay any derivative proceeding for such period as the court deems appropriate.

(b) See Section 508 (applicability to foreign corporations).


CROSS-REFERENCES

Demand, § 503.
“Derivative proceeding” defined, § 501.

OFFICIAL COMMENT

Section 504 provides that if the nonprofit corporation undertakes an inquiry, the court may in its discretion stay the proceeding for such period as the court deems appropriate. This might occur where the complaint is filed 90 days after demand but the inquiry into matters raised by the demand has not been completed or where a demand has not been investigated but the corporation commences the inquiry after the complaint has been filed. In any case, it is expected that the court will monitor the course of the inquiry to ensure that it is proceeding expeditiously and in good faith.

§ 505. DISMISSAL

(a) The court must dismiss a derivative proceeding on motion by the nonprofit corporation if one of the groups specified in subsection (b) or (e) has determined in good faith after conducting a reasonable inquiry upon which its conclusions are based that the maintenance of the derivative proceeding is not in the best interests of the corporation.

(b) Unless a panel is appointed pursuant to subsection (e), the determination in subsection (a) must be made by:

(1) a majority vote of independent directors present at a meeting of the board of directors if the independent directors constitute a quorum; or

(2) a majority vote of a committee consisting of two or more independent directors appointed by majority vote of independent directors present at a meeting of the board of directors, regardless of whether the independent directors present at the meeting constituted a quorum.

(c) If a derivative proceeding is commenced after a determination has been made rejecting a demand by a member, the complaint must allege with particularity facts establishing either:

(1) that a majority of the board of directors did not consist of independent directors at the time the determination was made; or

(2) that the requirements of subsection (a) have not been met.

(d) If a majority of the board of directors consisted of independent directors at the time the determination was made, the plaintiff has the burden of proving that the requirements of subsection (a) have not been met; if not, the nonprofit corporation has the burden of proving that the requirements of subsection (a) have been met.
(e) Upon motion by the nonprofit corporation, the court may appoint a panel of one or more independent individuals to make a determination whether the maintenance of the derivative proceeding is in the best interests of the corporation. In such case, the plaintiff has the burden of proving that the requirements of subsection (a) have not been met.

(f) An individual is independent for purposes of this section if the individual does not have:

1. a material interest in the outcome of the proceeding, or
2. a material relationship with a person who has such an interest.

(g) None of the following by itself causes a director to be considered not independent for purposes of this section:

1. the nomination, election, or appointment of the director by persons who are defendants in the derivative proceeding or against whom action is demanded;
2. the naming of the director as a defendant in the derivative proceeding or as a person against whom action is demanded; or
3. the approval by the director of the act being challenged in the derivative proceeding or demand if the act resulted in no personal benefit to the director.


CROSS-REFERENCES

Board of directors:
committees, § 825.
meetings, § 820.
quorum and voting, § 824.
Demand, § 1303.
“Derivative proceeding” defined, § 1301.
“Material interest” defined, § 102.
“Material relationship” defined, § 102.

OFFICIAL COMMENT

When a board of directors properly rejects a demand to bring an action, judicial decisions indicate that the derivative action should be dismissed. Section 505(a) specifically provides that the proceeding shall be dismissed if there is a proper determination that the maintenance of the proceeding is not in the best interests of the corporation. This determination can be made prior to commencement of the suit in response to a demand or after the commencement upon examination of the allegations of the complaint.
The procedures set forth in Section 505 are not intended to be exclusive. As noted in the
comment to Section 503, there may be instances where a decision to commence an action falls
within the authority of an officer of the nonprofit corporation depending upon the amount of the
claim and the identity of the potential defendants.

1. The Persons Making the Determination

Section 505(b) prescribes the persons by whom the determination in subsection (a) may
be made. The subsection provides that the determination may be made by a majority vote of
independent directors if there is a quorum of independent directors, or by a committee of
independent directors appointed by a vote of the independent directors. These provisions parallel
the mechanics for determining entitlement to indemnification in Section 855. In this respect this
clause is an exception to Section 825 which required the approval of at least a majority of all the
directors in office to create a committee and appoint members.

The decisions that have examined the qualifications of directors making the
determination have required that the directors be both “disinterested” in the sense of not having a
personal interest in the transaction being challenged (as opposed to a benefit which devolves
upon the nonprofit corporation or all members generally), and “independent” in the sense of not
being influenced in favor of the defendants by reason of personal or other relationships. Only the
word “independent” has been used in Section 505(b) because it is believed that a person who has
an interest in the transaction would not be independent. The concept of an independent director is
not intended to be limited to non-officer or “outside” directors but may in appropriate
circumstances include directors who are also officers.

Section 505(g)(1) makes it clear that the participation of non-independent directors or
members in the nomination, election, or appointment of a new director will not prevent the new
director from being considered independent. Section 505(g)(1) therefore rejects the concept that
the mere appointment of new directors by the non-independent directors makes the new directors
not independent in making the necessary determination because of an inherent structural bias.
Section 505(g)(2) and (3) also provide that the fact that a director has been named as a defendant
or approved the action being challenged does not cause the director to be considered not
independent. It is expected that a court will be able to assess any actual bias in deciding whether
the director is independent without any presumption arising out of the method of the director’s
appointment, the mere naming of the director as a defendant, or the director’s approval of the act
where the director received no personal benefit from the transaction.

Section 505(e) provides for a determination by a panel of one or more independent
persons appointed by the court. Section 505(a) provides for the appointment only upon motion
by the nonprofit corporation. This would not, however, prevent the court on its own initiative
from appointing a special master pursuant to applicable state rules of procedure.

The procedure in Section 505(e) may be desirable in a number of circumstances. If there
are no independent directors available, the nonprofit corporation may not wish to enlarge the
board to add independent directors or may be unable to find persons willing to serve as
independent directors. In addition, if there are independent directors, they may not have the
available time to conduct the inquiry in an expeditious manner.

Appointment by the court should also eliminate any question about the independence of
the person making the determination. Although the nonprofit corporation may wish to suggest to
the court possible appointees, the court will not be bound by these suggestions and, in any case,
will want to satisfy itself with respect to independence at the same time the person is appointed.

Although Section 505(b)(2) requires a committee of at least two directors, subsection (e)
permits the appointment of only one person in recognition of the potentially increased costs to
the nonprofit corporation for the fees and expenses of an outside person.

Under Section 812, a designated body may perform the functions of the board of
directors under this section.

2. Standards to be Applied

Section 505(a) requires that the determination be made by the appropriate persons in
good faith after conducting a reasonable inquiry upon which their conclusions are based. The
word “inquiry” rather than “investigation” has been used to make it clear that the scope of the
inquiry will depend upon the issues raised and knowledge of the group making the determination
with respect to the issues. In some cases, the issues may be so simple or the knowledge of the
group so extensive that little additional inquiry is required. In other cases, the group may need to
engage counsel and other professionals to make an investigation and assist the group in its
evaluation of the issues.

The phrase “in good faith” modifies both the determination and inquiry. The test, which
is also included in Section 830 (standards of conduct for directors) and 851 (permissible
indemnifications), is subjective and means “honestly or in an honest manner.”

The phrase “upon which its conclusions are based” requires that the inquiry and the
conclusions follow logically. This provision authorizes the court to examine the determination to
ensure that it has some support in the findings of the inquiry. The burden of convincing the court
about this issue lies with whichever party has the burden under Section 505(d). This phrase does
not require the persons making the determination to prepare a report that sets forth their
determination and the bases therefor, since circumstances will vary as to the need for such a
report. There may, however, be many instances where good corporate practice will include such
a procedure.

Section 505 is not intended to modify the general standards of conduct for directors set
forth in Section 830, but rather to make those standards somewhat more explicit in the context of
a derivative proceeding. In this regard, the independent directors making the determination
would be entitled to rely on information and reports from other persons in accordance with
Section 830(b).
Because Section 503 requires demand in all cases, the distinction between demand-excused and demand-required cases does not apply. Section 505(c) and (d) carry forward the distinction, however, by establishing pleading rules and allocating the burden of proof depending on whether there is a majority of independent directors. Section 505(c) assigns the plaintiff the threshold burden of alleging facts establishing that a majority of the board is not independent. If there is an independent majority, the burden remains with the plaintiff to plead and establish that the requirements of Section 505(a) have not been met. If there is no independent majority, the burden is on the nonprofit corporation on the issues delineated in Section 505(a). In this case, the corporation must prove both the independence of the decision makers and the propriety of the inquiry and determination.

§ 506. DISCONTINUANCE OR SETTLEMENT

(a) A derivative proceeding may not be discontinued or settled without the court’s approval. If the court determines that a proposed discontinuance or settlement will substantially affect the interests of the members or a class of members of the nonprofit corporation, the court must direct that notice be given to the members affected.

(b) See Section 508 (applicability to foreign corporations).

CROSS-REFERENCES

“Derivative proceeding” defined, § 501.

OFFICIAL COMMENT

Section 506 requires that all proposed settlements and discontinuances must receive judicial approval. This requirement seems a natural consequence of the proposition that a derivative suit is brought for the benefit of all members and avoids many of the evils of the strike suit by preventing the individual member-plaintiff from settling privately with the defendants.

Section 506 also requires notice to all affected members if the court determines that the proposed settlement may substantially affect their interests. This provision permits the court to decide that no notice need be given if, in the court’s judgment, the proceeding is frivolous or has become moot. The section also makes a distinction between classes of members.

Section 506 does not address the issue of which party should bear the cost of giving notice. This is a matter left to the discretion of the court reviewing the proposed settlement.

§ 507. SECURITY FOR COSTS; PAYMENT OF EXPENSES
(a) In any derivative proceeding brought under Section 502(a)(1) (standing), the nonprofit corporation may seek an order at any stage of the proceeding requiring the plaintiffs to give security for reasonable expenses, including attorney fees and expenses, that may be incurred by the corporation in connection with the proceeding. The corporation may have recourse to the security in such amount as the court determines upon termination of the proceeding. The amount of security may be increased or decreased in the discretion of the court upon a showing that the security provided has or may become inadequate or excessive. Security may be denied or limited in the discretion of the court upon a preliminary showing, by application and upon such types of proof as may be required by the court, establishing prima facie that the requirement of full or partial security would impose undue hardship on plaintiffs and serious injustice would result.

(b) On termination of the derivative proceeding the court may order:

1. the nonprofit corporation to pay the plaintiff’s expenses (including counsel fees) incurred in the proceeding if it finds that the proceeding has resulted in a substantial benefit to the corporation;

2. the plaintiff to pay any defendant’s expenses (including counsel fees) incurred in defending the proceeding if it finds that the proceeding was commenced or maintained without reasonable cause or for an improper purpose; or

3. a party to pay an opposing party’s expenses (including counsel fees) incurred because of the filing of a pleading, motion, or other paper, if it finds that the pleading, motion, or other paper was not well grounded in fact, after reasonable inquiry, or warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law and was interposed for an improper purpose, such as to harass or cause unnecessary delay or needless increase in the cost of litigation.

(c) See Section 508 (applicability to foreign corporations).


CROSS-REFERENCES

“Derivative proceeding” defined, § 501.

OFFICIAL COMMENT

The requirement in Section 507(b)(1) that the court may order the corporation to pay the plaintiff’s expenses if it finds that the proceeding has resulted in a “substantial” benefit to the corporation, should discourage a plaintiff from proposing inconsequential matters to justify the payment of counsel fees. The provision does not specify the method for calculating attorneys’ fees given that there is a substantial body of case law that delineates this issue, which usually includes taking into account the amount or character of the benefit to the corporation.
The standard under section 507(b)(2) for the court to require the plaintiff to pay the defendants’ expenses if the action was commenced without reasonable cause or for an improper purpose is intended to discourage proceedings brought for the sole purpose of obtaining early settlement payments by defendants to avoid significant defense costs, while also protecting plaintiffs whose suits have a reasonable foundation.

Section 507(b)(3) has been added to deal with other abuses in the conduct of derivative litigation which may occur on the part of the defendants and their counsel as well as by the plaintiffs and their counsel. This provision may be unnecessary if these abuses are already addressed under applicable rules of civil procedure.

§ 508. APPLICABILITY TO FOREIGN CORPORATIONS

In any derivative proceeding brought in the right of a foreign nonprofit corporation, the matters covered by this [Chapter] shall be governed by the laws of the jurisdiction of incorporation of the foreign corporation except for Sections 504 (stay of proceedings), 506 (discontinuance or settlement), and 507 (security for costs, payment of expenses).


CROSS-REFERENCES

“Derivative proceeding” defined, § 501.
Foreign corporations, generally, Ch. 13.

OFFICIAL COMMENT

Section 508 clarifies the application of the provisions of Chapter 5 to foreign nonprofit corporations by setting forth a choice of law provision for derivative proceedings involving foreign nonprofit corporations. It provides, subject to three exceptions, that the matters covered by Chapter 5 shall be governed by the laws of the jurisdiction of incorporation of the foreign corporation.

The three exceptions to the general rule are areas which are traditionally part of the forum’s oversight of the litigation process: (i) Section 504, dealing with the ability of the court to stay proceedings; (ii) Section 506, setting forth the procedure for settling a proceeding; and (iii) Section 507, providing for the assessment of reasonable expenses (including counsel fees) in certain situations.

§ 509. NOTICE TO ATTORNEY GENERAL

The plaintiff in a derivative proceeding must notify the attorney general within ten days after commencing the proceeding if it involves a charitable corporation.
CROSS-REFERENCES

“Charitable corporation” defined, § 102.
“Derivative proceeding” defined, § 501.

OFFICIAL COMMENT

The notice under Section 509 provides the attorney general with an opportunity to learn of and evaluate the dispute. The attorney general may, but is not required to, join in the action. See Section 140.

[CHAPTER] 6
MEMBERSHIPS AND FINANCIAL PROVISIONS

A. Admission of Members
B. Rights and Obligations of Members
C. Resignation and Termination
D. Delegates
E. Financial Provisions

[Subchapter] A
ADMISSION OF MEMBERS

§ 601. No requirement of members.
§ 602. Admission.
§ 603. Consideration.

§ 601. NO REQUIREMENT OF MEMBERS

(a) A nonprofit corporation is not required to have members.

(b) Where the articles of incorporation or bylaws of a nonprofit corporation do not provide that it shall have members, or where a corporation has in fact no members entitled to vote on a matter, any provision of this [Act] or any other provision of law requiring notice to, the presence of, or the vote, consent, or other action by members of the corporation in connection with the matter shall be satisfied by notice to, the presence of, or the vote, consent, or other action by the board of directors or a designated body of the corporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.01.

CROSS-REFERENCES
OFFICIAL COMMENT

Nonprofit corporations are not required to have members. They may operate with elected, appointed, or designated directors, or a self-perpetuating board. See Section 8.04(b). They may also operate with a system of delegates who are entitled to vote in a representative assembly for the election of directors or on other matters. The delegates may or may not themselves be members of the corporation, and may or may not be selected by persons that are members of the corporation. See Section 630.

§ 602. ADMISSION

(a) A person may not be admitted as a member without the person’s consent.

(b) If a membership corporation provides certificates of membership to the members, the certificates shall not be registered or transferable except as provided in the articles of incorporation or bylaws.

(c) A person is not a member of a nonprofit corporation unless the person meets the definition of a “member” in Section 102 ([Act] definitions), regardless of whether the corporation designates or refers to the person as a member.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.02.

CROSS-REFERENCES

Conditions and procedures for admission of members, § 302(14).
Consideration for admission, § 603.
“Membership corporation” defined, § 102.
Resignation and termination of members, Subch. 6C.
Rights and obligations of members, Subch. 6B.

OFFICIAL COMMENT

Section 302(14) allows corporations to “establish conditions for admission of members” and “admit members.” These requirements will be upheld unless they conflict with federal or state law.
Any person may be admitted as a member if they qualify under the established criteria and procedures. See Section 102 ("member"). As the definition of "person" contained in Section 102 is all encompassing; minors, corporations, partnerships, governmental subdivisions and any other person without limitation may be admitted to membership.

Section 602(a) prevents nonprofit corporations from admitting persons as members unless they consent to becoming members. Consent may be express or implied, and thus the consent does not have to be in a record. For example, consent may be implied by acceptance of membership benefits knowing that the benefits are only offered to members.

Nonprofit corporations sometimes name persons as members without knowing or having the ability to identify individual members. For example, a corporation’s bylaws may provide that “all poor people within one mile of city hall are members entitled to vote for directors.” In many instances there is no way to prepare a list of these “members” or meet the notice or other requirements of the act as to them, unless they identify themselves to the corporation. As a result of Section 602(b), the above bylaw provision simply authorizes poor people in the area to become members. Before they became members they would have to apply for membership or consent to join by attending a meeting, voting, or otherwise evidencing consent. Until they had manifested this consent they would not be "members" as that term is defined in Section 102.

A membership corporation may provide certificates to its members that indicate their membership in the corporation. Section 602(b) makes those certificates non-transferable, with the result that the only way a membership may be transferred is in compliance with Section 611.

§ 603. CONSIDERATION

Except as provided in its articles of incorporation or bylaws, a membership corporation may admit members for no consideration or for such consideration as is determined by the board of directors. The consideration may take any form, including promissory notes, intangible property, or past or future services. Payment of the consideration may be made at such times and upon such terms as are set forth in or authorized by the articles of incorporation, bylaws, or action of the board.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.03.

CROSS-REFERENCES

Admission of members, § 602.
"Board of directors" defined, § 102.
"Member" defined, § 102.
"Membership corporation" defined, § 102.

OFFICIAL COMMENT
Issuance of a membership, unlike the sale of stock, does not necessarily confer something of value. Nonprofit corporations need the ability to issue memberships for no consideration or such consideration as is set forth in or determined by their articles, bylaws, or board. Section 603 provides this flexibility.

If memberships are to be issued for consideration, the board of directors has wide discretion to fix the consideration. It may be a stated amount or based on a formula. For example, in some trade associations the cost of joining is based on the sales, net worth, or other characteristics of the applicant.

Provisions regarding the amount, nature and time of payment may be set forth in the articles of incorporation, bylaws, or action of the board. To the extent the articles or bylaws do not deal with those subjects, the board has the authority to act as it considers appropriate. When determining the nature, timing, and amount, if any, of payments, board members must act consistently with their duties of care and loyalty. The obligation of members to make payments to their corporation is dealt with in Section 613.

The provisions of this section also apply to a designated body under Section 812. Thus a designated body may determine the consideration for memberships and how the consideration is to be paid.

[Subchapter] B

RIGHTS AND OBLIGATIONS OF MEMBERS

§ 610. Differences in rights and obligations of members.

§ 611. Transfers.

§ 612. Member’s liability to third parties.

§ 613. Member’s liability for dues, assessments, and fees.

§ 614. Creditor’s action against member.

§ 615. Designated body.

§ 610. DIFFERENCES IN RIGHTS AND OBLIGATIONS OF MEMBERS

(a) Except as otherwise provided in the articles of incorporation or bylaws, each member of a membership corporation has the same rights and obligations as every other member with respect to voting, dissolution, membership transfer, and other matters.

(b) See Section 922(a) (bylaw amendments requiring member approval).

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.10.

CROSS-REFERENCES

Admission of members, § 602.

Consideration for memberships, § 603.
Section 610 allows great flexibility and diversity in membership rights. In the absence of an applicable provision in the articles of incorporation or bylaws, all members have the same rights and obligations with respect to voting, dissolution, transfer of their memberships, and other matters.

The differences among members may relate to dues, assessments, transfers of memberships, use of facilities, termination or suspension of members, voting, distributions on dissolution, and other factors. Distinctions may be made between individual, corporate, and other entities that are members of the corporation. These distinctions among members may be based on size, net worth, number of employees, activity, and other factors. These distinctions may but do not necessarily result in classes having the right to vote separately on matters requiring a member vote. See Sections 904 and 922.

Once members have been admitted, a vote of the members may be required to change membership rights and obligations. See Sections 903, 904, 921 and 922. The obligations of members to their corporation are dealt with in Section 613.

§ 611. TRANSFERS

(a) Except as provided in the articles of incorporation or bylaws, a member of a membership corporation may not transfer a membership or any right arising therefrom.

(b) Where the right to transfer a membership has been provided, a restriction on that right shall not be binding with respect to a member holding a membership issued prior to the adoption of the restriction unless the restriction is approved by the affected member.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.11.

CROSS-REFERENCES

Differences in rights and obligations of members, § 610.
“Membership” defined, § 102.
“Membership corporation” defined, § 102.

OFFICIAL COMMENT

Section 611(a) provides that a membership in a membership corporation cannot be transferred unless the articles of incorporation or bylaws provide for transfers. A corporation’s articles or bylaws may provide for transfers if the members want transferable memberships. The articles or bylaws may impose limitations, conditions, and fees as a condition to transferring
memberships. For example, the articles or bylaws could provide that transfers may be made only with the approval of the board of directors.

Section 611(b) is particularly important to members of mutual benefit corporations if their memberships represent a valuable asset. It provides that no restriction on transfer can be imposed after the fact without approval of the affected member.

As Section 611(a) makes clear, the membership transfers to which this section applies are actions taken by the member. A new member may also be substituted for an existing member identified in the articles of incorporation or bylaws by an appropriate amendment of the articles or bylaws, but that type of action is not a transfer subject to this section.

§ 612. MEMBER’S LIABILITY TO THIRD PARTIES

A member of a membership corporation is not, as such, personally liable for the acts, debts, liabilities, or obligations of the corporation.


CROSS-REFERENCES

Liability for preincorporation transactions, § 2.04.
“Member” defined, § 102.
“Membership corporation” defined, § 102.

OFFICIAL COMMENT

Section 612 sets forth the general rule that members have no personal liability to third parties for the acts, debts, liabilities, or obligations of their corporation. Following incorporation, members have limited liability in the absence of: (i) facts allowing a court to pierce the corporate veil; or (ii) a legally enforceable obligation of a member to the corporation. See Section 204 as to the liability of persons purporting to act as or on behalf of a corporation that has not been formed.

§ 613. MEMBER’S LIABILITY FOR DUES, ASSESSMENTS, AND FEES

(a) A membership corporation may levy dues, assessments, and fees on its members to the extent authorized in the articles of incorporation or bylaws. Dues, assessments, and fees may be imposed on members of the same class either alike or in different amounts or proportions, and may be imposed on a different basis on different classes of members. Members of a class may be made exempt from dues, assessments, and fees to the extent provided in the articles or bylaws.

(b) The amount and method of collection of dues, assessments, and fees may be fixed
in the articles of incorporation or bylaws, or the articles or bylaws may authorize the board of
directors or members to fix the amount and method of collection.

(c) The articles of incorporation or bylaws may provide reasonable means, such as
termination and reinstatement of membership, to enforce the collection of dues, assessments, and
fees.

(d) See Section 922(a) (bylaw amendments requiring member approval).


CROSS-REFERENCES

Creditor’s action against member, § 614.
Liability to third parties, § 612.
“Member” defined, § 102.
“Membership corporation” defined, § 102.
Obligations of members, § 610.

OFFICIAL COMMENT

Shareholders rarely obligate themselves to make payments to business corporations in
addition to the amounts they pay to acquire their shares. Members, on the other hand, particularly
members of professional associations or other mutual benefit corporations, often agree to pay
dues to support the purposes of their corporation and may make yearly or other payments for
benefits or services provided by membership corporations.

Persons who become members in a corporation whose bylaws authorize dues,
assessments, or fees agree to the imposition of those items by virtue of accepting their
membership in the corporation.

The term “fees” includes initiation fees.

The provisions of this section also apply to a designated body under Section 812. Thus
Section 613(c) will permit the bylaws to authorize a designated body to fix the amount and
method of collection of fees, assessments and dues.

§ 614. CREDITOR’S ACTION AGAINST MEMBER

(a) A proceeding may not be brought by a creditor of a membership corporation to
reach the liability, if any, of a member to the corporation unless final judgment has been
rendered in favor of the creditor against the corporation and execution has been returned
unsatisfied in whole or in part or unless the proceeding would be useless.

(b) All creditors of a membership corporation, with or without reducing their claims
to judgment, may intervene in any creditor’s proceeding brought under subsection (a) to reach and apply unpaid amounts due the corporation. Any or all members who owe amounts to the corporation may be joined in the proceeding.


CROSS-REFERENCES

Liability for fees, etc., § 613.
Liability to third parties, § 612.
“Membership corporation” defined, § 102.

OFFICIAL COMMENT

A member is generally not liable for the debts, liabilities, or obligations of a nonprofit corporation. See Section 612. This section does not change that rule. This section deals only with the procedure by which a creditor of the corporation may reach a liability owed by a member to the corporation, such as an unpaid subscription for membership.

Section 614 requires a creditor to obtain a final judgment against a membership corporation before suing its members unless a proceeding against the corporation would be useless. A proceeding usually would be useless if a corporation were bankrupt or it was obvious that it did not have sufficient assets to meet the obligation. Section 614 is not intended to preclude the availability of other remedies to a creditor, as, for example, under the Uniform Voidable Transactions Act.

§ 615. DESIGNATED BODY

A designated body may be vested with powers otherwise exercisable by the members, as provided in Section 812 (designated body).

[Subchapter] C

RESIGNATION AND TERMINATION

§ 620. Resignation.
§ 621. Termination and suspension.
§ 622. Purchase of memberships.

§ 620. RESIGNATION

(a) A member of a membership corporation may resign at any time.

(b) The resignation of a member does not relieve the member from any obligations incurred or commitments made prior to resignation.
CROSS-REFERENCES

Liability for fees, etc., § 613.

Liability to third parties, § 612.

“Membership corporation” defined, § 102.

OFFICIAL COMMENT

Section 620(a) sets forth the basic right of a member to resign from a membership corporation at any time. A nonprofit organization generally cannot force a person to belong to it, except in limited instances where membership is required by law, such as certain homeowners associations or bar associations in states that have an integrated bar. See Section 103 which preserves the application of such other laws.

Although a membership corporation generally may not force a person to be a member, a person may be liable to the corporation for wrongfully withdrawing in violation of contractual or other obligations to remain as a member. Under Section 620(b) a person may be liable for obligations incurred or commitments made prior to the resignation. These commitments may extend beyond the time the member resigns.

Resignation from membership will not allow a person to avoid liability for goods or services already provided or for ongoing obligations to which the member agreed prior to resignation. Section 620(b). This provision is particularly important to membership corporations that provide benefits or services to members’ businesses. The member in joining the organization may promise to use its facilities or services for a specified period of time. While Section 620(a) allows a member to resign at any time, Section 620(b) allows the corporation to enforce or obtain damages for violation of a member’s agreement.

§ 621. TERMINATION AND SUSPENSION

(a) A membership in a membership corporation may be terminated or suspended for the reasons and in the manner provided in the articles of incorporation or bylaws.

(b) A proceeding challenging a termination or suspension for any reason must be commenced within one year after the effective date of the termination or suspension.

(c) The termination or suspension of a member does not relieve the member from any obligations incurred or commitments made prior to the termination or suspension.

(d) See Section 922(a) (bylaw amendments requiring member approval).
CROSS-REFERENCES

“Member” defined, § 102.
“Membership” defined, § 102.
“Membership corporation” defined, § 102.

OFFICIAL COMMENT

Section 621 does not deal with the question of the substantive grounds for termination. It also does not specify any requirements that the procedures for termination or suspension must satisfy, but leaves the determination of those procedures to the members. The procedures will require due process for the member being terminated or suspended, but the nature of the process to be provided will depend on the reason for the termination or suspension. Suspension for failure to comply with administrative requirements such as paying dues, for example, do not require the type of due process required when a member is to be terminated for misconduct.

A prior version of the act differentiated between termination and expulsion, using the term “termination” when speaking of memberships and the term “expulsion” when speaking of members. That distinction has been eliminated in favor of the single term “termination.”

If the membership in a membership corporation is limited to persons who are members in good standing in a lodge, church, club, society, or other entity, the articles of incorporation or bylaws may provide that failure on the part of a person to remain in good standing in the other entity will be sufficient cause to terminate the membership of the person in the corporation.

To provide finality, Section 621(b) requires that a proceeding challenging a termination or suspension be commenced within one year after the date of the termination or suspension.

A person who has been terminated or suspended is liable for dues, assessments, and fees based on commitments made or obligations incurred prior to the termination or suspension. If the person has contracted or agreed to make payments to the nonprofit corporation regardless of his or her status as a member, that obligation continues even though the person is suspended or is no longer a member.

§ 622. PURCHASE OF MEMBERSHIPS

(a) A charitable corporation may not purchase any of its memberships or any right arising therefrom. A membership corporation that is not a charitable corporation may purchase any of its memberships or any right arising therefrom only to the extent provided in and in accordance with the articles of incorporation or bylaws.

(b) See Sections 106(b) (relationship of [Act] to other laws) and 922(a) (bylaw
amendments requiring member approval).

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.22.

CROSS-REFERENCES

“Membership corporation” defined, § 102.
Rights and obligations of members, § 610.
When repurchases may not be made, § 641(b).

OFFICIAL COMMENT

Assets of membership corporations that are held for a public, charitable or religious purpose are not available for distribution to members either while the corporation is operating or upon dissolution. Corporations that hold such assets are prohibited by other laws from purchasing their memberships because such a purpose can have the effect of impermissibly distributing restricted assets to the members. As provided in Section 106(b), those other laws control over this section. Members in mutual benefit corporations, on the other hand, may have an economic interest in the corporation and their memberships may represent a valuable asset. Upon dissolution, any surplus may be distributed to members in the absence of some other distribution provision.

Certain protections must be provided to the creditors of the corporation to ensure that the assets are not improperly diverted to members thereby rendering the corporation unable to meet its liabilities. Consequently, the repurchase of a membership is made subject to the restrictions on distributions in Section 641(b).

A bylaw provision authorizing purchase of memberships must be approved by the members. See Section 922.

The repurchase of a membership under this section is different from a termination of membership under Section 621 because a termination usually does not involve the payment of any consideration to the member being terminated.

[Subchapter] D
DELEGATES

§ 630. Delegates.

§ 630. DELEGATES

(a) A membership corporation may provide in its articles of incorporation or bylaws for delegates.

(b) The articles of incorporation or bylaws may set forth provisions relating to:
(1) the characteristics, qualifications, rights, limitations, and obligations of
delegates including their selection and removal;
(2) calling, noticing, holding, and conducting meetings of delegates; and
(3) carrying on corporate activities during and between meetings of delegates.
(c) An assembly or other organized group of delegates constitutes a designated body.


CROSS-REFERENCES

“Designated body.” § 812.
Notice, § 103.

OFFICIAL COMMENT

Section 630 authorizes nonprofit corporations to operate with delegates rather than or in
addition to members or a board of directors. Section 630 authorizes the articles of incorporation
or bylaws to set forth rules in regard to delegates, meetings of delegates, and carrying on
corporate activities during and between meetings of delegates.

Delegates may be given not just some or all of the authority of members, but also some of
the authority of the board of directors to act on those matters specified in the articles of
incorporation or bylaws.

Insofar as the delegates have been given the powers of members, they have analogous
rights, duties, and obligations. Similarly, when delegates are exercising powers of the board of
directors they will have the duties and liabilities of directors. See Section 812.

§ 640. DISTRIBUTIONS PROHIBITED

(a) Except as permitted under Section 622 (purchase of memberships) or 641
(compensation and other permitted payments), a nonprofit corporation shall not pay dividends or
make distributions of any part of its assets, income, or profits to its members, directors, members
of a designated body, or officers.

(b) This section does not apply to a contract or transaction authorized pursuant to
Section 860 (conflicting interest transactions; voidability).

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
(2008), § 6.40.

CROSS-REFERENCES

Compensation and other permitted payments, § 641.
“Designated body” defined, § 102.
“Director” defined, § 102.
“Member” defined, § 102.
“Officer” defined, § 102.
Purchase of memberships, § 622.

OFFICIAL COMMENT

Section 640 sets forth the basic rule that a nonprofit corporation is prohibited from paying
dividends or making other types of distributions. If a transfer is a direct payment to a member as
a result of the member’s interest in the nonprofit corporation, it is prohibited except to the extent
provided in Section 641. Cash dividends from whatever source are the clearest example of
prohibited dividends.

The question arises as to what a nonprofit corporation can do with profits it generates as
it cannot use the profits to pay dividends. Corporations that are exempt from federal income tax
under Section 501(c)(3) of the Internal Revenue Code typically use profits to further their public,
charitable, or religious purposes. Other nonprofit corporations may use profits to improve their
facilities and services.

While members may benefit from the use of the nonprofit corporation’s facilities and
services, that benefit is not a dividend and is not considered a distribution because the
corporation is conferring benefits upon its members in conformity with its purposes.

A payment by a nonprofit corporation that is not derived from “any part of its income or
profit” is not a distribution. Thus the return of an overcharge or the provision of services for
which members have paid is not a distribution, nor is the payment of reasonable compensation
for services.

A payment by a nonprofit corporation pursuant to a contract or transaction authorized
under Section 860 is not a distribution.

§ 641. COMPENSATION AND OTHER PERMITTED PAYMENTS
(a) A nonprofit corporation may pay reasonable compensation or reimburse reasonable expenses to members, directors, members of a designated body, or officers for services rendered.

(b) A nonprofit corporation may confer benefits upon or make contributions to members or nonmembers in conformity with its purposes, repurchase its memberships only to the extent provided in Section 622 (purchase of memberships), or repay capital contributions, except when:

1. the corporation is currently insolvent or would thereby be made insolvent or rendered unable to carry on its purposes; or

2. the fair value of the assets of the corporation remaining after the conferring of benefits, contribution, repurchase, or repayment would be insufficient to meet its liabilities.

(c) A nonprofit corporation may make distributions of cash or property to members upon dissolution or final liquidation only as permitted by this Act.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.41.

CROSS-REFERENCES

Corporate purposes, § 301.
“Designated body” defined, § 102.
“Director” defined, § 102.
Dissolution, Ch. 11.
“Member” defined, § 102.
“Officer” defined, § 102.
Purchase of memberships, § 622.

OFFICIAL COMMENT

Most nonprofit corporations do not compensate individuals for serving as directors. In some nonprofit corporations, however, compensation may be appropriate as a result of the time and effort needed to serve as a director, the responsibilities undertaken, and other relevant factors. Section 811 allows the board of directors to set the compensation of directors for serving as directors. The general power of the board under Section 801 to manage the affairs of the corporation also gives the board the power to set the compensation of directors who serve as officers or in some other capacity.

Distributions upon dissolution or final liquidation are governed by Chapter 11. Normally, the members of a nonprofit corporation that is not a charitable corporation will receive its net worth upon dissolution. Members of a charitable corporation, in contrast, normally will not share in its net worth upon dissolution since they do not have any economic interest in its assets. Under limited circumstances, however, a charitable corporation may distribute its assets to its members,
if those members are themselves charitable corporations or otherwise recognized as exempt
under Section 501(c)(3) of the Internal Revenue Code.

§ 642. CAPITAL CONTRIBUTIONS OF MEMBERS

(a) A membership corporation that is not a charitable corporation may provide in its
articles of incorporation or bylaws that members, upon or subsequent to admission, must make
capital contributions. Except as provided in the articles or bylaws, the amount shall be fixed by
the board of directors. The requirement of a capital contribution may apply to all members, or to
members of a single class, or to members of different classes in different amounts or
proportions.

(b) The adoption or amendment of a capital contribution requirement, whether or not
approved by the members, shall not apply to a member who did not vote in favor of the adoption
or amendment until 30 days after the member has been given notice of the adoption or
amendment.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.42.

CROSS-REFERENCES

Dues, assessments, and fees, § 613.
“Membership corporation” defined, § 102.
When capital contributions may not be repaid, § 641(b).

OFFICIAL COMMENT

Mutual benefit corporations may find it desirable to require the members to make capital
contributions at certain times, for example, to fund improvements to a clubhouse or other
facilities of the corporation. Capital contributions are typically different from membership
obligations like dues in that capital contributions are larger in amount and sporadic or
nonrecurring. They also differ in that capital contribution requirements must be set forth in the
articles of incorporation or bylaws. As a result, Section 642(b) provides that adoption or
amendment of a capital contribution will not apply to a member who does not vote in favor of
the change until 30 days after notice to the member. This will permit the member to resign if the
member does not wish to satisfy the capital contribution requirement. A similar delay does not
apply to changes in dues, assessments, or fees.

The provisions of this section also apply to a designated body under Section 812. Thus a
designated body may perform any of the functions of the board of directors described in this
section.

§ 643. DEBT AND SECURITY INTERESTS
(a) A nonprofit corporation may not issue bonds or other evidences of indebtedness except for money or other property, tangible or intangible, or labor or services actually received by or performed for the corporation or for its benefit or in its formation or reorganization, or a combination thereof. In the absence of fraud, the judgment of the board of directors as to the value of the consideration received by the corporation is conclusive.

(b) The board of directors may authorize a mortgage or pledge of, or the creation of a security interest in, all or any part of the property of the nonprofit corporation, or any interest therein. Unless otherwise restricted in the articles of incorporation or bylaws, the vote or consent of the members is not required to make effective such action by the board.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.43.

CROSS-REFERENCES

When debt instruments may not be repaid, § 641(b).

OFFICIAL COMMENT

Issuance of bonds or debt instruments must be done in compliance with applicable federal and state securities laws, subject to any applicable exemptions from registration under those laws. The application of such laws is preserved by Section 106.

The provisions of this section also apply to a designated body under Section 812. Thus the functions of the board of directors under this section with respect to debts and security interests may be assigned to a designated body instead.

§ 644. PRIVATE FOUNDATIONS

(a) Except as provided in subsection (b), a nonprofit corporation that is a private foundation as defined in Section 509(a) of the Internal Revenue Code must:

(1) distribute such amounts for each taxable year at such time and in such manner as not to subject the corporation to tax under Section 4942 of the Internal Revenue Code;

(2) not engage in any act of self-dealing as defined in Section 4941(d) of the Internal Revenue Code;

(3) not retain any excess business holdings as defined in Section 4943(c) of the Internal Revenue Code;

(4) not make any investments in such manner as to subject the corporation to tax under Section 4944 of the Internal Revenue Code; and

(5) not make any taxable expenditures as defined in Section 4945(d) of the Internal Revenue Code.
(b) Subsection (a) does not apply to a nonprofit corporation incorporated before January 1, 1970 that has been properly relieved from the requirements of Section 508(e)(1) of the Internal Revenue Code by a timely judicial proceeding.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 6.44.

CROSS-REFERENCES

Powers, § 302.

Purposes, § 301.

OFFICIAL COMMENT

Under Section 508(e)(1) of the Internal Revenue Code, a private foundation (as defined in Section 509(a)) is not exempt from federal income tax under Section 501(a) unless its governing instrument includes provisions the effects of which are:

(1) to require its income for each taxable year to be distributed at such time and in such manner as not to subject the foundation to tax under Section 4942; and

(2) to prohibit the foundation from engaging in any act of self-dealing (as defined in Section 4941(d)), from retaining any excess business holdings (as defined in Section 4943(c)), from making any investments in such manner as to subject the foundation to tax under Section 4944, and from making any taxable expenditures (as defined in Section 4945(d)).

Section 1.508-3(d) of the Income Tax Regulations provides that a private foundation’s governing instrument is deemed to conform with the requirements of Section 508(e) of the Internal Revenue Code if valid provisions of state law have been enacted which either require the foundation to comply with the provisions of Section 508(e)(1), or treat the required provisions as contained in the foundation’s governing instrument.

Section 508(e)(2) of the Internal Revenue Code provides that the requirements of paragraph 1 of the section do not apply to a private foundation organized before January 1, 1970 which has been excused from complying with the requirements of paragraph 1 by a court order secured in a proceeding begun before January 1, 1972. That exception is preserved by Section 6.44(b).

Under the applicable Income Tax Regulation (Section 1.508(3)(d)), this section satisfies the requirement that a private foundation’s governing instrument include such provisions. The section applies only to foundations that are corporations, and does not satisfy the requirements of Section 508(e) in the case of trusts or other entities that qualify as private foundations under Section 509(a) of the Code.
MEMBER MEETINGS

Subchapter

A. Procedures
B. Voting
C. Voting Agreements

[Subchapter] A

PROCEDURES

§ 701. Annual and regular meetings.
§ 702. Special meeting.
§ 703. Court-ordered meeting.
§ 704. Action without meeting.
§ 705. Notice of meeting.
§ 706. Waiver of notice.
§ 707. Record date.
§ 708. Conduct of member meeting.
§ 709. Action by ballot.
§ 710. Remote participation in member meeting.

§ 701. ANNUAL AND REGULAR MEETINGS

(a) Except in the case of a membership corporation that holds meetings only of delegates and not of the members, a membership corporation shall hold a meeting of members annually at a time stated in or fixed in accordance with the articles of incorporation or bylaws. The articles of incorporation or bylaws of a membership corporation that holds meetings only of delegates and not of the members may provide for meetings of the delegates to be held less frequently than annually but at least every six years.

(b) A membership corporation may hold regular meetings on a regional or other basis at times stated in or fixed in accordance with the articles of incorporation or bylaws.

(c) Except as provided in subsection (e), annual and regular meetings of the members may be held in or out of this state at the place stated in or fixed in accordance with the articles of incorporation or bylaws. If no place is so stated or fixed, annual and regular meetings shall be held at the nonprofit corporation’s principal office.

(d) The failure to hold an annual or regular meeting at the time stated in or fixed in accordance with the articles of incorporation or bylaws does not affect the validity of any corporate action.

(e) The articles of incorporation or bylaws may provide that an annual or regular meeting of members does not need to be held at a geographic location if the meeting is held by any means of communication by which the members have the opportunity to read or hear the
proceedings substantially concurrently with their occurrence, vote on matters submitted to the
members, pose questions, and make comments.

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
(2008), § 7.01. Cf. Model Business Corporation Act
(2016 Revision), § 7.01.

CROSS-REFERENCES

Action by ballot, § 709.
Action without meeting, § 704.
Annual election of directors, § 803.
Court-ordered meeting, § 703.
Director holdover terms, § 805.
List of members at meeting, § 720.
“Membership corporation” defined, § 102.
Notice of meeting, § 705.
“Principal office”:
   defined, § 102.
   designated in annual report, § 421.
Proxies, § 722.
Quorum and voting requirements, §§ 724-.26.
Special meeting, § 702.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 701(a) requires every membership corporation to hold an annual meeting of
members each year, unless the corporation holds meetings only of delegates (in which case the
articles of incorporation or bylaws may provide for less frequent meetings of delegates, so long
as a meeting of delegates is held at least once every six years). The principal action to be taken at
the annual meeting is the election of directors pursuant to Section 804, but the purposes of an
annual meeting are not limited and any matters appropriate for member action may also be
considered at that meeting. An annual meeting is also an appropriate forum for a member to raise
any relevant question about the corporation’s operations.

The requirement of Section 701(a) that an annual meeting be held is phrased in
mandatory terms to ensure that every member entitled to participate in an annual meeting has the
unqualified right to (i) demand that an annual meeting be held and (ii) compel the holding of the
meeting under Section 703 if the nonprofit corporation does not promptly hold the meeting and if
the members have not elected directors by written consent. If no member objects, rather than
holding an annual meeting, the members may elect directors and take other appropriate action by
consent under Section 704. That practice creates no problem under Section 701, because Section
701(d) provides that failure to hold an annual meeting does not affect the validity of any
corporate action. If the members fail to elect directors, the directors currently in office continue
in office under Section 805(d) beyond the expiration of their terms except as provided in the
articles of incorporation or bylaws.
Some membership corporations hold regular meetings of members in addition to holding an annual meeting of members. Section 701(b) recognizes this practice and allows corporations to hold regular meetings at times stated in or fixed in accordance with their articles of incorporation or bylaws. The act does not specify any particular business that must be considered at regular meetings.

The time and place of the annual meeting is to be “stated in or fixed in accordance with the articles of incorporation or bylaws.” If the articles or bylaws do not themselves fix a time and place for the annual meeting, authority to fix them may be delegated to the board of directors or to a specified corporate officer. Section 701 thus gives nonprofit corporations the flexibility to hold annual meetings in varying places at varying times as convenience may dictate.

The annual meeting may be held either inside or outside the state or in a foreign country, but if the bylaws do not fix, or state the method of fixing, the place of the meeting, the meeting must be held at the “principal office” of a membership corporation. The principal office is defined in Section 102 as the location of the principal executive office of the corporation, which may or may not be its registered or official office under Section 220. Section 421 requires that the address of the principal office be specified in the corporation’s annual report. An annual meeting may also be held electronically if the requirements of Section 701(e) are satisfied.

If the annual meeting is not held either within 6 months of the close of a membership corporation’s fiscal year or within 15 months of the last annual meeting, a member may compel an annual meeting to be held under Section 703. In the absence of a demand for a meeting, a corporation can operate indefinitely without actually holding an annual meeting.

Because communications technology is evolving rapidly, Section 701(e) does not attempt to identify the types of communications technology that may be used to conduct an annual or regular meeting of the members that is not held at a geographic location. Any type of technology may be used as long as it satisfies the substantive requirements of Section 701(e). A similar provision regarding special meetings is provided in Section 702(f). Because both Section 701(e) and Section 702(f) require the articles of incorporation or bylaws to authorize the use of communications technology when it is the sole way a meeting will be conducted, such a provision should be clear regarding whether it applies to annual and regular meetings as well as to special meetings.

§ 702. SPECIAL MEETING

(a) A membership corporation must hold a special meeting of members:

(1) at the call of its board of directors or the person or persons authorized to do so by the articles of incorporation or bylaws; or

(2) if the holders of at least 10%, or such other amount less than 10% or up to 25% as the articles of incorporation or bylaws shall specify, of all the votes entitled to be cast on
an issue proposed to be considered at the proposed special meeting sign, date, and deliver to the
corporation one or more demands in a record for the meeting describing the purpose or purposes
for which it is to be held.
(b) Unless otherwise provided in the articles of incorporation or bylaws, a demand for
a special meeting may be revoked by notice to that effect received by the membership
corporation from the members calling the meeting prior to the receipt by the corporation of
demands sufficient in number to require the holding of a special meeting.
(c) If not otherwise fixed under Section 703 (court-ordered meeting) or 707 (record
date), the record date for determining members entitled to demand a special meeting shall be the
first date on which a signed demand of members is delivered to the nonprofit corporation. A
demand for a special meeting shall not be effective unless, within 60 days after the earliest date
on which a demand delivered to the corporation was signed, demands signed by members
holding at least the percentage of votes specified in or fixed in accordance with Section 702(a)(2)
have been delivered to the corporation.
(d) Except as provided in Section 702(f), special meetings of the members may be
held in or out of this state at the place stated in or fixed in accordance with the articles of
incorporation or bylaws. If no place is so stated or fixed, special meetings shall be held at the
corporation’s principal office.
(e) Only business within the purpose or purposes described in the meeting notice
required by Section 705(c) (notice of meeting) may be conducted at a special meeting of the
members.
(f) The articles of incorporation or bylaws may provide that a special meeting of
members does not need to be held at a geographic location if the meeting is held by means of any
communications technology whereby the members have the opportunity to read or hear the
proceedings substantially concurrently with their occurrence, vote on matters submitted to the
members, pose questions, and make comments.

(2016 Revision), § 7.02.

CROSS-REFERENCES

Action by ballot, § 709.
Action without meeting, § 704.
Annual meeting, § 701.
Court-ordered meeting, § 703.
List of members at meeting, § 720.
“Membership corporation” defined, § 102.
Notice of meeting, § 705.
“Principal office”:

defined, § 102.
OFFICIAL COMMENT

Any meeting other than an annual or regular meeting is a special meeting under Section 702. At an annual meeting directors are elected and, subject to any applicable special notice requirement prescribed by the act or by the articles of incorporation, any relevant issue pertaining to the corporation may be considered, while at a special meeting only matters within the specific purposes for which the meeting is called may be considered.

1. Who May Call A Special Meeting

A special meeting may be called under Section 702(a) by the board of directors or the persons authorized to do so by the articles of incorporation or bylaws or upon demand by members as described below. Typically, the person or persons holding certain designated offices within the corporation, e.g., the president, chair of the board of directors, or chief executive officer, are given authority to call special meetings of the members. In addition, the holders of at least 10 percent of the votes entitled to be cast on a proposed issue at the special meeting may require the membership corporation to hold a special meeting by signing, dating, and delivering one or more demands for a special meeting that set forth the purpose of the desired meeting. That percentage may be decreased or increased (but to not more than 25 percent) by a provision in the articles of incorporation or bylaws fixing a different percentage.

Members demanding a special meeting do not all need to sign a single demand, but the demands must all describe essentially the same purpose or purposes. Revocations of demands will be effective if notice is delivered to the corporation in the manner contemplated by Section 103 and received before the corporation receives the requisite number of demands requiring that a special meeting be called. Revocations received after that time will have no effect. Upon receipt of demands from members with the requisite number of votes, the corporation (through an appropriate officer) must call the special meeting at a reasonable time and place. The members’ demand may suggest a time and place but the final decision on such matters belongs to the corporation. If no meeting is held within the time periods specified in Section 703, a member who is entitled to participate, or who signed a demand, may seek judicial relief under that section requiring that the meeting be held.

Section 702(c) fixes a record date for determining the members entitled to sign a demand for a special meeting of members. Unless a record date is otherwise fixed for this purpose, the record date is the date the first member signs the demand. If a member initially signs a demand but later seeks to withdraw the demand, the corporation may permit the member to do so.

2. Discretion as to Call of Special Meeting
Under Section 702(a)(2) it is possible that more than one faction of members may demand meetings at roughly the same time or that a single (or changing) faction of members may request consecutive, overlapping, or repetitive meetings. The responsible corporate officers should have some discretion as to the call and purposes of a meeting, and where demands are repetitious or overlapping, they should have the right to refuse to call a meeting for a purpose identical or similar to a purpose for which a previous special meeting was held in the recent past. Similarly, they should have some discretion to decline to call a special meeting when an annual or regular meeting will be held in the near future. This limited discretion of the corporation to deny repetitive or overlapping demands may ultimately be tested under Section 703, which itself gives the court discretion whether or not to compel the holding of a special meeting under these circumstances. See the Official Comment to Section 703.

3. **Business That May Be Conducted at a Special Meeting**

Section 705(c) provides that a notice of a special meeting must include a “description of the purpose for which the meeting is called.” Section 702(e) states that only business that is within that purpose may be conducted at the special meeting. The word “within” was chosen, rather than a broader phrase like “reasonably related to,” to describe the relationship between the notice and the authorized business to assure a member who does not attend a special meeting that new or unexpected matters will not be considered in the member’s absence.

4. **Location**

A special meeting may be held either inside or outside the state or in a foreign country, but if the bylaws do not fix, or state the method of fixing, the place of the meeting, the meeting must be held at the “principal office” of the membership corporation. The principal office is defined in Section 102 as the location of the principal executive office of the corporation and may or may not be its registered office under Section 220. Section 421 requires that the address of the principal office be specified in the corporation’s annual report.

A special meeting may also be held using electronic technology, such as the Internet, if the requirements of Section 702(f) are satisfied. Because communications technology is evolving rapidly, Section 702(f) does not attempt to identify the types of communications technology that may be used to conduct a special meeting of the members that is not held at a geographic location. Any type of technology may be used as long as it satisfies the substantive requirements of Section 702(f). A similar provision regarding annual and regular meetings is provided in Section 701(e). Because both Section 701(e) and Section 702(f) require the articles of incorporation or bylaws to authorize the use of communications technology when it is the sole way a meeting will be conducted, such a provision should be clear regarding whether it applies to annual and regular meetings as well as to special meetings.

5. **Designated Body**

The provisions of this section relating to the board of directors also apply to a designated body under Section 812. Thus a designated body may be given the authority to call and otherwise act with respect to a special meeting.
§ 703. COURT-ORDERED MEETING

(a) The [name or describe] court of the county where the principal office of a membership corporation (or, if not in this state, its registered office) is located may summarily order a meeting to be held:

(1) on application of any member entitled to participate in an annual or regular meeting if an annual meeting was not held within the earlier of 6 months after the end of the corporation’s fiscal year or 15 months after its last annual meeting; or

(2) on application of a member who signed a demand for a special meeting under Section 702 (special meeting), if:

   (i) notice of the special meeting was not given within 30 days after the first day on which the requisite number of demands have been delivered to the corporation; or

   (ii) the special meeting was not held in accordance with the notice.

(b) The court may fix the time and place of the meeting, determine the members entitled to participate in the meeting, specify a record date for determining members entitled to notice of and to vote at the meeting, prescribe the form and content of the meeting notice, fix the quorum required for specific matters to be considered at the meeting (or direct that the votes represented at the meeting constitute a quorum for action on those matters), and enter other orders necessary to accomplish the purpose or purposes of the meeting.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 7.03. Cf. Model Business Corporation Act (2016 Revision), § 7.03.

CROSS-REFERENCES

Annual meeting, § 701.
Notices and other communications, § 103.
Member list for voting at meeting, § 720.
“Membership corporation” defined, § 102.
Notice of meeting, § .05.
“Principal office”:
   defined, § 102.
   designated in annual report, § 421.
Quorum and voting requirements, §§ 724-726.
Registered office:
   designated in annual report, § 421.
   required, §220.
Regular meeting, § 701.
Voting entitlement generally, § 721.
Section 703 provides the remedy for members if a membership corporation refuses or fails to hold a meeting of members as required by Section 701 or 702. Because a meeting must be held within 60 days of the notice date under Section 705, the maximum delay between the demand for a special meeting and the right to petition a court for a summary order is 90 days.

1. Discretion of the Court to Order a Meeting

The court has broad discretion under Section 703 whether to order that a meeting be held, since the language of the statute is that the court “may summarily order” that a meeting be held. A court, for example, may refuse to order a special meeting if the specified purpose is repetitive of the purpose of a special meeting held in the recent past. Alternatively, the court may view the demand as a good faith request for reconsideration of an action taken in the recent past and may order a meeting to be held. Similarly, even though a demand for an annual meeting is not a formal prerequisite for an application for a summary order under this section, the court may withhold setting a time and date for the annual meeting for a reasonably short period in order to permit the corporation to do so.

2. Notice, Time, Place, and Quorum Requirements

If the court orders that a meeting be held, the court has wide discretion over the terms of the order, including the matters set forth in Section 703(b). The discretion of the court with respect to quorum requirements prevents a holder of the majority of the votes (who may not desire that a meeting be held) from frustrating the court-ordered meeting by not attending to prevent the existence of a quorum. To prevent misunderstanding about a special quorum requirement, if one is imposed, it is appropriate for the court to order that the notice of the meeting state specifically and conspicuously that a special quorum requirement is applicable to the court-ordered meeting. The court may also enter orders overriding the articles of incorporation or bylaws relating to matters such as notice (including advance notice requirements), and the time and place of the meeting.

3. Status as Annual Meeting

The court may provide that a meeting it has ordered is to be the annual meeting. If so provided, the meeting should be viewed as compliance with Section 701, precluding all other member requests for an annual meeting for that year.

§ 704. ACTION WITHOUT MEETING

(a) Except as provided in the articles of incorporation or bylaws, action required or permitted by this [Act] to be taken at a meeting of the members may be taken without a meeting if the action is taken by all the members entitled to vote on the action. The action must be evidenced by one or more consents in a record bearing the date of signature and describing the
action taken, signed by all the members entitled to vote on the action, and delivered to the
membership corporation for inclusion in the minutes or filing with the corporate records.

(b) If not otherwise fixed under Section 707 (record date) and if prior action by the
board of directors is not required respecting the action to be taken without a meeting, the record
date for determining members entitled to take action without a meeting is the first date on which
a signed consent is delivered to the membership corporation. If not otherwise fixed under Section
707 and if prior action by the board of directors is required respecting the action to be taken
without a meeting, the record date is the close of business on the day the board of directors took
the prior action. A consent is not effective to take the corporate action referred to therein unless,
within 60 days after the earliest date on which a consent delivered to the corporation as required
by this section was signed, consents signed by members entitled to cast the required number of
votes on the action have been delivered to the corporation. A consent may be revoked by a
signed notice in a record to that effect delivered to the corporation before unrevoked consents
sufficient in number to take the corporate action have been delivered to the corporation.

(c) A consent signed under this section has the effect of a meeting vote and may be
described as such.

(d) If the articles of incorporation or the bylaws require that notice of proposed
corporate action be given to members not entitled to vote on the action and the action is to be
taken by consent of the members entitled to vote, the membership corporation must deliver to the
members not entitled to vote notice of the proposed action at least 10 days before the action is
taken. The notice must contain or be accompanied by the same material that would have been
required to be delivered to members not entitled to vote in a notice of meeting at which the
proposed action would have been submitted to the members for action.

(2016 Revision), § 7.04.

CROSS-REFERENCES

Acceptance of consents, § 723.
“Deliver” defined, § 102.
“Membership corporation” defined, § 102.
Notices and other communications, § 103.
“Sign” defined, § 102.
Voting entitlement generally, § 721.

OFFICIAL COMMENT

The default rule under Section 704 is that all the members entitled to vote on an issue
may act by unanimous consent without a meeting unless the articles of incorporation or bylaws
expressly limit the use of action by consent.
Unanimous consent is generally obtainable only for matters on which there are relatively few members entitled to vote. Although Section 704 only authorizes unanimous consent, it permits the articles of incorporation or bylaws to vary that rule. Thus, the articles or bylaws could provide for consent by less than all the members (typically a majority) or prohibit action by consent and require a meeting whenever the members are to act on an issue.

Action by consent has the same effect as a meeting vote and may be described as such, including in filings with the secretary of state.

1. Form of Consent

To be effective, consents must be in a record, dated, signed by all the members entitled to vote, and delivered to the membership corporation in the manner contemplated by Section 103(d).

A member or proxy may use an electronic transmission to consent to an action. If an electronic transmission is used to consent to an action, the corporation must be able to determine from the transmission the date of the signature and that the consent was authorized by the member or a proxy. See Sections 102 (“electronic,” “sign,” and “signature”) and 103(d).

In some cases, more votes may be required to approve an action by less than unanimous consent than would be required to approve the same action at a meeting that is not attended by all members. For example, for a corporation with 1,000 members eligible to vote, unrevoked consents from at least 501 members are necessary to take action by consent under the default quorum and voting requirement provisions of Section 725. In contrast, at a meeting at which the minimum quorum is present, the same action could be taken with the vote of 251 members, or even fewer if not all members present vote. Where the act or the corporation’s articles of incorporation or bylaws provide for a greater voting requirement, however, the number of members required to consent to an action may be the same as the number of members required to approve the action at a meeting of members.

The phrase “one or more consents” is included in Section 704(a) to make it clear that all members do not need to sign the same piece of paper or electronic record. To minimize the possibility that action by consent will be authorized by action of persons who may no longer be members at the time the action is taken, Section 704(b) requires that all consents be signed within 60 days after the earliest signature date appearing on the consents delivered to the corporation.

2. Revocation of Consent

Before action by consent is effective, any member may withdraw a consent simply by delivering a revocation of consent to the corporation.

3. Notice to Nonvoting Members
Section 704 is applicable to all member actions, including the approval of fundamental corporate changes described in Chapters 9, 10, 11, and 12. Section 705(a) requires that notice of an annual, regular, or special meeting be given only to members entitled to vote at the meeting. The articles of incorporation or bylaws, however, may require that notice also be given to members not entitled to vote. If notice is required to be given to members not entitled to vote, Section 704(d) provides that notice to those members must be given at least 10 days before a corporate action taken by consent is effective.

§ 705. NOTICE OF MEETING

(a) A membership corporation must deliver notice to the members of the date, time, and place of each annual, regular, or special meeting of the members. If the board of directors has authorized participation by means of remote communication pursuant to Section 710 (remote participation in member meeting) for members of any class, the notice to the members of that class must describe the means of remote communication to be used. Except as provided in the articles of incorporation or the bylaws:

(1) the notice must be given no fewer than 10 nor more than 60 days before the meeting date; and

(2) the corporation must give notice only to members entitled to vote at the meeting as of the record date for determining the members entitled to notice of the meeting.

(b) Unless this [Act], the articles of incorporation, or the bylaws require otherwise, notice of an annual or regular meeting need not include a description of the purpose or purposes for which the meeting is called.

(c) Notice of a special meeting of members must include a description of the purpose or purposes for which the meeting is called.

(d) If not otherwise fixed under Section 703 (court-ordered meeting) or 707 (record date), the record date for determining members entitled to notice of and to vote at a meeting of the members is the day before the first notice is delivered to members.

(e) Unless the articles of incorporation or bylaws require otherwise, if a meeting of the members is adjourned to a different date, time, or place, notice need not be given of the new date, time, or place if the new date, time, or place is announced at the meeting before adjournment. If a new record date for the adjourned meeting is or must be fixed under Section 707, notice of the adjourned meeting must be given under this section to the members entitled to vote at the adjourned meeting as of the record date fixed for notice of the adjourned meeting.

(f) Except as provided in the articles of incorporation or bylaws, when giving notice of an annual or regular meeting of members, a nonprofit corporation must give notice of a matter a member intends to raise at the meeting if:
(1) requested in writing to do so by a person entitled to raise the matter at the
meeting; and

(2) the request is received by the secretary of the corporation at least ten days
before the corporation gives notice of the meeting.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 7.05. Cf. Model Business Corporation Act (2016 Revision), § 7.05.

CROSS-REFERENCES

Annual meeting, § 7.01.
“Deliver” defined, § 102.
“Membership corporation” defined, § 102.
Notice, § 103.
Notice otherwise required:
Amendment of articles of incorporation, § 903.
Amendment of Bylaws, § 922.
conversion, § 1252.
disposition of assets, § 1002.
dissolution, § 1102.
domestication, § 1242.
merger and membership exchange, § 1220.
Regular meeting, § 701.
Remote participation in members’ meetings, § 710.
Special meeting, § 702.
Waiver of notice, § 706.

OFFICIAL COMMENT

Members entitled to notice must be given notice of annual, regular, and special meetings pursuant to Section 705 unless the notice is waived pursuant to Section 706. Notice must be given at least 10 but not more than 60 days before the meeting date.

1. Members Entitled to Notice

Generally, only members who are entitled to vote at a meeting are entitled to notice. Thus, notice usually needs to be sent only to members entitled to vote for an election of directors or generally on other matters (in the case of an annual or regular meeting), and on matters within the specified purposes set forth in the notice (in the case of a special meeting), and only to such members on the record date. In addition, the articles of incorporation or bylaws may require that notice of meeting be given to all or specified voting groups of members who are not entitled to vote on the matters considered at those meetings.

2. Statement of Matters to be Considered at an Annual Meeting
Notice of all special meetings must include a description of the purpose or purposes for which the meeting is called and the matters acted upon at the meeting are limited to those within the notice of meeting. By contrast, the act does not require that the notice of an annual or regular meeting refer to any specific purpose or purposes, and any matter appropriate for member action may be considered. As recognized in Section 705(b), however, other provisions of the act provide that certain types of fundamental corporate changes may be considered at an annual or regular meeting only if specific reference to the proposed action appears in the notice of meeting. If the board of directors chooses, a notice of an annual or regular meeting may contain references to purposes or proposals not required by statute. In the event that management intends to present non-routine proposals for a member vote and members have not otherwise been informed of such proposals, good corporate practice suggests that references to such proposals be made in the notice. In any event, if a notice of an annual or regular meeting refers specifically to one or more purposes, the meeting is not limited to those purposes.

3. Record Date

The selection of the day before the notice is delivered as the catch-all record date under Section 705(d) is intended to permit the corporation to deliver notices to members on a given day without regard to any changes in membership during that day. For this reason, this section is consistent with the general principle set forth in the last sentence of Section 707(a) that the board of directors may not fix a retroactive record date.

4. Notice of Adjourned Meetings

Section 705(e) provides rules for adjourned meetings and determines whether new notice must be given to members. If a new record date is or must be fixed under Section 707(c), the 10 to 60 day notice requirement and all other requirements of Section 705 must be complied with because notice must be given to the members as of the new record date. In such circumstances, a new quorum for the adjourned meeting must also be established. See Section 725, which provides that if a quorum exists for a meeting, it is deemed to continue to exist automatically for an adjourned meeting unless a new record date is or must be set for the adjourned meeting.

5. Alternative Forms of Notice

The manner in which notice may be delivered to the members is governed by Section 103. A church or similar religious body may decide to provide for notice of meetings by announcement at church or religious services, in which case it should specify the frequency and timing of notice (e.g., “announcement at any two services held during different weeks within 30 days before the time at which the meeting of members will be held”). Other nonprofit corporations may choose to deliver notice in a manner similar to the way business corporations deliver notice to their shareholders.

§ 706. WAIVER OF NOTICE
(a) A member may waive any notice required by this [Act], the articles of incorporation, or the bylaws before or after the date and time of the meeting or action. The waiver must be in a record, be signed by the member entitled to the notice, and be delivered to the membership corporation for filing by the corporation with the minutes or corporate records.

(b) The attendance of a member at a meeting:

(1) waives objection to lack of notice or defective notice of the meeting, unless the member at the beginning of the meeting objects to holding the meeting or transacting business at the meeting;

(2) waives objection to consideration of a particular matter at the meeting that is not within the purpose described in the meeting notice, unless the member objects at the meeting to considering the matter.


CROSS-REFERENCES

Acceptance of waiver, § 723.
Action without meeting, § 704.
Meeting notice, § 705.
“Membership corporation” defined, § 102.
Notices and other communications, § 103.
Proxies, § 722.
Remote participation in shareholders’ meetings, § 710.
“Sign” defined, § 102.

OFFICIAL COMMENT

A notice of member meetings serves two principal purposes: (1) it advises members of the date, time and place of the annual, regular, or special meeting, and (2) in the case of a special meeting (or an annual or regular meeting at which fundamental changes may be made), it advises members of the purposes of the meeting. Section 706(b)(1) provides that attendance at a meeting constitutes waiver of any failure to receive the notice or defects in the statement of the date, time, and place of any meeting. Defects waived by attendance for this purpose include a failure to send the notice altogether, delivery to the wrong address, a misstatement of the date, time, or place of the meeting, and a failure to notice the meeting within the time periods specified in Section 705(a). If a member believes that the defect in or failure of notice was in some way prejudicial, the member must state at the beginning of the meeting, an objection to holding the meeting or transacting any business or the objection is waived. If this objection is made, the corporation may correct the defect by sending proper notice to the members for a subsequent meeting or by obtaining waivers of notice from all members who did not receive the notice required by Section 705.
For purposes of Section 706, “attendance” at a meeting involves the presence of the member in person or by proxy or, if authorized in accordance with Section 710, the member or proxy may attend by means of remote communication. A member who attends a meeting solely for the purpose of objecting to the notice is counted as present for purposes of determining whether a quorum is present. See Section 724 and the Official Comment.

In the case of special meetings, or annual or regular meetings at which fundamental corporate changes are considered, a second purpose of the notice is to inform members of the matters to be considered at the meeting. An objection that a particular matter is not within the stated purposes of the meeting cannot be raised until the matter is presented. Thus Section 706(b)(2) provides that a member waives this kind of objection by failing to object promptly when the matter is presented. If this objection is made, the corporation may correct the defect by sending proper notice to the members for a subsequent meeting or obtaining waivers of notice from all members. Whether a specific matter is within a stated purpose of a meeting is ultimately a matter for judicial determination, typically in a suit to invalidate action taken at the meeting brought by a member who was not present at the meeting or who was present at the meeting and preserved an objection under Section 706(b).

The purpose of both waiver rules in Section 706(b) is to require members with technical objections to holding the meeting or considering a specific matter to raise them at the outset and not reserve them to be raised only if they are unhappy with the outcome of the meeting. The rules set forth in this section differ in some respects from the waiver rules for directors set forth in Section 823 where a waiver is inferred if the director acquiesces in the action taken at a meeting even if the director raised a technical objection to the notice of a meeting at the outset.

§ 707. RECORD DATE

(a) The articles of incorporation or bylaws may fix or provide the manner of fixing the record date for one or more voting groups to determine the members entitled to notice of a meeting of the members, to demand a special meeting, to vote, or to take any other action. If the articles or bylaws do not fix or provide for fixing the record date, the board of directors of the membership corporation may fix the record date.

(b) A record date fixed under this section may not be more than 70 days before the meeting or action requiring a determination of members and may not be retroactive.

(c) A determination of members entitled to notice of or to vote at a meeting of the members is effective for any adjournment of the meeting unless the board of directors fixes a new record date, which it must do if the meeting is adjourned to a date more than 120 days after the date fixed for the original meeting.

(d) If a court orders a meeting adjourned to a date more than 120 days after the date fixed for the original meeting, it may provide that the original record date continues in effect or it may fix a new record date.
CROSS-REFERENCES

Annual meeting, § 701.
Court-ordered meeting, § 703.
“Membership corporation” defined, § 102.
Other record date provisions:
    action without meeting, § 704.
    notice of meeting, § 705.
    special meeting, § 702.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 707 authorizes the board of directors to fix record dates for determining members entitled to take any action unless the articles of incorporation or bylaws themselves fix or provide for the fixing of a record date. A separate record date may be established for each voting group entitled to vote separately on a matter at a meeting, or a single record date may be established for all voting groups entitled to participate in the meeting. If a record date for a specific action is not fixed by the articles, bylaws, or the board, the section of the act that deals with that action itself fixes the record date. For example, Section 705(d), relating to giving notice of a meeting, provides that the record date for determining who is entitled to notice of and to vote at a meeting (if not fixed by the articles, bylaws, or directors) is the close of business on the day before the date the corporation first gives notice to members of the meeting.

A record date may not be fixed more than 70 days before the meeting or action in question and may not be fixed retroactively. Once set, the same record date may be utilized for an adjournment of the meeting that reconvenes within 120 days after the date fixed for the original meeting or the board of directors may fix a new record date. If the adjourned meeting takes place more than 120 days after the date fixed for the original meeting, Section 707(c) requires that a new record date be fixed. But if an adjournment is ordered by a court, Section 707(d) allows the court to provide that the original record date continues to be applicable or to fix a different date. In any event, after a record date is fixed, if a new record date subsequently is or must be fixed under Section 707, Section 705 requires that new notice be given to the persons who are members entitled to vote as of the new record date, and Section 724 requires that a quorum be reestablished for that meeting.

§ 708. CONDUCT OF MEMBER MEETING

(a) At each meeting of members, an individual appointed in one of the following ways must preside as chair:

1) as provided in the articles of incorporation or bylaws;
(2) in the absence of a provision in the articles or bylaws, by the board of directors; or
(3) in the absence of both a provision in the articles or bylaws and an appointment by the board, by the members at the meeting.

(b) Except as provided in the articles of incorporation or bylaws, the chair determines the order of business and may establish rules for the conduct of the meeting.

(c) Any rules adopted for, and the conduct of, the meeting must be fair to the members.

(d) At the meeting the chair may announce when the polls close for each matter voted upon. If no announcement is made, the polls close upon the final adjournment of the meeting. After the polls close, no ballots, proxies, or votes, nor any revocations or changes to ballots, proxies, or votes may be accepted.


CROSS-REFERENCES

Annual meeting, § 7.01.
Court-ordered meeting, § 7.03.
Regular meeting, § 7.01.
Special meeting, § 7.02.

OFFICIAL COMMENT

Section 708 provides that, at any meeting of the members, there will be a chair who presides over the meeting. Inherent in the chair’s power in Section 708(b) to establish rules for the conduct of the meeting is the authority to require that the order of business be observed and that any discussion or comments from members or their proxies be confined to the business item under discussion. The rules for conduct of the meeting may cover such subjects as the proper means for obtaining the floor, who shall have the right to address the meeting, the manner in which members will be recognized to speak, time limits per speaker, the number of times a member may address the meeting, and the person to whom questions should be addressed. The chair must be fair in determining the order of business and in establishing rules for the conduct of the meeting so as not to unfairly foreclose the right of members – subject to the act, the articles of incorporation, and the bylaws – to raise items which are properly a subject for member discussion or action at some point in the meeting prior to adjournment.

The act provides that only business within the purpose or purposes described in the meeting notice may be conducted at a special meeting of members. See Sections 702(e) and 705(c).
§ 709. ACTION BY BALLOT

(a) Except as otherwise restricted by the articles of incorporation or bylaws, any action that may be taken at any meeting of members may be taken without a meeting if the membership corporation delivers notice that includes a ballot to every member entitled to vote on the matter.

(b) A ballot must:

(1) be in a record;

(2) set forth each proposed action;

(3) provide an opportunity to vote for, or withhold a vote for, each candidate for election as a director; and

(4) provide an opportunity to vote for or against each other proposed action.

(c) Approval by ballot pursuant to this section of action other than election of directors is valid only when the number of votes cast by ballot equals or exceeds the quorum required to be present at a meeting authorizing the action, and the number of approvals equals or exceeds the number of votes that would be required to approve the matter at a meeting at which the total number of votes cast was the same as the number of votes cast by ballot.

(d) All solicitations for votes by ballot must:

(1) indicate the number of responses needed to meet the quorum requirements;

(2) state the percentage of approvals necessary to approve each matter other than election of directors; and

(3) specify the time by which a ballot must be received by the membership corporation in order to be counted.

(e) Except as otherwise provided in the articles of incorporation or bylaws, a ballot may not be revoked.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 7.09.

CROSS-REFERENCES

Acceptance of ballot, § 723.

Action by members by consent, § 704.
Election of directors, § 727.
“Members” defined, § 102.
“Membership corporation” defined, § 102.

OFFICIAL COMMENT

If ballots are used in the manner authorized by Section 709, the membership corporation does not need to convene a meeting of its members. Thus the use of ballots under Section 709 is different from the distribution of ballots at a meeting to facilitate voting at the meeting. If ballots are to be used in the manner authorized by Section 709, the corporation must deliver a notice to each member entitled to vote, except that Section 103 will apply to the delivery of the notice and excuse the corporation from giving notice with an accompanying ballot to members that are not reachable.

Voting by ballot under this section is an alternative to acting by consent under Section 704. In effect, the use of ballots is a way to conduct a vote of members remotely instead of at a meeting. Thus Section 709(d) provides rules that are substantively similar to the rules on quorums and required vote applicable to member meetings, but which differ from the rules in Section 704 on action by consent.

§ 710. REMOTE PARTICIPATION IN MEMBER MEETING

(a) Members of any class may participate in any meeting of members by means of remote communication to the extent the board of directors authorizes such participation for that class. Participation as a member by means of remote communication is subject to any guidelines and procedures the board of directors adopts that conform to Section 708(c).

(b) Members participating by means of remote communication are deemed present and may vote at the meeting if the membership corporation has implemented reasonable measures:

(1) to verify that each person participating remotely as a member is a member; and

(2) to provide the members a reasonable opportunity to participate in the meeting and to vote on matters submitted to the members, including an opportunity to communicate, and to read or hear the proceedings of the meeting, substantially concurrently with the proceedings.

OFFICIAL COMMENT

Section 710 permits members to participate in meetings by means of remote communication, such as over the Internet or through telephone conference calls, subject to the conditions set forth in Section 710(b) and any other guidelines and procedures that the board of directors adopts. This would include the use of electronic ballots to the extent authorized by the
board of directors. This authorization extends as well to anyone to whom a member has granted a proxy appointment. Section 710(a) ensures that the board of directors has the sole discretion to determine whether to allow members to participate by means of remote communication.

Section 710 allows the board of directors to limit participation by means of remote communication to all members of a particular class, but does not permit the board of directors to limit such participation to particular members within a class.

Section 710 is not intended to expand the rights to participate in meetings or otherwise alter the ability of the board of directors or the chair to conduct meetings, pursuant to section 708, in a manner that is fair. For example, many corporations limit member comments and, if that practice is fair to members consistent with section 708, that practice is not changed by section 710. The two requirements under section 710(b) reflect the minimum deemed necessary to safeguard the integrity of the members’ meeting. Section 710 specifically gives the board of directors the flexibility and discretion to adopt additional guidelines and procedures for allowing members to participate in a meeting by means of remote communication.

To give corporations the flexibility to choose the most efficient means of remote communication under Section 710(a), the board of directors may require that members communicate their desire to participate by a certain date and condition the provision of remote communication or the form of communication to be used on the affirmative response of a certain number or proportion of members eligible to participate. If the board of directors authorizes member participation by means of remote communication pursuant to Section 710, that authorization and the process for participating by remote means of communication must be included in the meeting notice required by Section 705.

[Subchapter] B
VOTING

§ 720. Members list for meeting.
§ 721. Voting entitlement of members.
§ 722. Proxies.
§ 723. Acceptance of votes and other instruments.
§ 724. Quorum and voting requirements for voting groups.
§ 725. Action by single and multiple voting groups.
§ 726. Different quorum or voting requirements.
§ 727. Voting for directors.
§ 728. Inspectors of election.

§ 720. MEMBERS LIST FOR MEETING

(a) After fixing a record date for a meeting, a membership corporation must prepare an alphabetical list of the names of all its members who are entitled to vote at that meeting of the members. The list must show the address of and number of votes each member is entitled to cast at the meeting.
(b) The list of members must be available for inspection by any member, beginning two business days after notice of the meeting is given for which the list was prepared and continuing through the meeting, at the membership corporation’s principal office or at a place identified in the meeting notice in the city where the meeting will be held. A member or the member’s agent is entitled on demand in a record to inspect and, subject to the requirements of Section 402(c) (inspection rights of members), to copy the list, during regular business hours and at the member’s expense, during the period it is available for inspection.

(c) The membership corporation must make the list of members available at the meeting, and a member or the member’s agent is entitled to inspect the list at any time during the meeting or any adjournment.

(d) If a membership corporation refuses to allow a member or the member’s agent to inspect the list of members before or at the meeting (or copy the list as permitted by subsection (b)), the [name or describe] court of the county where the corporation’s principal office (or, if none in this state, its registered office) is located, on application of the member, may:

1. summarily order the inspection or copying at the corporation’s expense;
2. postpone the meeting for which the list was prepared until the inspection or copying is complete;
3. order the corporation to pay the member’s costs (including reasonable counsel fees) incurred to obtain the order; and
4. order other appropriate relief.

(e) Refusal or failure to prepare or make available the list of members does not affect the validity of action taken at the meeting.

(f) Instead of making the list of members available as provided in subsection (b), a membership corporation may state in a notice of meeting that the corporation has elected to proceed under this subsection. A member of a corporation that has elected to proceed under this subsection must state in the member’s demand for inspection a proper purpose for which inspection is demanded. Within ten business days after receiving a demand under this subsection, the corporation must deliver to the member making the demand an offer of a reasonable alternative method of achieving the purpose identified in the demand without providing access to or a copy of the list of members. An alternative method that reasonably and in a timely manner accomplishes the proper purpose set forth in the demand relieves the corporation from making the list of members available under subsection (b), unless within a reasonable time after acceptance of the offer the corporation fails to do the things it offered to do. Any rejection of the corporation’s offer must be in a record and must indicate the reasons the alternative proposed by the corporation does not meet the proper purpose of the demand.
OFFICIAL COMMENT

1. When the List Must be Available

Section 720(b) and (c) govern when the list of members must generally be available for inspection. The requirement of availability for continuous inspection permits the membership corporation and others soliciting votes to be on a relatively equal footing. If, however, notice of the meeting is waived by all the members, the list need be available only at the meeting itself under Section 720(c) unless one or more waivers are conditioned upon receipt of the list.

2. Where the List Must be Maintained

Sections 720(b) and (c) also govern where the membership corporation must maintain the list. If the corporation changes the location of its meeting, it may correspondingly change the location of the list under Section 720(b).

3. Form in Which the List is Maintained

Section 720 does not require the list of members to be in any particular form. It may be maintained, for example, in electronic form. If the list is maintained in other than written form, however, suitable equipment must be provided so that a comprehensible list may be inspected by a member as required by Section 720.

4. Consequences of Failing to Prepare the List or Refusal to Make it Available
Section 720 creates a corporate obligation rather than an obligation imposed upon a corporate officer. If the membership corporation fails to prepare the list or refuses to permit a member to inspect it, either before the meeting as required by Section 720(b) or at the meeting itself as required by Section 720(c), a member may apply to the appropriate court under Section 720(d). If the court orders a copy of the list to be provided to the members, the copying is at the corporation’s expense; if the corporation produces the list voluntarily pursuant to Section 720(b) or (c), any inspection and copying are the member’s expense.

This judicial remedy is the only sanction for violation of Section 720 since Section 720(e) provides that the failure to prepare, maintain, or produce the list does not affect the validity of any action taken at the meeting.

5. Right to Obtain a Copy of the List

Section 720(b) permits members to “inspect” the list without limitation, but permits the member to “copy” the list only if the member complies with the requirement of Section 402(c) that the demand be “made in good faith and for a proper purpose.” The right to copy the list may be satisfied at the corporation’s option, if reasonable, by furnishing to the member a copy of the list upon payment of a reasonable charge. See Sections 403(b) and (c). The distinction between “inspection” and “copying” set forth in Section 720(b) reflects an accommodation between competing considerations of permitting members access to the list before a meeting and possible misuse of the list.

6. Relationship to Right to Inspect Corporate Records Generally

Section 720 creates a right of members to inspect a list of members in advance of and at a meeting that is independent of the rights of members to inspect corporate records under Subchapter 4A. A member may obtain the right to inspect the list of members as provided in Subchapter 4A without regard to the provisions relating to the pendency of a meeting in Section 720, and similarly the limitations of Subchapter 4A are not applicable to the right of inspection created by Section 720 except to the extent the member seeks to copy the list in advance of the meeting.

The right to inspect under Subchapter 4A is also broader in the sense that in some circumstances the member may make or receive copies of the documents the member is entitled to inspect. See Section 403.

§ 721. VOTING ENTITLEMENT OF MEMBERS

(a) Except as provided in the articles of incorporation or bylaws, a member is entitled to one vote on:

(1) each candidate for election as a director;
(2) approval of a fundamental transaction; and

(3) any other matter on which the articles or bylaws require a vote of the members.

(b) Except as provided in the articles of incorporation or bylaws, if a membership stands of record in the names of two or more persons, then acts with respect to voting the membership have the following effects:

(1) if only one person acts, that act binds all; and

(2) if more than one person acts, the voting of the membership is divided on a pro rata basis among all of the persons acting.


CROSS-REFERENCES

Acceptance of votes, § 723.
Meetings of members, §§ 701-703.
Proxy voting, § 722.
Voting by nominees, § 723.
Voting by voting groups, §§ 102, 724, 725.

OFFICIAL COMMENT

Section 721(a) provides that each member, regardless of class, is entitled to one vote unless otherwise provided in the articles of incorporation or bylaws. The articles or bylaws may provide for multiple or fractional votes, and may provide that some classes of members are nonvoting on some or all matters, or that some classes of members have a single vote per member or different multiple or fractional votes per member, or that some classes constitute one or more separate voting groups and are entitled to vote separately on the matter.

In order to reflect the possibility that members may have multiple or fractional votes, all provisions relating to quorums, voting, and similar matters in the act are phrased in terms of “votes” rather than “members.”

§ 722. PROXIES

(a) Except as provided in the articles of incorporation or bylaws, a member may vote in person or by proxy.

(b) A member or the member’s agent or attorney-in-fact may appoint a proxy to vote or otherwise act for the member by signing an appointment form in a record. An appointment
form must contain or be accompanied by information from which it can be determined that the
member or the member’s agent or attorney-in-fact authorized the appointment of the proxy.

(c) An appointment of a proxy is effective when a signed appointment in a record is
received by the inspectors of election, the officer or agent of the membership corporation
authorized to count votes, or the secretary. An appointment is valid for 11 months unless a longer
period, which may not exceed three years, is expressly provided in the appointment form.

(d) The death or incapacity of the member appointing a proxy does not affect the
right of the membership corporation to accept the proxy’s authority unless notice of the death or
incapacity is received by the inspectors of election, the officer or agent authorized to count votes,
or the secretary before the proxy exercises his authority under the appointment.

(e) Subject to Section 723 (acceptance of votes and other instruments) and to any
express limitation on the proxy’s authority stated in the appointment form, a membership
corporation is entitled to accept the proxy’s vote or other action as that of the member making
the appointment.

(2016 Revision), § 7.22.

CROSS-REFERENCES

Acceptance of proxy votes, § 7.23.
“Membership corporation” defined, § 102.
Notices and other communications, § 103.
“Secretary” defined, § 102.

OFFICIAL COMMENT

1. Nomenclature

The word “proxy” is often used ambiguously, sometimes referring to the grant of
authority to vote, sometimes to the document granting the authority, and sometimes to the person
to whom the authority is granted. In the act the word “proxy” is used only in the last sense; the
term “appointment form” is used to describe the document or communication appointing the
proxy; and the word “appointment” is used to describe the grant of authority to vote.

Section 722(b) permits the practice whereby members who have been provided in proxy
materials with a personal identification number may submit their vote and identifying number to
a person who, acting as the member’s agent, causes that information to be transmitted, directly or
indirectly, to the inspector of election.

Section 103 governs when an appointment form is “received” and “effective.” If the
appointment form contains an express limitation on the power to vote or direction as to how to
vote the membership on a particular matter, the corporation must count the votes in a manner
consistent with that limitation or direction. See section 722(e).

3. **Duration of Appointment**

An appointment form that contains no expiration date is valid for 11 months unless it
provides for a longer period of up to three years. This ensures that in the normal course a new
appointment will be solicited at least once every 12 months. An appointment form may validly
specify its term if the parties agree, which may be longer or shorter than 11 months.

Although death or incapacity of the appointing member revokes an agency appointment
under common law principles, Section 722(d) modifies the common law rule to provide that the
membership corporation may accept the vote of the proxy until the appropriate person receives
notice of the member’s death or incapacity. In view of the widespread dispersal of members in
many corporations, it is not feasible for the corporation to learn of these events independently of
notice. On the other hand, Section 722(d) does not affect the validity of the appointment or its
manner of exercise as between the proxy and the personal representatives of the decedent or
incompetent.

§ 723. **ACCEPTANCE OF VOTES AND OTHER INSTRUMENTS**

(a) If the name signed on a ballot, consent, waiver, demand, or proxy appointment
corresponds to the name of a member, the membership corporation if acting in good faith is
entitled to accept the ballot, consent, waiver, demand, or proxy appointment and give it effect as
the act of the member.

(b) If the name signed on a ballot, consent, waiver, demand, or proxy appointment
does not correspond to the name of its member, the membership corporation if acting in good
faith is nevertheless entitled to accept the ballot, consent, waiver, demand, or proxy appointment
and give it effect as the act of the member if:

1. the member is an entity and the name signed purports to be that of an
   officer or agent of the entity;

2. the name signed purports to be that of an administrator, executor,
   guardian, or conservator representing the member and, if the corporation requests, evidence of
   fiduciary status acceptable to the corporation has been presented with respect to the ballot,
   consent, waiver, demand, or proxy appointment;

3. the name signed purports to be that of a receiver or trustee in bankruptcy
   of the member and, if the corporation requests, evidence of this status acceptable to the
   corporation has been presented with respect to the ballot, consent, waiver, demand, or proxy
   appointment;
(4) the name signed purports to be that of a beneficial owner or attorney-in-fact of the member and, if the corporation requests, evidence acceptable to the corporation of the signatory’s authority to sign for the member has been presented with respect to the ballot, consent, waiver, demand, or proxy appointment;

(5) two or more persons are the member as co-tenants or fiduciaries and the name signed purports to be the name of at least one of the co-owners and the person signing appears to be acting on behalf of all the co-owners.

(c) The membership corporation is entitled to reject a ballot, consent, waiver, demand, or proxy appointment if the secretary or other officer or agent authorized to tabulate votes, acting in good faith, has reasonable basis for doubt about the validity of the signature on it or about the signatory’s authority to sign for the member.

(d) The membership corporation, its officer or agent, any person authorized by the corporation, or an inspector of election appointed under Section 728 (inspectors of election) that accepts or rejects a ballot, consent, waiver, demand, or proxy appointment in good faith and in accordance with the standards of this section or Section 722(b) (proxies) is not liable in damages to the member for the consequences of the acceptance or rejection.

(e) Corporate action based on the acceptance or rejection of a ballot, consent, waiver, or proxy appointment under this section is valid unless a court of competent jurisdiction determines otherwise.

(f) If an inspector of election has been appointed under Section 728, the inspector of election may request information and make determinations under Sections 723(a), (b), and (c). Any determination made by the inspector of election under those subsections is controlling.


CROSS-REFERENCES

Action by ballot, § 709.
Consents, § 704.
“Entity” defined, § 102.
Inspectors of election, § 728.
“Membership corporation” defined, § 102.
Officers, § 840.
Proxies, § 722.
“Secretary” defined, § 102.
“Sign” defined, § 102.
Waiver of notice, § 706.

OFFICIAL COMMENT
Membership corporations are often asked to accept a written instrument as evidence of action by a member. These instruments usually involve appointment forms for a proxy to vote on behalf of a member, but may also include waivers of notice, consents to action without a meeting, requests for a special meeting of members, and similar instruments involving action by the members. Included within the scope of this section are both ballots used as provided in Section 709 as a substitute for a vote at a meeting and also ballots distributed at a meeting for the use of the members and proxies in attendance at the meeting. Usually the corporation or its officers will have no personal knowledge of the circumstances under which the instrument was executed and no way of verifying whether the signature on the instrument is in fact the signature of the member or other appropriate person.

Section 723 establishes general rules permitting the membership corporation, its officers and agents, and any inspector of election appointed under section 728 to accept these instruments if they appear to be signed by a member or by a person who has authority to execute the instrument for the member and they are accompanied by whatever authenticating evidence is requested. Section 723 also establishes general rules for rejecting these instruments. The rules set forth in this section are not exclusive and may be supplemented by additional rules established by the corporation.

A purpose of Section 723 is to protect the membership corporation, its officers and agents and any inspector of election from liability for damages to a member if action is taken in accordance with Section 723. Under Section 723(d) there is no liability to the member if the corporation or inspector of election, acting in good faith, accepts an instrument that meets the requirements of Section 723(a) or (b) or accepts an electronic transmission authorized by Section 722(b), even if it turns out that the execution was invalid or unauthorized. Similarly, no liability exists if an instrument is rejected in accordance with Section 723(c) because the corporation or inspection of election, again acting in good faith, has a “reasonable basis for doubt,” even though it turns out that the instrument was properly executed by the member. This protection extends to officers and other persons who are authorized by the corporation to accept or reject an instrument identified in Section 723. Section 723 does not, however, address the question whether an action was properly or improperly taken or approved, and Section 723(e) makes clear that the validity of corporate action is ultimately a matter for judicial resolution through review of the results of a vote in a suit to enjoin or compel corporate action. It is contemplated that any such proceeding will be brought promptly, typically before the corporate action is consummated or the corporation’s position otherwise changes in reliance on the vote, and that any proceeding that is not brought promptly under the circumstances would normally be barred because of laches.

Similarly, Section 723 does not address the liability of the proxy to the member for exercising authority beyond that granted or for disobeying instructions. These matters are governed by the law of agency and not by Section 723.

A corporation may wish to establish guidelines that it will follow in determining whether to accept a vote, ballot, consent, waiver, or proxy appointment to provide consistency in the corporation’s application of the general rules set forth in section 723.
If an inspector of election has been appointed under Section 729, the inspector has the authority under Section 723, as well as the corporation. If there is a difference in a determination by the corporation and the inspector, the inspector’s determination controls as against the corporation under Section 723(f).

§ 724. QUORUM AND VOTING REQUIREMENTS FOR VOTING GROUPS

(a) Members entitled to vote as a separate voting group may take action on a matter at a meeting only if a quorum of those members exists with respect to that matter. Except as provided in the articles of incorporation or bylaws, a majority of the votes entitled to be cast on the matter by the voting group constitutes a quorum of that voting group for action on that matter.

(b) Except as provided in the articles of incorporation or bylaws, once a member is present or represented for any purpose at a meeting, the member is deemed present for quorum purposes for the remainder of the meeting and for any adjournment of that meeting unless a new record date is or must be fixed for that adjourned meeting.

(c) If a quorum exists, action on a matter (other than the election of directors) by a voting group is approved if the votes cast within the voting group favoring the action exceed the votes cast opposing the action, unless the articles of incorporation or bylaws require a greater number of affirmative votes.

(d) An amendment of the articles of incorporation or bylaws adding, changing, or deleting a quorum or voting requirement for a voting group greater than specified in Section 724(a) or (c) is governed by Section 726 (different quorum or voting requirements).

(e) If a meeting cannot be organized because a quorum is not present, those members present may adjourn the meeting to such time and place as they may determine. The articles of incorporation or bylaws may provide that when a meeting that has been adjourned for lack of a quorum is reconvened, those members present, although less than a quorum as fixed in this section, the articles, or the bylaws, nonetheless constitute a quorum if the original notice of the meeting, or a notice of the adjourned meeting, states that those members who attend a meeting that has been adjourned for lack of a quorum will constitute a quorum even though they are less than a quorum.

(f) The election of directors is governed by Section 727 (voting by directors).


CROSS-REFERENCES

Adjourned meeting record date, § 707.
Amendment of articles of incorporation, Subch. 10A.
OFFICIAL COMMENT

Section 7.24 establishes general quorum and voting requirements for voting groups for purposes of the act. As defined in Section 102, a “voting group” consists of all members of a class that under the articles of incorporation, bylaws, or the act are entitled to vote and be counted together collectively on a matter. Members entitled to vote “generally” on a matter (that is, all members entitled to vote on the matter by the articles, bylaws, or the act that do not expressly have the right to be counted or tabulated separately) are a single voting group. The determination of which members form part of a single voting group must be made from the provisions of the articles, bylaws, and the act. On most matters coming before meetings of the members, only a single voting group, consisting of a class of members, will be involved, and action on such a matter is effective when approved by that voting group pursuant to Section 724. See Section 725(a).

The voting group concept permits a single section of the act to deal with quorum and voting rules applicable to a variety of single and multiple voting group situations.

1. Determination of Voting Groups under the Act

Under the act, classes of members are generally not entitled to vote separately by voting group except to the extent specifically authorized by the articles of incorporation or bylaws. But Chapters 10 and 12 grant classes of members the right to vote separately when fundamental changes are proposed that may adversely affect that class. Under the act even a class that is expressly described as nonvoting under the articles of incorporation or bylaws may be entitled to vote separately on an amendment to the articles of incorporation or bylaws that affects the class in a designated way. See Section 1004(d).

In addition to the provisions of the act, separate voting by voting group may be authorized by the articles of incorporation or bylaws (except that the statutory privilege of voting by separate voting groups cannot be diluted or reduced). On some matters the board of directors may condition its submission of matters to members on their approval by specific voting groups designated by the board of directors. Sections 724 and 725 establish the mechanics by which all voting by single or multiple voting groups is carried out.

In some situations, members of a single class may be entitled to vote in two different voting groups. See the Official Comment to Section 725.

2. Quorum and Voting Requirements in General
A nonprofit corporation’s determination of the voting groups entitled to vote, and the quorum and voting requirements applicable to that determination, should be determined separately for each matter coming before a meeting. As a result, different quorum and voting requirements may be applicable to different portions of a meeting, depending on the matter being considered. In the normal case where only a single voting group is entitled to vote on all matters coming before a meeting of members, a single quorum and voting requirement will usually be applicable to the entire meeting.

3. Quorum Requirements for Action by Voting Group

Under Section 724(b), once a member is present at a meeting, the member is deemed present for quorum purposes throughout the meeting. Thus, a voting group may continue to act despite the withdrawal of members. The articles of incorporation or bylaws, however, may modify this default rule.

A member who comes to a meeting to object on grounds of lack of notice is considered present for purposes of determining the presence of a quorum.

If a new record date is set, new notice must be given to members of a voting group and a quorum must be established from within the members of that voting group as of the new record date.

4. Voting Requirements for Approval by Voting Group

Section 724(c) provides that an action (other than the election of directors, which is governed by Section 727) is approved by a voting group at a meeting at which a quorum is present if the votes cast in favor of the action exceed the votes cast opposing the action, unless the articles of incorporation or bylaws require a greater number of votes. This default rule differs from a formulation appearing in some state statutes that an action is approved at a meeting at which a quorum is present if it receives the affirmative vote of a majority of the members represented at that meeting. That formulation in effect treated abstentions as negative votes; the act treats them truly as abstentions.

5. Modification of Standard Requirements

The articles of incorporation or bylaws may modify the quorum and voting requirements of Section 724 for a single voting group or for all voting groups entitled to vote on any matter. The articles or bylaws may increase the quorum and voting requirements to any extent desired up to and including unanimity upon compliance with Section 726. They may also require that members of different classes are entitled to vote separately or together on specific issues or provide that actions are approved only if they receive the favorable vote of a majority of the members of a voting group present at a meeting at which a quorum is present. The articles or bylaws may also decrease the quorum requirement as desired.
Many nonprofit corporations have a low member turnout and need a low quorum to hold meetings of the members. In recognition of this need, this section does not set a lower limit on what the articles of incorporation or bylaws may set as a quorum requirement. For example, the bylaws may provide that a quorum is composed of those members who attend a meeting. This insures a quorum so long as one member is present.

§ 725. ACTION BY SINGLE AND MULTIPLE VOTING GROUPS

(a) If this [Act], the articles of incorporation, or the bylaws provide for voting by a single voting group on a matter, action on that matter is taken when voted upon by that voting group as provided in Section 724 (quorum and voting requirements for voting groups).

(b) If this [Act], the articles of incorporation, or the bylaws provide for voting by two or more voting groups on a matter, action on that matter is taken only when voted upon by each of those voting groups counted separately as provided in Section 724. Action may be taken by different voting groups on a matter at different times.


CROSS-REFERENCES

Change of voting group requirements, § 726.
Number of votes per member, § 721.
Quorum and voting requirements, § 724.
Supermajority requirements, § 726.
Voting by voting groups on amendments of articles of incorporation, § 1004.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 725(a) provides that when a matter is to be voted upon by a single voting group, action is taken when the voting group votes upon the action as provided in Section 724. In most instances the single voting group will consist of all the members of the class or classes entitled to vote by the articles of incorporation or bylaws. Voting by two or more voting groups as contemplated by Section 725(b) is the exceptional case.

Implicit in Section 725(b) are the concepts that (1) different quorum and voting requirements may be applicable to different matters considered at a single meeting, and (2) different quorum and voting requirements may be applicable to different voting groups voting on the same matter. See the Official Comment to Section 724. Each group entitled to vote must independently meet the quorum and voting requirements established by Section 724. If a quorum is present for one or more voting groups but not for all voting groups, Section 725(b) provides that the voting groups for which a quorum is present may vote upon the matter, even though their vote alone will not be sufficient for the matter to be approved.
A single meeting, furthermore, may consider matters on which action by several voting groups is required and also matters on which only a single voting group may act. Action may be taken on the matters on which the single voting group may act even though no quorum is present to take action on other matters.

Normally, each class of members will participate in only a single voting group. But since members entitled by the articles of incorporation or bylaws to vote generally on a matter are always entitled to vote in the voting group consisting of the general voting members, in some instances classes of members may be entitled to be counted in two voting groups. This will occur whenever a class of members entitled to vote generally on a matter under the articles or bylaws is affected by the matter in a way that gives rise to the right to have its vote counted separately as an independent voting group under the act.

§ 726. MODIFYING QUORUM OR VOTING REQUIREMENTS

(a) The articles of incorporation or bylaws may provide for a higher or lower quorum or voting requirement for members (or voting groups of members) than is provided for by this Act.

(b) An amendment to the articles of incorporation or bylaws that adds, changes, or deletes a quorum or voting requirement must meet the same quorum requirement and be adopted by the same vote and voting groups required to take action under the quorum and voting requirements then in effect or proposed to be adopted, whichever is greater.


CROSS-REFERENCES

Amendment of articles of incorporation, Ch. 10A.
Amendment of bylaws, Ch. 10B.
Quorum and voting requirements in general, § 725.
Voting by voting group, § 725.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 726(a) permits the articles of incorporation or bylaws to increase or decrease the quorum or voting requirements for approval of an action by members to any desired level, so long as the change is adopted in accordance with the requirements of section 726. For example, a “supermajority” provision that requires an 80% affirmative vote of all eligible votes of a voting group present at the meeting may not be removed from the articles or reduced in any way except by an 80% affirmative vote. If the 80% requirement is coupled with a quorum requirement for a voting group that members entitled to cast two-thirds of the total votes must be present in person
or by proxy, both the 80% voting requirement and the two-thirds quorum requirement are
immune from reduction except at a meeting of the voting group at which the two-thirds quorum
requirement is met and the reduction is approved by an 80% affirmative vote.

If the proposal is to increase the 80% voting requirement to 90%, that proposal must be
approved by a 90% affirmative vote at a meeting of the voting group at which the two-thirds
quorum requirement is met; if the proposal is to increase the two-thirds quorum requirement to
three-quarters without changing the 80% voting requirement, that proposal must be approved by
an 80% affirmative vote at a meeting of the voting group at which a three-quarters quorum
requirement is met.

§ 727. VOTING FOR DIRECTORS

(a) Except as provided in the articles of incorporation or bylaws, directors of a
membership corporation are elected by a plurality of the votes cast by the members entitled to
vote in the election at a meeting at which a quorum is present.

(b) Members do not have a right to cumulate their votes for directors.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 7.27. Cf. Model Business Corporation Act
(2016 Revision), § 7.28.

CROSS-REFERENCES

“Membership corporation” defined, § 102.
Notice of meeting, see § 705.
Notices and other communications, see § 103.
Proxies, § 722.
Quorum of members, § 724.
“Voting group” defined, § 102.

OFFICIAL COMMENT

As used in Section 727(a), election by a “plurality” means that the individuals with the
largest number of votes are elected as directors up to the maximum number of directors to be
chosen at the election. In elections in which several factions are competing within a voting
group, an individual may be elected with votes of fewer than a majority of the votes cast. The
articles of incorporation or bylaws of a membership corporation may, however, provide a
different manner of election of directors.

The entire board of directors may be elected by a single voting group or the articles of
incorporation may provide that different voting groups are entitled to elect a designated number
or fraction of the board of directors. See Section 804. Elections are contested only within specific
voting groups.
This edition of the act continues the decision to eliminate cumulative voting. Because the act at one time permitted a nonprofit corporation to provide for cumulative voting, existing cumulative voting rights are preserved by Section 1401(c).

§ 728. INSPECTORS OF ELECTION

(a) A membership corporation may appoint one or more inspectors to act at a meeting of members in connection with determining voting results. Each inspector must agree in a record that the inspector will faithfully execute the duties of inspector with strict impartiality and according to the best of the inspector’s ability. The inspectors may appoint or retain other persons to assist the inspectors in the performance of the duties of inspector under subsection (b), and may rely on information provided by those persons and other persons, including those appointed to count votes, unless the inspectors believe reliance is unwarranted.

(b) The inspectors must:

1. ascertain the number of members and their voting power;
2. determine the members present at a meeting;
3. determine the validity of proxies and ballots;
4. count the votes; and
5. determine and report the results.

(c) In performing their duties, the inspectors may examine:

1. the proxy appointment forms and any other information provided in accordance with Section 722(b) (proxies);
2. any envelope or related writing submitted with those appointment forms;
3. any ballots;
4. any evidence or other information specified in Section 724 (quorum and voting requirements for voting groups); and
5. the relevant books and records of the membership corporation relating to its members and their entitlement to vote.

(d) The inspectors also may consider other information that they believe is relevant and reliable for the purpose of performing any of the duties assigned to them pursuant to subsection (b).
(e) An inspector and any person appointed by an inspector to assist with the inspector’s duties may, but need not, be a director, member of a designated body, member, officer, or employee of the membership corporation. A person who is a candidate for office to be filled at the meeting may not be an inspector or a person so appointed.


CROSS-REFERENCES

“Membership corporation” defined, § 102.
Officers of the corporation, § 840.
Proxies, § 722.

OFFICIAL COMMENT

Section 728(a) permits a membership corporation to appoint inspectors of election. The selection of inspectors should usually be made by responsible officers or by the directors, as authorized either generally or specifically in the corporation’s bylaws. Alternate inspectors could also be designated to replace any inspector who fails to act. The requirement of a report in a record is to facilitate judicial review of determinations made by inspectors. The ability of inspectors to retain other persons to assist them does not limit the ability of the corporation also to appoint others, such as a vote tabulator to assist in the vote counting process.

To determine the validity of proxy appointments and ballots, depending on the issues presented, the inspectors of election may be required to determine whether appointment forms have been validly executed by the member, to identify the latest executed appointment form and to determine whether the proxy cast more votes than the member was entitled to cast. The inspectors are expected to apply the provisions of Chapter 7 regarding acceptance of proxy appointments and voting, including those in Sections 708(d), 722(h), and 724. In the event of a challenge of any determination by the inspectors in a court of competent jurisdiction, the court should give such weight to determinations of fact by the inspectors, as it deems appropriate, taking into account the relationship of the inspectors, if any, to the management of the nonprofit corporation and other persons interested in the outcome of the vote, the evidence available to inspectors, whether their determinations appear to be consistent and reasonable, and such other circumstances as the court regards as relevant. The court may review de novo all determinations of law made by the inspectors.

Section 728(d) gives the inspectors broad discretion with respect to the information they may consider but does not require that they take any specific action with respect to such information other than to specify in their report the information they considered and the other details listed in section 728(d).
§ 730. VOTING AGREEMENTS

(a) Except as provided in the articles of incorporation or bylaws, two or more members may provide for the manner in which they will vote by signing an agreement in a record for that purpose. A voting agreement is valid for the period provided in the agreement.

(b) A voting agreement created under Section 730 is specifically enforceable, except that a voting agreement is not enforceable to the extent that enforcement of the agreement would violate the purposes of the membership corporation.


CROSS-REFERENCES

Corporate purposes, § 3.01.
“Member” defined, § 102.
“Membership corporation” defined, § 102.

OFFICIAL COMMENT

Section 730(a) explicitly recognizes agreements among two or more members as to voting, except as provided in the articles of incorporation or bylaws. The only formal requirements are that they be in a record and signed by all the participating members. In other respects their validity is to be judged like any other contract.

A voting agreement may provide its own enforcement mechanism, such as by the appointment of a proxy to vote for the members that are parties to the agreement. If no enforcement mechanism is provided, a court may order specific enforcement of the agreement and order the votes cast as the agreement contemplates. A voting agreement is not enforceable, however, to the extent that its enforcement would violate the nonprofit corporation’s purposes.

[Chapter] 8

DIRECTORS AND OFFICERS

Subchapter
A. Board of Directors
B. Meetings and Action of the Board
C. Directors
D. Officers
E. Indemnification and Advancement of expenses
F. Conflicting Interest Transactions
§ 801. Requirement for and functions of board of directors.

(a) A nonprofit corporation must have a board of directors.

(b) Except as provided in Section 812 (designated body), all corporate powers must be exercised by or under the authority of the board of directors of the nonprofit corporation, and the activities and affairs of the corporation must be managed by or under the direction, and subject to the oversight, of its board of directors.


CROSS-REFERENCES

Designated body, § 812.
Director standards of conduct, § 830.
Indemnification, §§ 850 through 858.
Officers, §§ 840 and 841.

OFFICIAL COMMENT

Section 801(a) requires that every nonprofit corporation have a “board of directors.” The definition of “board of directors” in Section 102 provides that the term refers to “the group of individuals responsible for the management of the activities and affairs of the nonprofit corporation, regardless of the name used to refer to the group.” Thus the board of directors may be referred to as the “board of trustees” or by some other name. Regardless of the name by which it is known, if a group satisfies the definition of “board of directors” it will have that status.
That term “board of directors” is defined in Section 102 to include a designated body to the extent the powers, functions, or authority of the board have been vested in the designated body. The ability to create one or more designated bodies permits wide flexibility when designing the governance structure of a particular corporation.

In Section 801(b) the phrase “by or under the direction, and subject to the oversight, of” encompasses the varying functions of boards of directors of different nonprofit corporations. In some corporations, the board of directors may be involved in the day-to-day activities and affairs and it may be reasonable to describe management as being “by” the board of directors. In many other corporations, the activities and affairs are managed “under the direction, and subject to the oversight, of” the board of directors, and operational management is delegated to officers and other professional managers.

While Section 801(b), in providing for corporate powers to be exercised under the authority of the board of directors, allows the board of directors to delegate to appropriate officers, employees or agents of the nonprofit corporation authority to exercise powers and perform functions not required by law to be exercised or performed by the board of directors itself, responsibility to oversee the exercise of that delegated authority nonetheless remains with the board of directors. The scope of that oversight responsibility will vary depending on the nature of the corporation’s activities.

Although delegation does not relieve the board of directors from its responsibility to oversee the activities and affairs of the nonprofit corporation, directors are not personally responsible for actions or omissions of officers, employees, or agents of the corporation, so long as the directors have relied reasonably and in good faith upon those officers, employees, or agents. See Sections 830 and 831 and their Official Comments. Directors generally have the power to probe into day-to-day management to any depth they choose, but they have the obligation to do so only to the extent that the directors’ oversight responsibilities may require, or, for example, when they become aware of matters that make reliance on management or other persons unwarranted.

§ 802. QUALIFICATIONS OF DIRECTORS

A director of a nonprofit corporation must be an individual [of the age of majority]. The articles of incorporation or bylaws may prescribe other qualifications for directors. A director need not be a resident of this state or a member of the corporation unless the articles or bylaws so prescribe.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.02. Cf. Model Business Corporation Act (2016 Revision), § 8.02(a) and (c).

CROSS-REFERENCES

Articles of incorporation, § 202 and Subch. 9A.
Bylaws, § 206 and Subch. 9B.
Selection of directors, § 804.

§ 803. NUMBER OF DIRECTORS

(a) A board of directors must consist of three or more directors, with the number specified in or fixed in accordance with the articles of incorporation or bylaws.

The elimination of mandatory special qualifications for directors is now nearly universal, but the articles of incorporation or bylaws may prescribe special qualifications where a nonprofit corporation considers that appropriate.

Some states permit a minority of directors of a nonprofit corporation to be younger than the age of majority, sometimes limiting the use of such directors to youth clubs or other nonprofit corporations with a similar mission. Restricting service as a director of a corporation to individuals of the age of majority is proposed as an optional provision in Section 802, and an enacting state should review its existing law before deciding whether to include that optional provision.

Although this section requires that directors be individuals, there is no such requirement with respect to delegates or members of a designated body. The definition of “delegate” in Section 102 refers simply to a “person”; and the definition of “designated body” in Section 102 refers to “a person or group.” “Person” is defined in Section 102 to include “an individual and an entity.” The qualifications of members of a designated body are dealt with in Section 812(c).

Qualifications may apply to all board members or to a specified percentage or number of directors. An example of a qualification applying to fewer than all directors would be a requirement that at least two directors must have specified nonprofit, business, or professional experience or a particular educational degree or background. Careful consideration should be given to the intended effect of the application of any qualification that applies to fewer than all directors in the context of an election contest in which only some of the nominees satisfy this qualification. In the event that specified qualifications for some or all directors are not satisfied, remedial steps could be addressed in the articles of incorporation or bylaws, or can be left to other mechanisms available to a nonprofit corporation, its members and/or its board, such as the provisions permitting changes in the number of directors and providing for the filling of vacancies on the board. See Sections 803 and 810.

The purpose of Section 802(a) is to permit qualifications that may benefit the corporation by enhancing the board’s ability to perform its role effectively. However, this needs to be balanced against the risk that qualifications could be misused for entrenchment purposes by incumbents or for other improper purposes. An example of a qualification that would not be proper would be a requirement that is impermissibly discriminatory under the Civil Rights Act of 1964.
(b) The number of directors may be increased or decreased (but to no fewer than
three) from time to time by amendment to, or in the manner provided in, the articles of
incorporation or bylaws.

Revision), § 8.03(a) and (b).

CROSS-REFERENCES

Deadlocked board of directors as ground for dissolution, § 1120.
Staggered terms for directors, § 806.
Terms of directors generally, § 805.
Voting for directors, § 727.

OFFICIAL COMMENT

Section 803 prescribes rules for (i) determining the size of the board of directors and
(ii) changing the number of directors once the board’s size has been established.

1. Number of Directors

Section 803(a) requires a nonprofit corporation to have a minimum of three directors. So
long as that limitation is satisfied, the size of the board of directors may fixed initially in one or
more of the fundamental corporate documents, or the decision as to the size of the initial board of
directors may be made thereafter in the manner authorized in those documents.

2. Changes in the Size of the Board of Directors

Section 803(b) provides a nonprofit corporation with the freedom to design its articles of
incorporation and bylaws relating to the size of its board with a view to achieving the
combination of flexibility for the board of directors and protection for members that it deems
appropriate. The articles or bylaws could provide for a specified number of directors or a board
size within a range from a minimum to a maximum, or an unlimited size not fewer than three,
with the number to be fixed by the members or the board. If the members or the board want to
change the specified size of the board, to change the range established for the size of the board,
or to change from a board size within a range or of unlimited size to a specified board size or
vice versa, member or board action would be required to make those changes by amending the
articles or bylaws. Any change would be made in the manner provided by the articles or bylaws.
Typically, the board would be permitted to change the board size within the established range. If
a corporation wishes to ensure that any change in the number of directors be approved by
members, then an appropriate restriction would need to be included in the articles or bylaws.

The board’s power to change the number of directors, like all other board powers, is
subject to compliance with applicable standards governing director conduct. In particular, it may
be inappropriate to change the size of the board for the primary purpose of maintaining control or
defeating particular candidates for the board.
§ 804. SELECTION OF DIRECTORS

(a) The directors of a membership corporation (other than any initial directors named in the articles of incorporation or elected by the incorporators) shall be elected by the members entitled to vote at the time at the first annual meeting of members, and at each annual meeting thereafter, unless the articles or bylaws provide some other time or method of election, or provide that some or all of the directors are appointed by some other person or designated in some other manner.

(b) The directors of a nonmembership corporation (other than any initial directors named in the articles of incorporation or elected by the incorporators) shall be elected, appointed, or designated as provided in the articles or bylaws. If no method of designation or appointment is set forth in the articles or bylaws, the directors (other than any initial directors) shall be elected by the board.

(c) If the articles of incorporation or bylaws authorize dividing the members into classes, the articles or bylaws may also authorize the election of all or a specified number of directors by the holders of one or more authorized classes of members. A class or multiple classes of members entitled to elect one or more directors is a separate voting group for purposes of the election of directors.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.04.

CROSS-REFERENCES

Initial directors:
- appointed by incorporators, § 205
- named in articles, § 202
“Membership corporation” defined, § 102.
“Nonmembership corporation” defined, § 102.
Number of directors, § 803
Staggered terms for directors, § 806
Terms of directors generally, § 805.

OFFICIAL COMMENT

1. Membership Corporations

If a nonprofit corporation has members, the members are entitled to elect all the directors in the absence of a contrary provision in the articles of incorporation or bylaws. The articles or bylaws may set forth a simple one-vote-per-member structure or may provide for election by voting groups of members, chapters or other organizational units or by region or other geographic groupings. See Sections 202 and 205 as to appointment of initial directors. See Sections 704, 709, 721, 725, and 727 as to the ways in which members may vote.
Section 804 should be applied in a manner consistent with the concept that an election procedure must be reasonable. The act does not specify detailed procedures, but leaves the matter to developing case law.

Even if a nonprofit corporation has members, the members need not elect some or all of the directors. Directors may hold office as a result of designation in the articles of incorporation or bylaws or as a result of being appointed by some person or entity.

Designation occurs when the articles of incorporation or bylaws name an individual as a director or designate the holder of some office or position as a director. For example, the President of Harvard, the Bishop of New York, or the head of a union may become a director of a nonprofit corporation pursuant to an article or bylaw provision designating the holder of their position as a director of the corporation. The individual would cease to be a director upon ceasing to hold the designated position.

2. Nonmembership Corporations

Section 804 authorizes self-perpetuating boards of directors. If a nonprofit corporation does not have members, the board elects directors in the absence of a provision in the articles of incorporation or bylaws setting forth some other approach.

3. “Ex Officio” Directors

An individual may serve as a director of a nonprofit corporation “ex officio,” which means that the individual is a director because of some other office or position that the individual holds. The term “ex officio” does not include the concept that the position is nonvoting. If an ex officio director is to be non-voting, that must be provided for expressly.

§ 805. TERMS OF DIRECTORS GENERALLY

(a) The articles of incorporation or bylaws may specify the terms of directors. If a term is not specified in the articles or bylaws, the term of a director is one year. Except for directors who are appointed by persons who are not members or who are designated in a manner other than by election or appointment, the term of a director may not exceed six years.

(b) A decrease in the number of directors or term of office does not shorten an incumbent director’s term.

(c) Except as provided in the articles of incorporation or bylaws, the term of a director elected to fill a vacancy expires at the end of the unexpired term that the director is filling.

(d) Despite the expiration of a director’s term, the director continues to serve until the director’s successor is elected, appointed, or designated and until the director’s successor takes
office unless otherwise provided in the articles of incorporation or bylaws or there is a decrease in the number of directors.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.05. Cf. Model Business Corporation Act (2016 Revision), § 8.05.

CROSS-REFERENCES

Court-ordered meeting, § 703.
Number of Directors, § 803.
Removal of directors, §§ 808 and 809.
Resignation of directors, § 807.
Staggered terms for directors, § 806.
Vacancy on board, § 810.

OFFICIAL COMMENT

The usual term of directors is one year, but Section 805(a) permits the articles of incorporation or bylaws to provide for longer terms. The usual maximum term of directors is six years. However, no maximum term is provided for individuals who are appointed by persons who are not members (such as the board of another nonprofit corporation that is not a member) or a director who is designated by means other than election or appointment (such as the designation of the president of the nonprofit corporation as a member of the board). Directors who serve “ex officio” are “designated” for purposes of Section 805(a) and thus are not limited to a term of six years. The act does not provide for term limits and thus a director may be elected to more than one term, regardless of the length of a term, unless the articles of incorporation or bylaws limit the number of terms a director may serve.

Section 805(b) provides that a decrease in the number of directors does not shorten the term of an incumbent director or divest any director from office. Rather, the incumbent director’s term expires on the date that the incumbent director’s term would have expired prior to the decrease in the number of directors and the incumbent director does not continue to serve (“holdover”) after that date.

Section 805(d) provides for “holdover” directors so that directorships do not automatically become vacant at the expiration of their terms, unless there is a decrease in the number of directors or unless otherwise provided in the articles of incorporation or bylaws. This means that the power of the board to act continues uninterrupted even if an annual meeting at which directors are to be elected is not held; or the members, in a membership corporation, or the board, in a nonmembership corporation, are deadlocked or otherwise do not elect directors at the meeting.

§ 806. STAGGERED TERMS FOR DIRECTORS
The articles of incorporation or bylaws may provide for staggering the terms of directors by dividing the total number of directors into groups of one or more directors. The terms of office and number of directors in each group do not need to be uniform.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.06. Cf Model Business Corporation Act (2016 Revision), § 8.06.

CROSS-REFERENCES

Voting for directors, § 727.
Number of directors, § 803.
Removal of directors, §§ 808 and 809.
Resignation of directors, § 807.
Terms of directors generally, § 805.
Vacancies on board, § 810.

OFFICIAL COMMENT

Section 806 permits the practice of “classifying” the board or “staggering” the terms of directors so that less than all of the directors are elected each year. Unlike the case with business corporations, where each class of directors must be as nearly equal in number as possible, this section permits classes of directors to vary in size from each other. This section also does not limit the number of classes that may be created.

§ 807. RESIGNATION OF DIRECTORS

(a) A director may resign at any time by delivering a notice of resignation in a record to the board of directors, its chair, or the secretary of the corporation.

(b) A resignation is effective when the notice is delivered unless the notice specifies a later effective time or an effective time determined upon a future event.


CROSS-REFERENCES

“Deliver” defined, § 102.
Notice, § 103.
“Secretary” defined, § 102.
Vacancy on board, § 810.

OFFICIAL COMMENT
The resignation of a director is effective when the resignation notice is delivered unless the notice specifies a later effective time, in which case the director continues to serve until that later time. Because a director giving a notice with a delayed effective date is still a director, that director may participate in all decisions until the specified time, including the choice of a successor under Section 810.

Under Section 810, a vacancy that will occur at a specific later date by reason of a resignation effective at a later date may be filled before the vacancy occurs, but the new director may not take office until the vacancy occurs.

§ 808. REMOVAL OF DIRECTORS BY MEMBERS OR OTHER PERSONS

(a) Removal of directors of a membership corporation is subject to the following provisions:

(1) The members may remove, with or without cause, one or more directors who have been elected by the members, unless the articles of incorporation or bylaws provide that directors may be removed only for cause. The articles or bylaws may specify what constitutes cause for removal. See Section 922(a) (bylaw amendments requiring member approval).

(2) Except as provided in the articles of incorporation or bylaws, if a director is elected by a voting group of members, or by a chapter or other organizational unit, or by a region or other geographic grouping, only the members of that voting group or chapter, unit, region, or grouping may participate in the vote to remove the director.

(3) The notice of a meeting of members at which removal of a director is to be considered must state that the purpose, or one of the purposes, of the meeting is removal of the director.

(4) The board of directors of a membership corporation may not remove a director except as provided in subsection (c) or in the articles of incorporation or bylaws.

(b) The board of directors may remove a director of a nonmembership corporation:

(1) With or without cause, unless the articles of incorporation or bylaws provide that directors may be removed only for cause. The articles or bylaws may specify what constitutes cause for removal.

(2) As provided in subsection (c).

(c) The board of directors of a membership corporation or nonmembership corporation may remove a director who:

(1) has been declared of unsound mind by a final order of court:
(2) has been convicted of a felony;

(3) has been found by a final order of court to have breached a duty as a director under [Subchapter] 8C (directors);

(4) has missed the number of board meetings specified in the articles of incorporation or bylaws, if the articles or bylaws at the beginning of the director’s current term provided that a director may be removed for missing the specified number of board meetings; or

(5) does not satisfy at the time any of the qualifications for directors set forth in the articles of incorporation or bylaws at the beginning of the director’s current term, if the decision that the director fails to satisfy a qualification is made by the vote of a majority of the directors who meet all of the required qualifications.

(d) A director who is designated in the articles of incorporation or bylaws may be removed by an amendment to the articles or bylaws deleting or changing the designation. See Section 930 (approval by third persons).

(e) Except as provided in the articles of incorporation or bylaws, a director who is appointed by persons other than the members may be removed with or without cause by those persons.


CROSS-REFERENCES

Member meetings, §§ 701 through 703.
“Membership corporation” defined, § 102.
“Nonmembership corporation” defined, § 102.
Notice of meeting, § 705.
Quorum for voting group, §§ 724 and 726.
Removal of directors by judicial proceeding, § 809.
Standards of conduct for directors, § 830.
Voting for directors, § 727.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 808(a) provides a default rule that the members have the power to change at will the directors elected by them. However, Section 808 permits the power to remove directors without cause to be eliminated by a provision in the articles of incorporation or bylaws. A director may be removed by court proceeding under Section 809 despite this section.
Although Section 808(b) and (c) have specific requirements with respect to removal of directors elected by particular voting groups, those directors nevertheless may be removed by court proceeding under Section 809. Section 808(d) acknowledges the seriousness of director removal by requiring the meeting notice to state that removal of specific directors will be proposed. Section 808(d) governs removal of directors at a meeting of members, but does not preclude removal by means of member action by written consent under Section 704. In the absence of a greater vote requirement in the articles of incorporation or bylaws, removal of a director by less than unanimous written consent would require that a majority of the members of the relevant voting group consent to the removal.

§ 809. REMOVAL OF DIRECTORS BY JUDICIAL PROCEEDING

(a) The [name or describe] court of the county where the principal office of a nonprofit corporation (or, if none in this state, its registered office) is located may remove a director from office in a proceeding commenced by or in the right of the corporation if the court finds that:

(1) the director engaged in fraudulent conduct with respect to the corporation or its members, grossly abused the position of director, or intentionally inflicted harm on the corporation; and

(2) considering the director’s course of conduct and the inadequacy of other available remedies, removal would be in the best interest of the corporation.

(b) A member, individual director, or member of a designated body proceeding on behalf of the nonprofit corporation under subsection (a) shall comply with all of the requirements of [Chapter] 5 (derivative proceedings).

(c) The court, in addition to removing the director, may bar the director from being reelected, redesignated, or reappointed for a period prescribed by the court.

(d) Nothing in this section limits the equitable powers of the court to order other relief.

(e) If a proceeding is commenced under this section to remove a director of a charitable corporation, the plaintiff must give the attorney general notice in record form of the commencement of the proceeding.


CROSS-REFERENCES

Derivative proceedings, Ch. 5.

Standards of conduct for directors, § 830.
“Member” defined, § 102.

“Principal office” defined, § 102.

designated in annual report, § 421.

“Proceeding” defined, § 102.

Registered office:

designated in annual report, § 421.

required, §§ 202 and 220.

Removal by members, § 808.

OFFICIAL COMMENT

Section 809 is designed to operate in the limited circumstance where other remedies are inadequate to address serious misconduct by a director and it is impracticable for members to invoke removal under Section 808 in the case of a membership corporation or the directors in a nonmembership corporation. Misconduct serious enough to justify the extraordinary remedy of judicial removal does not involve any matter falling within an individual director’s lawful exercise of business judgment, no matter how unpopular the director’s views may be with the other members of the board. Policy and personal differences among the members of the board of directors should be left to be resolved by the members in a membership corporation or by the board in a nonmembership corporation.

Section 809 is designed to interfere as little as possible with the usual mechanisms of corporate governance. It is not intended to permit judicial resolution of internal corporate disputes involving issues other than those specified in subsection (a).

Section 809(d) makes it clear that the court is not restricted to the removal remedy in actions under this section but may order any other equitable relief. Where, for example, the complaint concerns an ongoing course of conduct that is harmful to the nonprofit corporation, the court may enjoin the director from continuing that conduct. In another instance, the court may determine that the director’s continuation in office is inimical to the best interest of the corporation.

A proceeding under this section may be brought directly by the board of directors. A proceeding may also be brought by a member or an individual director or member of a designated body suing derivatively. If an action is brought derivatively, all of the provisions of Chapter 5, including dismissal under Section 505, are applicable to the action.

§ 810. VACANCY ON BOARD

(a) Except as otherwise provided in subsection (b), the articles of incorporation, or the bylaws, if a vacancy occurs on the board of directors, including a vacancy resulting from an increase in the number of directors, the vacancy may be filled by a majority of the directors remaining in office even if they constitute less than a quorum.
(b) Except as provided in the articles of incorporation or bylaws, a vacancy in the position of a director who is:

(1) elected by a voting group of members, by a chapter or other organizational unit of members, or by a region or other geographic grouping of members, may be filled during the first three months after the vacancy occurs only by that voting group or chapter, unit, region, or grouping;

(2) appointed by persons other than the members, may be filled only by those persons; or

(3) designated in the articles of incorporation or bylaws may not be filled by action of the board of directors.

(c) A vacancy that will occur at a specific later time (by reason of a resignation effective at a later time under Section 807(b) (resignation of directors) or otherwise) may be filled before the vacancy occurs but the new director may not take office until the vacancy occurs.


CROSS-REFERENCES

Number of directors, § 803.
Quorum and voting of directors, § 824.
Removal of directors, §§ 808 and 809.
Resignation of directors, § 807.
Terms of directors generally, § 805.
Voting by voting group, §§ 724 and 725.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 810(a) allows a majority of the directors remaining in office to fill vacancies even though they are fewer than a quorum. For example, on a board of six directors where a quorum is four, if there are two vacancies, the vacancies may be filled by action of three of the remaining directors.

Section 810(b)(1) protects the special rights of groups of members to elect directors by restricting the ability of the board of directors to fill a vacancy of a director elected by the group. The group is given the exclusive opportunity to fill the vacancy for an initial period, but the board is then given the power to fill the vacancy if the group does not act. The board never has the power, however, to fill a vacancy in the case of a director designated or appointed in a manner other than election. Only the persons authorized to appoint a director may fill a vacancy.
in the appointed board seat. A vacancy in a designated board seat will only be filled when an
individual satisfies the requirements of the designation.

Under Section 810(c), the director in the office that will become vacant may participate
in the selection of a successor. Such a vacancy typically arises when there is a resignation by a
director that is effective at a later date; it may also arise in connection with retirements or with
prospective amendments to bylaws.

§ 811. COMPENSATION OF DIRECTORS

Unless the articles of incorporation or bylaws provide otherwise, the board of directors
may fix the compensation of directors.

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
Revision), § 8.11.

CROSS-REFERENCES

Board and advisory committees, § 825.
Standards of conduct for directors, § 830.

OFFICIAL COMMENT

When exercising their power under Section 811, the directors must comply with their
duties as directors under Subchapter 8C.

Reimbursement of expenses incurred as a director in accordance with expense
reimbursement policies of the nonprofit corporation, or as approved by the board, does not
constitute compensation under this section. See Section 641 with respect to amounts that may be
paid as compensation or reimbursement of expenses.

§ 812. DESIGNATED BODY

(a) Some, but less than all, of the powers, authority, or functions of the board of
directors of a nonprofit corporation under this [Act] may be vested by the articles of
incorporation or bylaws in a designated body. If such a designated body is created:

(1) The provisions of this [Chapter] and other provisions of law on the rights,
duties, and liabilities of the board of directors or directors individually also apply to the
designated body and to the members of the designated body individually. The provisions of this
[Chapter] and other provisions of law on meetings, notice, and the manner of acting of the board
of directors also apply to the designated body in the absence of an applicable rule in the articles
of incorporation, bylaws or internal operating rules of the designated body.
(2) To the extent the powers, authority, or functions of the board of directors have been vested in the designated body, the directors are relieved from their duties and liabilities with respect to those powers, authority, and functions.

(3) A provision of the articles of incorporation regarding indemnification of directors or limiting the liability of directors adopted pursuant to Section 202(b)(8) or (c) (articles of incorporation) applies to members of the designated body, except as otherwise provided in the articles.

(b) Some, but less than all, of the rights or obligations of the members of a nonprofit corporation under this [Act] may be vested by the articles of incorporation or bylaws in a designated body. If such a designated body is created:

(1) The provisions of this [Chapter] and other provisions of law on the rights and obligations of members also apply to the designated body and to the members of the designated body individually. The provisions of this [Chapter] and other provisions of law on meetings, notice, and the manner of acting of members also apply to the designated body in the absence of an applicable provision in the articles of incorporation, bylaws or internal operating rules of the designated body.

(2) To the extent the rights or obligations of the members have been vested in the designated body, the members are relieved from responsibility with respect to those rights and obligations.

(c) The articles of incorporation or bylaws may prescribe qualifications for members of a designated body. Except as otherwise provided by the articles or bylaws, a member of a designated body does not need to be:

(1) an individual,

(2) a director, officer, or member of the nonprofit corporation, or

(3) a resident of this state.

(d) See Section 922(a) (bylaw amendments requiring member approval).


CROSS-REFERENCES

“Board of directors” defined, § 102.
“Designated body defined, § 102
Requirements for and functions of board of directors, § 801.
“Member” defined, § 102.

OFFICIAL COMMENT
It is not necessary for a designated body to be referred to by that name, and designated bodies are typically referred to by the name they have for other purposes.

If all the powers, authority, and functions of the board of directors are vested in a body, it is not a designated body but has instead the status of the board of directors. Similarly, if all the rights and obligations of the members are vested in a group of persons, the group is not a designated body and its members instead have the status of members.

If all the members of a group of individuals that have some of the powers, authority, or functions of the board of directors are directors and the group is established by action of the board, the group will be a committee of the board rather than a designated body. If at least one member of a group is not a director, however, the group will be a designated body.

Use of a designated body does not reduce accountability because this section makes clear that members of a designated body have the duties and liabilities of directors when discharging functions that would otherwise be within the purview of the board.

See Section 1030 with respect to special requirements for approval of amendments of the articles of incorporation or bylaws.

The Official Comments to certain sections of the act indicate some of the important issues on which a designated body can act, but those comments are not intended to be an exhaustive indication of how designated bodies may be used.

[Subchapter] B
MEETINGS AND ACTION OF THE BOARD

§ 820. MEETINGS
(a) The board of directors may hold regular or special meetings in or out of this state.
(b) Unless restricted by the articles of incorporation or bylaws or action of the board of directors, any or all directors may participate in a meeting of the board through the use of any means of communication by which all directors participating may simultaneously hear each other during the meeting. A director participating in a meeting by this means is deemed to be present in person at the meeting.
CROSS-REFERENCES

Action without meeting, § 821.
Call and notice of meeting, § 822.
Quorum and voting, § 824.
Waiver of notice, § 823.

OFFICIAL COMMENT

Section 820 provide flexibility with respect to holding meetings of directors and authorizes those meetings to be held anywhere. No distinction is made between meetings in-state and out-of-state.

Under Section 820, a meeting in which any or all of the directors participate through any means of communication that complies with section 820(b) will meet the statutory requirements. Depending on the nature of the matters to be considered, however, a board of directors may require an in-person meeting to provide greater opportunity for interchange. If a director is hearing-impaired, participation by that or other directors in a meeting by means of communications technology will still be permissible, if reasonable accommodations are made to permit the hearing-impaired director to follow the discussion.

The provisions of this section also apply to meetings of a designated body. See Section 812(a)(1).

§ 821. ACTION WITHOUT MEETING

(a) Except to the extent that the articles of incorporation or bylaws require that action by the board of directors be taken at a meeting, action required or permitted by this [Act] to be taken by the board of directors may be taken without a meeting if each director signs a consent in a record describing the action to be taken and delivers it to the nonprofit corporation.

(b) Action taken under this section is the act of the board of directors when one or more consents signed by all the directors are delivered to the nonprofit corporation. The consent may specify a later time as the time at which the action taken is to be effective. A director’s consent may be withdrawn by a revocation in a record signed by the director and delivered to the corporation before delivery to the corporation of unrevoked consents signed by all the directors.

(c) A consent signed under this section has the effect of action taken at a meeting of the board of directors and may be described as such in any document.
Directors may take action by consent without a meeting only when approval of an action is unanimous. Accordingly, if a director abstains, is recused or withholds consent on an action, the action could not be authorized by consent, and a meeting would need to be held for the action to be approved.

A designated body may act without a meeting pursuant to this section. See Section 812(a)(1).

§ 822. CALL AND NOTICE OF MEETING

(a) Unless the articles of incorporation or bylaws provide otherwise, regular meetings of the board of directors may be held without notice of the date, time, place, or purpose of the meeting.

(b) Unless the articles of incorporation or bylaws provide for a longer or shorter period, special meetings of the board of directors must be preceded by at least two days’ notice of the date, time, and place of the meeting. The notice need not describe the purpose of the special meeting unless required by the articles of incorporation or bylaws.

(c) Unless the articles of incorporation or bylaws provide otherwise, the chair of the board, the highest ranking officer of the corporation, or 20% of the directors then in office may call and give notice of a meeting of the board of directors.

(d) The articles of incorporation or bylaws may authorize oral notice of meetings of the board of directors.

Unlike regular meetings of the board of directors, special meetings always 
require notice, the timing of which may be varied by the articles of 
incorporation or bylaws. The notice may be in a record or oral if oral notice is reasonable in the circumstances. See Section 103(a). If the notice of a special meeting is mailed, it must be deposited with the U.S. Mail at least seven days before the meeting because Section 103(e)(3) provides that notice by mail is effective five days after mailing.

No statement of the purpose of any meeting of the board is necessary in the notice unless required by the articles of incorporation or bylaws. These requirements differ from the requirements applicable to meetings of members because of the fundamental differences in the roles and involvement of directors and members.

The provisions of this section also apply to meetings of a designated body. See Section 812(a)(1).

§ 823. WAIVER OF NOTICE

(a) A director may waive any notice required by this [Act], the articles of incorporation, or the bylaws before or after the date and time stated in the notice. Except as provided by subsection (b), the waiver must be in a record, signed by the director entitled to the notice, and delivered to the nonprofit corporation for filing by the corporation with the minutes or corporate records.

(b) A director’s attendance at or participation in a meeting waives any required notice to the director of the meeting, unless the director at the beginning of the meeting (or promptly upon arrival) objects to holding the meeting or transacting business at the meeting and does not, after objecting, vote for or assent to action taken at the meeting.


CROSS-REFERENCES

Action without meeting, § 821.
Call and notice of meeting, § 822.
Meetings of board of directors, § 820.
Notice generally, § 103.
“Record” defined, § 102.
OFFICIAL COMMENT

If a director actually attends the meeting, Section 823(b) generally provides that the director may not subsequently raise an objection based on lack of notice. If a director does wish to object, the director must call attention to the lack of notice at the outset of the meeting or promptly upon arriving and not vote for any action taken at the meeting. That director may then attack the validity of any action taken at the meeting on the grounds of lack of notice, as may any other director who was not given notice and was not present at the meeting.

A member of a designated body may waive notice in the manner provided in this section. See Section 812(a)(1).

§ 824. QUORUM AND VOTING

(a) Except as provided in subsection (b), the articles of incorporation, or the bylaws, a quorum of the board of directors consists of a majority of the directors in office before a meeting begins.

(b) The articles of incorporation or bylaws may authorize a quorum of the board of directors to consist of no fewer than the greater of one-third of the number of directors in office or two directors.

(c) If a quorum is present when a vote is taken, the affirmative vote of a majority of directors voting is the act of the board of directors unless a greater vote is required by the articles of incorporation or bylaws.

(d) A director who is present at a meeting of the board of directors when corporate action is taken is deemed to have assented to the action taken unless:

(1) the director objects at the beginning of the meeting (or promptly upon arrival) to holding it or transacting business at the meeting;

(2) the dissent or abstention by the director from the action taken is entered in the minutes of the meeting; or

(3) the director delivers notice in a record of the director’s dissent or abstention to the presiding officer of the meeting before its adjournment or to the corporation promptly after adjournment of the meeting.

(e) The right of dissent or abstention is not available to a director who votes in favor of the action taken.
CROSS-REFERENCES

Action without meeting, § 821.
Board and advisory committees, § 825.
Meetings of board of directors, § 820.
Notice, § 103.
Number of directors, § 803.
“Record” defined, § 102.
“Secretary” defined, § 102.
Standards of conduct for directors, § 830.

OFFICIAL COMMENT

Section 824(a) allows the articles of incorporation or bylaws to increase the quorum up to and including unanimity or to reduce it to not less than one-third (or at least two directors).

Section 824(c) generally requires a majority vote of those directors voting for action by the board, but allows the articles or bylaws to increase the vote necessary for the board to take action. The increased vote could be either a supermajority requirement, or a requirement that action by the board requires the affirmative vote of a majority of the directors present.

The phrase “when a vote is taken” in Section 824(c) is designed to make clear that the board of directors may act only when a quorum is present. If directors leave during the course of a meeting, the board of directors may not act after the number of directors present is reduced to less than a quorum.

If a director, who is present at a meeting, wishes to object or abstain with respect to action taken by the board of directors or a committee, that director must make his or her position clear in one of the ways described in Section 824(d). Section 824(d) serves the important purpose of bringing the position of the dissenting director clearly to the attention of the other directors. The requirement of an objection in a record also prevents a director from later seeking to avoid responsibility because of unexpressed doubts about the wisdom of the action taken. The right of dissent or abstention is not available to a director who voted in favor of the action taken.

Section 824(d) applies only to directors who are present at the meeting. Directors who are not present are not deemed to have assented to any action taken at the meeting in their absence.

This section applies to meetings of a designated body. See Section 812(a)(1).

§ 825. BOARD AND ADVISORY COMMITTEES
(a) Except as restricted by the articles of incorporation or bylaws, the board of directors may establish one or more board committees composed exclusively of one or more directors to perform functions of the board.

(b) Unless this [Act], the articles of incorporation, or the bylaws provide otherwise, the establishment of a committee and appointment of directors to it must be approved by the greater of:

(1) a majority of all the directors in office when the action is taken; or

(2) the number of directors required by the articles of incorporation or bylaws to take action under Section 824 (quorum and voting).

(c) Sections 820 (meetings) through 824 apply to board committees and their members.

(d) A board committee may exercise the powers of the board of directors under Section 801 (requirement for and functions of board of directors), to the extent specified by the board or in the articles of incorporation or bylaws, except that a board committee may not:

(1) authorize distributions;

(2) in the case of a membership corporation, approve or propose to members action that this [Act] requires be approved by members;

(3) fill vacancies on the board of directors or, subject to subsection (g), on any of its committees; or

(4) adopt, amend, or repeal a provision of the articles or bylaws.

(e) The creation of, delegation of authority to, or action by a committee does not alone constitute compliance by a director with the standards of conduct described in Section 830.

(f) The board of directors may appoint one or more directors as alternate members of any board committee to replace any absent or disqualified member during the member’s absence or disqualification. If the articles of incorporation, bylaws, or the action creating a board committee so provides, the member or members present at any board committee meeting and not disqualified from voting may, by unanimous action, appoint another director to act in place of an absent or disqualified member during that member’s absence or disqualification.

(g) A nonprofit corporation may create or authorize the creation of one or more advisory committees whose members need not be directors. An advisory committee:

(1) is not a committee of the board; and

(2) may not exercise any of the powers of the board.
CROSS-REFERENCES

Amendment of articles, Subch. 9A.
Amendment of bylaws, Subch. 9B.
Derivative proceedings, Ch. 5.
Designated body, § 812.
Designated body defined, § 102.
Distributions prohibited, § 640.
“Membership corporation” defined, § 102.
Quorum and voting, § 824.
Requirements for and functions of board of directors, § 801.
Standards of conduct for directors, § 830.
Vacancy on board, § 810.

OFFICIAL COMMENT

Section 825(a) through (f) deals only with board committees authorized to perform functions of the board.

Under Section 825(a), except as otherwise provided by this [Act], the articles of incorporation, or bylaws, a board committee may consist of a single director. This accommodates situations in which only one director may be present or available to make a decision on short notice, as well as situations in which it is unnecessary or inconvenient to have more than one member on a board committee or where only one board member is disinterested or independent with respect to a matter.

The requirement of section 825(b) that, unless this [Act], the articles, or bylaws otherwise provide, a board committee may be created only by the affirmative vote of the greater of a majority of all the directors in office when the action is taken or the number of directors required by the articles of incorporation or bylaws to take action under Section 824 (quorum and voting), reflects the importance of the decision to invest board committees with power to act under Section 825.

The statement of nondelegable functions set out in Section 825(d)(1) through (4) is based on the principle that the listed actions so substantially affect the rights of members, if the nonprofit corporation is a membership corporation, or are so fundamental to the governance of the corporation that they should be determined by the full board and not delegated to a committee. On the other hand, Section 825(d) allows board committees to take many actions that may be material, such as the authorization of long-term debt and capital investment.

Section 825(e) makes clear that although the board of directors may delegate to a committee the authority to take action, the designation of the committee, the delegation of
authority to it, and action by the committee does not alone constitute compliance by a noncommittee board member with the director’s responsibility under Section 830. On the other hand, a noncommittee director also does not automatically incur personal risk should the action of the particular committee fail to meet the standard of conduct set out in Section 830. The noncommittee member’s liability in these cases will depend upon whether the director’s conduct was actionable under Section 831. Also, Section 825(e) has no application to a member of the committee itself. The standards of conduct applicable to a committee member are set forth in Section 830.

Section 825(f) is a rule of convenience that permits the board of directors or the other board committee members to replace an absent or disqualified member during the time that the member is absent or disqualified. Unless otherwise provided or unless a quorum is no longer present, replacement of an absent or disqualified member of a committee is not necessary to permit the other committee members to continue to perform their duties.

Section 825(g) recognizes that the board of directors or management may establish nonboard committees to perform functions that are not required to be exercised by the board of directors. Those committees are sometimes purely advisory, but may also perform functions that would otherwise be performed by officers, employees, or agents. If a nonboard committee exercises any of the powers of the board, it will have the status of a designated body and its members will have fiduciary duties under Section 812.

[Subchapter] C
DIRECTORS
§ 830. Standards of conduct for directors.
§ 831. Standards of liability for directors.
§ 832. Directors’ liability for unlawful distributions.
§ 833. Loans to or guarantees for directors and officers. [Optional]

INTRODUCTORY COMMENT TO SUBCHAPTER C
The provisions of this act with respect to the duties and liabilities of directors of nonprofit corporations closely follow the provisions of the Model Business Corporation Act on the same subjects. This is consistent with the view that the relationship of directors to a nonprofit corporation is more akin to that of directors of business corporations than to that of trustees to their beneficiaries. Stern v. Lucy Webb Hayes National Training School for Deaconesses and Missionaries, 381 F.Supp. 1003 (D.D.C. 1974).

Depending on the status of a particular state’s law, Sections 830 and 831 will replace, modify, clarify, or set forth the basic standards that govern the conduct of directors of nonprofit corporations. States may have statutory or common law rules that apply a trust rule to director conduct. Those states should consider repealing those rules so that this act will replace those rules even though the corporation, as distinguished from its directors, may hold or be deemed to hold property in trust or subject to restrictions.
§ 830. STANDARDS OF CONDUCT FOR DIRECTORS

(a) Each director, when discharging the duties of a director, must act:

(1) in good faith, and

(2) in a manner the director reasonably believes to be in the best interests of the nonprofit corporation.

(b) The directors or members of a committee of the board of directors, when becoming informed in connection with their decision-making function or devoting attention to their oversight function, must discharge their duties with the care that a person in a like position would reasonably believe appropriate under similar circumstances.

(c) In discharging board or board committee duties a director must disclose, or cause to be disclosed, to the other board or committee members information not already known by them but known by the director to be material to the discharge of their decision-making or oversight functions, except that disclosure is not required to the extent that the director reasonably believes that doing so would violate a duty imposed under law, a legally enforceable obligation of confidentiality, or a professional ethics rule.

(d) In discharging board or board committee duties, a director who does not have knowledge that makes reliance unwarranted may rely on the performance by any of the persons specified in subsection (f)(1), (3), or (4) to whom the board may have delegated, formally or informally by course of conduct, the authority or duty to perform one or more of the board’s functions that are delegable under applicable law.

(e) In discharging board or board committee duties, a director who does not have knowledge that makes reliance unwarranted may rely on information, opinions, reports, or statements, including financial statements and other financial data, prepared or presented by any of the persons specified in subsection (f).

(f) A director is entitled to rely, in accordance with subsection (d) or (e), on:

(1) one or more officers, employees, or volunteers of the nonprofit corporation whom the director reasonably believes to be reliable and competent in the functions performed or the information, opinions, reports, or statements provided;

(2) legal counsel, public accountants, or other persons retained by the corporation as to matters involving skills or expertise the director reasonably believes are matters:

(i) within the particular person’s professional or expert competence,
(ii) as to which the particular person merits confidence;

(3) a board committee of which the director is not a member, if the director reasonably believes the committee merits confidence; or

(4) in the case of a corporation engaged in religious activity, religious authorities and ministers, priests, rabbis, imams, or other persons whose positions or duties the director reasonably believes justify reliance and confidence and whom the director believes to be reliable and competent in the matters presented.

(g) A director is not a trustee with respect to the nonprofit corporation or with respect to any property held or administered by the corporation, including property that may be subject to restrictions imposed by the donor or transferor of the property.


CROSS-REFERENCES

Board and advisory committees, § 825.
Conflict of interest transactions, Subch. 8F.
Derivative proceedings, Ch. 5.
Directors’ liability for unlawful distributions, § 832.
Indemnification and advancement of expenses, Subch. 8E.
Meetings of board of directors, § 820.
Officers, §§ 840 and 841.
Removal of directors, §§ 808 and 809.
Requirements for and functions of board of directors, § 801.
Standards of conduct for officers, § 842.
Standards of liability for directors, § 831.

OFFICIAL COMMENT

Section 830 sets standards of conduct for directors that focus on the manner in which directors make their decisions, not the correctness of the decisions made. Section 830 should be read in light of the basic role of directors set forth in Section 801(b), which provides that the “activities and affairs of the corporation must be managed by or under the direction, and subject to the oversight, of” the board, as supplemented by various provisions of the act assigning specific powers or responsibilities to the board. The standards of conduct for directors established by section 830 are analogous to those generally articulated by courts in evaluating director conduct, often referred to as the duties of care and loyalty.

Section 830 addresses standards of conduct of directors, i.e., the level of performance expected of directors undertaking the role and responsibility of the office of director. Section 830 does not address the liability of a director, although exposure to liability may result from a
failure to satisfy the standards of conduct required to be observed. The issue of director liability is addressed in Sections 831 and 832. Section 830 does, however, play an important role in evaluating a director’s conduct and the effectiveness of board action. It has relevance in assessing, under Section 831, the reasonableness of a director’s belief. Similarly, it has relevance in assessing a director’s timely attention to appropriate inquiry when particular facts and circumstances of significant concern materialize. It also serves as a frame of reference for determining, under Section 832(a), liability for an unlawful distribution. Finally, Section 830 compliance may influence a court’s analysis where injunctive relief against a transaction is being sought. Directors act both individually and collectively as a board in performing their functions and discharging their duties. Section 830 addresses actions in both capacities

Under the standards of Section 830, the board of directors may delegate or assign to appropriate officers or employees of the corporation the authority or duty to exercise powers that the law does not require the board to retain. Because the directors are entitled to rely on these persons, absent knowledge making reliance unwarranted, the directors will not be in breach of the standards under section 830 as a result of their delegatees’ actions or omissions, so long as the board acted in good faith and complied with the other standards of conduct set forth in section 830 in delegating responsibility and, where appropriate, monitoring performance of the duties delegated. In addition, Sections 830 (d), (e) and (f) permit a director to rely on enumerated third parties for specified purposes, although reliance is prohibited when a director has knowledge that makes reliance unwarranted. Section 830(a)’s standards of good faith and reasonable belief in the best interests of the corporation also apply to a director’s reliance under Sections 830 (d), (e), and (f).

This section also applies to a designated body pursuant to Section 812.

1. Section 830(a)

Section 830(a) establishes the basic standards of conduct for all directors and its mandate governs all aspects of directors’ conduct, including the requirements in other provisions of Section 830.

Two of the phrases used in Section 830(a) deserve further comment:

(1) The phrase “reasonably believes” is both subjective and objective in character. Its first level of analysis is geared to what the particular director, acting in good faith, actually believes—not what objective analysis would lead another director (in a like position and acting in similar circumstances) to conclude. The second level of analysis is focused specifically on “reasonably.” Although a director has wide discretion in gathering information and reaching conclusions, whether a director’s belief is reasonable (i.e., could (not would) a reasonable person in a like position and acting in similar circumstances, taking into account that director’s knowledge and experience, have arrived at that belief) ultimately involves an overview that is objective in character.
The phrase “best interests of the nonprofit corporation” is key to an understanding of a director’s duties. The term “corporation” is a surrogate for the enterprise and its purpose, as well as the members in a membership corporation that is not a charitable corporation.

Section 830 operates as a “baseline” principle governing director conduct in circumstances uncomplicated by self-interest. The act recognizes, however, that directors’ personal interests may not always align with the nonprofit corporation’s best interests and provides procedures by which situations and transactions involving conflicts of interest can be processed. See Subchapter E (indemnification and advancement of expenses) and Subchapter F (conflicting interest transactions) of this Chapter 8 and Chapter 5 (derivative proceedings). Those procedures generally contemplate that the interested director will provide appropriate disclosures and will not be involved in taking action the matter giving rise to the conflict of interest.

2. Section 830(b)

Section 830(b) establishes a general standard of care for directors in the context of their dealing with the board’s decision-making and oversight functions. Although certain aspects will involve individual conduct (e.g., preparation for meetings), these functions are generally performed by the board through collective action, as recognized by the reference in Section 830(b) to board and committee “members” and “their duties.” In contrast with Section 830(a)’s individual conduct mandate, Section 830(b) has a two-fold thrust: it provides a standard of conduct for individual action and, more broadly, it states a conduct obligation—“must discharge their duties”—concerning the degree of care to be used collectively by the directors when performing those functions. The standard is not what care a particular director might believe appropriate in the circumstances, but what a person in a like position and acting under similar circumstances would reasonably believe to be appropriate. Thus, the degree of care that directors should employ, under Section 830(b), involves an objective standard.

The process by which directors become informed in carrying out the decision-making and oversight functions will vary. The directors’ decision-making function is reflected in various sections of the act, including dismissal of derivative proceedings (Section 505); determination and authorization of indemnification (Section 855); conflicting interest transactions; voidability (Section 860); amendment of articles of incorporation (Sections 902, 903, 905 and 907); amendment of bylaws (Sections 920 and 921); member approval of certain dispositions (Section 1002(b)(1)); and approval of dissolution (Section 1102). The directors’ oversight function is established under Section 801. In discharging the Section 801 duties associated with the board’s oversight function, the standard of care entails primarily a requirement of attention. In contrast with the board’s decision-making function, which generally involves informed action at a point in time, the oversight function is concerned with a continuum and the attention of the directors accordingly involves participatory performance over a period of time.

Several of the phrases chosen to define the standard of conduct in Section 830(b) deserve specific mention:

(1) The phrase “becoming informed,” in the context of the decision-making function, refers to the process of gaining sufficient familiarity with the background facts and
circumstances to make an informed judgment. Unless the circumstances would permit a
reasonable director to conclude that he or she is already sufficiently informed, the standard of
care requires every director to take steps to become informed about the background facts and
circumstances before taking action on the matter at hand. The process typically involves review
of written materials provided before or at the meeting and attention to, or participation in, the
deliberations leading up to a vote. In addition to considering information and data on which a
director is expressly entitled to rely under Section 830(e), “becoming informed” can also involve
consideration of information and data generated by other persons; for example, review of
industry studies or research articles prepared by third parties. It can also involve direct
communications, outside of the boardroom, with members of management or other directors.
There is no one way for “becoming informed,” and both the method and measure—“how to” and
“how much”—are matters of reasonable judgment for the director to exercise.

(2) The phrase “devoting attention,” in the context of the oversight function, refers to
considering such matters as the nonprofit corporation’s information and reporting systems
generally and not to an independent investigation into particular system inadequacies or
noncompliance. Although directors typically give attention to future plans and trends as well as
current activities, they should not be expected to anticipate any particular problems that the
corporation may face except in those circumstances where something has occurred to make it
obvious to the board that the corporation should be addressing a particular problem. The standard
of care associated with the oversight function involves gaining assurances from management and
advisers that appropriate systems have been established, such as those concerned with legal
compliance, risk assessment or internal controls. Such assurances also should cover
establishment of ongoing monitoring of systems in place with appropriate follow-up responses
when alerted to issues requiring attention.

(3) The reference to “person,” without embellishment, is intended to avoid implying
any qualifications, such as specialized expertise or experience requirements, beyond the basic
attributes of common sense, practical wisdom, and informed judgment (however, see (6) below).

(4) The phrase “reasonably believe appropriate” refers to the array of possible options
that a person possessing the basic attributes of common sense, practical wisdom and informed
judgment would recognize to be available, in terms of the degree of care that might be
appropriate, and from which a choice by such person would be made. The measure of care that
such person might determine to be appropriate, in a given instance, would normally involve a
selection from the range of options and any choice within the realm of reason would be an
appropriate decision under the standard of care called for under Section 830(b). However, a
decision that is so removed from the realm of reason, or is so unreasonable, that it falls outside
the permissible bounds of sound discretion, and thus is an abuse of discretion, will not satisfy the
standard.

(5) The phrase “in a like position” recognizes that the “care” under consideration is
that which would be used by the “person” if that person were a director of the particular
nonprofit corporation.
The combined phrase “in a like position...under similar circumstances” is intended to recognize that (a) the nature and extent of responsibilities will vary, depending upon such factors as the size, complexity, urgency, and location of activities carried on by the particular nonprofit corporation, (b) decisions must be made on the basis of the information known to the directors without the benefit of hindsight, and (c) the special background, qualifications, and oversight responsibilities of a particular director may be relevant in evaluating that director’s compliance with the standard of care.

3. Section 830(c)

A requirement to disclose to other directors information that a director knows to be material to the decision-making or oversight functions of the board of directors or committee of the board is implicit in the standards of conduct set forth in Sections 830(a) and (b). Section 830(c) makes this explicit. Thus, for example, when a director knows information that the director recognizes is material to a decision by the board but is not known to the other directors, the director is obligated to see to it that such information is provided to the other directors. Such disclosure can occur through direct statements in meetings of the board, or by any other timely means, including, for example, communicating the information to the chair of the board or the chair of a committee, or to the corporation’s general counsel, and requesting that the recipient inform the other board or committee members of the information.

Section 830(c) recognizes that a duty of confidentiality to a third party can override a director’s obligation to share with other directors information pertaining to a current corporate matter. In some circumstances, a duty of confidentiality to a third party may even prohibit disclosure of the nature or the existence of the duty itself. Ordinarily, however, a director who withholds material information based on a reasonable belief that a duty of confidentiality to a third party prohibits disclosure should advise the other directors of the existence and nature of that duty. Under the standards of conduct set forth in Section 830(a), the withholding of material information may, depending on the nature of the material information and of the matter before the board of directors or committee of the board, require that a director abstain or recuse himself or herself from all or a portion of the other directors’ deliberation or vote on the matter to which the undisclosed information is material, or even resign as a director.

4. Section 830(d)

The delegation of authority and responsibility described in Section 830(d) may take a variety of forms, including (a) formal action, (b) implicit action through the election of corporate officers (e.g., chief financial officer or controller) or the appointment of corporate managers (e.g., credit manager), or (c) informal action through an appropriate course of conduct. Under Section 830(d), a director may properly rely on those to whom authority has been delegated pursuant to Section 830(d) respecting particular matters calling for specific action or attention in connection with the directors’ decision-making function as well as matters on the board’s continuing agenda, such as legal compliance and internal controls, in connection with the directors’ oversight function. Delegation should be carried out in accordance with the standard of care set forth in Section 830(b).
By identifying those persons upon whom a director may rely in connection with the discharge of duties, Section 830(d) does not limit the ability of directors to delegate their powers under Section 801(b), except where delegation is expressly prohibited by the act or otherwise by applicable law. See Section 825 and its Official Comment for discussion of delegation to committees of the board of the authority of the board under Section 801. By employing the concept of delegation, the act does not limit the ability of directors to establish baseline principles as to management responsibilities. Specifically, Section 801(b) provides that “all corporate powers must be exercised by or under the authority of” the board, and a basic board function involves the allocation of management responsibilities and the related assignment (or delegation) of corporate powers. For example, a board can properly decide to retain a third party to assume responsibility for the administration of designated aspects of risk management for the nonprofit corporation (e.g., health insurance or disability claims).

Although the board of directors may delegate the authority or duty to perform one or more of its functions, delegation and reliance under Section 830(d) may not alone constitute compliance with Sections 830(a) and (b) and the action taken by the delegatee may not alone satisfy the directors or a noncommittee board member’s Section 801 responsibilities. On the other hand, failure of the board committee or the corporate officer or employee performing the function delegated to meet Section 830(b)’s standard of care will not automatically result in violation by the board of Section 801. Factors to be considered in determining whether a violation of Section 801 has occurred will include the care used in the delegation to and supervision over the delegatee, and the amount of knowledge regarding the particular matter which is reasonably available to the particular director. Care in delegation and supervision includes appraisal of the capabilities and diligence of the delegatee in light of the subject and its relative importance and may be satisfied, in the usual case, by receipt of reports concerning the delegatee’s activities. The enumeration of these factors is intended to emphasize that directors may not abdicate their responsibilities and avoid accountability simply by delegating authority to others. Rather, a director who is accountable for the acts of delegatees will fulfill the director’s duties if the standards contained in section 830 are met.

5. Section 830(e)

Reliance under Section 830(e) on a report, statement, opinion, or other information is permitted only if the director has read or heard orally presented the report, statement, opinion, or other information in question, or took other steps to become generally familiar with it. A director must comply with the general standard of care of Section 830(b) in making a judgment as to the reliability and competence of the source of information upon which the director proposes to rely or, as appropriate, that it otherwise merits confidence.

6. Section 830(f)

In determining whether a corporate officer or employee is “reliable,” for the purposes of Section 830(f)(1), the director would typically consider (i) the individual’s background experience and scope of responsibility within the nonprofit corporation in gauging the individual’s familiarity and knowledge respecting the subject matter, and (ii) the individual’s record and reputation for honesty, care and ability in discharging responsibilities which he or she
undertakes. In determining whether a person is “competent,” the director would normally take into account the same considerations and, if expertise should be relevant, the director would consider the individual’s technical skills as well. Recognition of the right of one director to rely on the expertise and experience of another director, in the context of board or committee deliberations, is unnecessary, for reliance on shared experience and wisdom of other board members is an implicit underpinning of collective board conduct. In relying on another member of the board, a director would quite properly take advantage of the colleague’s knowledge and experience in becoming informed about the matter at hand before taking action; however, the director would be expected to exercise independent judgment when it comes time to vote.

Advisers on whom a director may rely under Section 830(f)(2) include not only licensed professionals, such as lawyers and accountants, but also those in other fields involving special experience and skills, such as management consultants. The adviser could be an individual or an organization, such as a law firm, accounting firm or investment advisory firm. Reliance on a nonmanagement director who is specifically engaged to undertake a special assignment or a particular consulting role would fall within this outside adviser frame of reference. In addition, a director may also rely on outside advisers where skills or expertise of a technical nature is not a prerequisite, or where the person’s professional or expert competence has not been established, so long as the director reasonably believes the person merits confidence. For example, a board might choose to engage a private investigator to inquire into a particular matter (e.g., follow up on rumors about a senior executive’s alleged misconduct) and properly rely on the private investigator’s report.

Section 803(f)(3) permits reliance on a board committee when it is submitting recommendations for action by the full board of directors as well as when it is performing supervisory or other functions in instances where neither the full board nor the committee takes dispositive action. For example, the compensation committee typically reviews proposals and makes recommendations for action by the full board. There also might be reliance upon an investigation undertaken by a board committee and reported to the full board, which forms the basis for a decision by the board not to take dispositive action. Another example is reliance on a board committee, such as an audit committee with respect to the board’s ongoing role of oversight of the accounting and auditing functions of the corporation. In addition where reliance on information or materials prepared or presented by a board committee is not involved, in connection with board action, a director may properly rely on oversight monitoring or dispositive action by a board committee (of which the director is not a member) empowered to act pursuant to authority delegated under Section 825 or acting with the acquiescence of the board. See the Official Comment to Section 825. A director may similarly rely on committees not created under Section 825 which have nondirector members and on designated bodies. In parallel with Section 830(f)(2)(ii), the concept of “confidence” is used instead of “competence” to avoid any inference that technical skills are a prerequisite. In the usual case, the appointment of committee members or the reconstitution of the membership of a standing committee (e.g., the audit committee), would alone manifest the noncommittee members’ belief that the committee “merits confidence.” Depending on the circumstances, the reliance contemplated by Section 830(f)(3) is geared to the point in time when the board takes action or the period of time over which a committee is engaged in an oversight function; consequently, the judgment to be made (i.e., whether a committee “merits confidence”) will arise at varying points in time. Ordinarily, after

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making an initial judgment that a committee (of which a director is not a member) merits confidence, a director may continue to rely on that committee so long as the director has no reason to believe that confidence is no longer warranted.

Section 830(f)(4) provides a special rule for religious corporations that permits directors to rely on superior authorities within a religious organization of which the corporation is a part.

7. Application To Officers

Section 830 generally deals only with directors and, pursuant to Section 812(a), with members of designated bodies. Section 842 and its Official Comment explain the extent to which principles set forth in Section 830 apply to officers.

8. Trust Property

Section 830(g) is not found in the Model Business Corporation Act because it is only relevant in the context of nonprofit corporations. It provides that a director is not a trustee with respect to the corporation or any property held by it. Absent Section 830(g), it might be possible to argue that a director meeting his or her duties under Section 830 was liable for a breach of trust by improperly using, disposing of, or otherwise dealing with assets held by the corporation in trust. As a result of Section 830(g), this argument has no validity. A director who satisfies Subchapter 8C, but improperly acts or fails to act in regard to property held in trust, will not be liable. Depending on a particular state’s law, if a corporation holds trust property, the corporation itself may be liable for breach of trust.

§ 831. STANDARDS OF LIABILITY FOR DIRECTORS

(a) A director shall not be liable to the nonprofit corporation or its members for any decision to take or not to take action, or any failure to take any action, as a director, unless the party asserting liability in a proceeding establishes that:

(1) liability is not precluded by a defense interposed by the director based on:

(i) any provision in the articles of incorporation authorized by Section 202(b)(10) or (c) (articles of incorporation);

(ii) the protection afforded by Section 860 (conflicting interest transactions; voidability); or

(iii) the protection afforded by Section 870 (business opportunities); and

(2) the challenged conduct consisted or was the result of:

(i) action not in good faith; or
(ii) a decision:

(A) which the director did not reasonably believe to be in the best interests of the corporation, or

(B) as to which the director was not informed to an extent the director reasonably believed appropriate in the circumstances; or

(iii) a lack of objectivity due to the director’s familial, financial or business relationship with, or a lack of independence due to the director’s domination or control by, another person having a material interest in the challenged conduct:

(A) which relationship or which domination or control could reasonably be expected to have affected the director’s judgment respecting the challenged conduct in a manner adverse to the corporation, and

(B) after a reasonable expectation to such effect has been established, the director shall not have established that the challenged conduct was reasonably believed by the director to be in the best interests of the corporation; or

(iv) a sustained failure of the director to devote attention to ongoing oversight of the activities and affairs of the corporation, or a failure to devote timely attention, by making (or causing to be made) appropriate inquiry, when particular facts and circumstances of significant concern materialize that would alert a reasonably attentive director to the need for such inquiry; or

(v) receipt of a financial benefit to which the director was not entitled or any other breach of the director’s duties to deal fairly with the corporation and its members that is actionable under applicable law.

(b) The party seeking to hold the director liable:

(1) for money damages, has the burden of establishing that:

(i) harm to the nonprofit corporation or its members has been suffered, and

(ii) the harm suffered was proximately caused by the director’s challenged conduct; or

(2) for other money payment under a legal remedy, such as compensation for the unauthorized use of corporate assets, shall also have whatever persuasion burden may be called for to establish that the payment sought is appropriate in the circumstances; or
for other money payment under an equitable remedy, such as profit recovery by or disgorgement to the corporation, shall also have whatever persuasion burden may be called for to establish that the equitable remedy sought is appropriate in the circumstances.

(c) Nothing contained in this section:

(1) in any instance where fairness is at issue, such as consideration of the fairness of a transaction to the nonprofit corporation under Section 860(a)(3), alters the burden of proving the fact or lack of fairness otherwise applicable,

(2) alters the fact or lack of liability of a director under another section of this [Act], such as the provisions governing the consequences of an unlawful distribution under Section 832 (directors’ liability for unlawful distributions), a conflicting interest transaction under Section 860, or taking advantage of a business opportunity under Section 870; or

(3) affects any rights to which the corporation or a director or member may be entitled under another statute of this state or the United States.

(d) Notwithstanding any other provision of this section, a director of a charitable corporation is not liable to the corporation or its members for money damages for any action taken, or any failure to take any action, as a director, except liability for:

(1) the amount of a financial benefit received by the director to which the director is not entitled;

(2) an intentional infliction of harm;

(3) a violation of Section 832; or

(4) an intentional violation of criminal law.


CROSS-REFERENCES

Derivative proceedings, Ch. 5.
Director’s conflicting interest transaction, Subch. 8F.
Directors’ liability for unlawful distributions, § 832
Duty of board of directors, § 801.
Expanded indemnification, § 202(b)(8).
Indemnification and advancement of expenses, Subch. 8F.
Loans to or guarantees for directors and officers, § 833.
 Provision limiting or eliminating director liability, § 202(c).
Removal of directors by judicial proceedings, § 809.
Standards of conduct for directors, § 830.
OFFICIAL COMMENT

Boards of directors and corporate managers make numerous decisions that involve the balancing of risks and benefits for the enterprise. Although some decisions turn out to have been unwise or the result of a mistake of judgment, it is not reasonable to impose liability for an informed decision made in good faith that with the benefit of hindsight turns out to be wrong or unwise. Therefore, as a general rule, a director is not exposed to personal liability for injury or damage caused by an unwise decision, and conduct conforming with the standards of Section 830 will almost always be protected regardless of the end result. Moreover the fact that a director’s performance fails to meet the standards of Section 830 does not in itself establish personal liability for damages that the nonprofit corporation may have suffered as a consequence. Nevertheless, a director can be held liable for misfeasance or nonfeasance in performing his or her duties. Section 831 sets forth the standards of liability of directors, as distinct from the standards of conduct set forth in Section 830.

This section also applies to a designated body pursuant to Section 812.

Courts have developed the broad common law concept of the business judgment rule. Although formulations vary, in basic principle, a board of directors generally enjoys a presumption of sound business judgment and its decisions will not be disturbed by a court substituting its own notions of what is or is not sound business judgment if the board’s decisions can be attributed to any rational business purpose. It is also presumed that, in making a business decision, directors act in good faith, on an informed basis, and in the honest belief that the action taken is in the best interests of the nonprofit corporation. The elements of the business judgment rule and the circumstances for its application continue to be developed and refined by courts. Accordingly, it would not be desirable to freeze the concept in a statute. Thus, section 831 does not codify the business judgment rule as a whole, although certain of its principal elements, relating to personal liability issues, are reflected in section 831(a)(2).

1. **Directors’ Liability**

A director’s exposure to financial liability (e.g., in a lawsuit for money damages suffered by the nonprofit corporation or its members claimed to have resulted from misfeasance or nonfeasance in connection with the performance of the director’s duties) can be analyzed as follows:

1. **Liability limitation.** If the nonprofit corporation is a charitable corporation (and its directors are accordingly entitled to the benefits of Section 831(d)), or if the corporation’s articles of incorporation contain a provision eliminating its directors’ liability to the corporation or its members for money damages, adopted pursuant to Section 202(c), there is no liability unless the director’s conduct involves one of the prescribed exceptions in Section 831(d) or Section 202(c) that preclude the elimination of liability. See Section 202 and its Official Comment.
2. Director’s conflicting interest transaction safe harbor. If the matter at issue involves a director’s conflicting interest transaction (as defined in Section 860) and one of the procedures in Section 860 has been followed to approve the transaction, there is no liability for the interested director arising out of the transaction.

3. Business opportunities safe harbors. Similarly, if the matter involves a director’s pursuit or taking of a business opportunity, there is no liability for that director if (i) an applicable limitation or elimination of any duty to offer that business opportunity has been adopted pursuant to Section 202(b)(10), or (ii) a safe harbor procedure under Section 870 has been properly implemented, even if the articles of incorporation contain no provision under Section 202(b)(10).

4. Business judgment rule. The presumptions, standards of judicial review, and procedural matters related to the business judgment rule may insulate a director from liability for conduct in connection with a corporate decision if none of (i) subsection (d), (ii) a provision of the articles of incorporation adopted pursuant to Section 202(c), or (iii) Section 870 does not shield the director’s conduct from liability.

5. Damages and proximate cause. If the business judgment rule does not shield the directors’ decision-making from liability, as a general rule it must be established that money damages were suffered by the nonprofit corporation or its members and those damages resulted from and were legally caused by the challenged act or omission of the director.

6. Other liability for money payment. Aside from a claim for damages, the director may have monetary liability for other reasons, for example, if corporate resources have been used without proper authorization.

7. Equitable profit recovery or disgorgement. An equitable remedy compelling the disgorgement of the director’s improper financial gain or entitling the nonprofit corporation to profit recovery, where directors’ duties have been breached, may require the payment of money by the director to the corporation.

8. Corporate indemnification. If the director is monetarily liable, the director may be indemnified by the nonprofit corporation for any payments made and expenses incurred, depending upon the circumstances. See Subchapter 8E.

9. Insurance. To the extent that corporate indemnification is not available, the director may be reimbursed for the money damages for which the director is accountable, together with proceeding-related expenses, if the claim and grounds for liability come within the coverage under directors’ and officers’ liability insurance that has been purchased by the nonprofit corporation pursuant to Section 857.

2. Section 831(a)

a. SECTION 831(a)(1) – affirmative defenses
If (i) a provision in the nonprofit corporation’s articles of incorporation adopted pursuant
to Section 202(c) shelters the director from liability for money damages, (ii) a provision in the
articles adopted pursuant to Section 202(b)(10) limits or eliminates any duty to offer the
particular business opportunity to the corporation and the procedures set forth in Section
202(b)(10) are followed, or (iii) approval under Section 860 or Section 870(a)(1) shelters the
director’s conduct in connection with a conflicting interest transaction or the pursuit or taking of
a business opportunity, and such defense applies to all claims in plaintiff’s complaint; then there
is no need to consider further the application of Section 831’s standards of liability. In any of
those events, the court would presumably grant the defendant director’s motion for dismissal or
summary judgment (or the equivalent) and the proceeding would be ended. If the defense applies
to some but not all of plaintiff’s claims, dismissal or summary judgment would presumably be
granted with respect to those claims. Termination of the proceeding or dismissal of claims on the
basis of a provision in the articles of incorporation or a safe harbor procedure will not
automatically follow, however, if the party challenging the director’s conduct can assert any of
the valid bases for contesting the availability of the liability shelter. Absent such a challenge, the
relevant shelter provision is self-executing and the individual director’s exoneration from
liability is automatic. Further, under both Section 860 and 870, the directors approving the
conflicting interest transaction or approving a director’s taking of the business opportunity will
presumably be protected as well, because compliance with the relevant standards of conduct
under Section 830 is important for their action to be effective and because, as noted above,
conduct meeting Section 830’s standards will almost always be protected.

If a claim of liability arising out of a challenged act or omission of a director is not
resolved and disposed of under Section 831(a)(1), Section 831(a)(2) provides the basis for
evaluating whether the conduct in question can be challenged. One of the elements in Section
831(a)(2) must be established for a director to have liability under Section 831.

b. SECTION 831(a)(2)(i) – GOOD FAITH

It is a basic standard under Section 831(a)(2)(i) that a director’s conduct in performing
the director’s duties be in good faith. If a director’s conduct can be successfully challenged
pursuant to other clauses of Section 831(a)(2), there is a substantial likelihood that the conduct in
question will also present an issue of good faith implicating Section 831(a)(2)(i). Similarly, if
Section 831(a)(2) included only subsection (i), much of the conduct with which the other clauses
are concerned could still be considered under that subsection, on the basis that such conduct
evidenced the director’s lack of good faith. Where conduct has not been found deficient on other
grounds, decision-making outside the bounds of reasonable judgment can give rise to an
inference of bad faith. That form of conduct, sometimes characterized as “reckless indifference”
or “deliberate disregard,” giving rise to an inference of bad faith also can raise a question
regarding whether the director could have reasonably believed that the best interests of the
 corporation would be served. These issues could arise, for example, in approval of conflicting
interest transactions. See the Official Comment to Section 860.

c. SECTION 831(a)(2)(ii) – REASONABLE BELIEF

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Liability under Section 831(a)(2)(ii) turns on a director’s reasonable belief with respect to the nature of the director’s decision and the degree to which the director has become informed. In each case, the director must have an actual subjective belief and, so long as it is the director’s honest and good faith belief, a director has wide discretion. There is also an objective element to be met, in that the director’s belief must also be reasonable. The inquiry is similar to that in section 830(a) – could a reasonable person in a like position and acting in similar circumstances have arrived at that belief? In the rare case where a decision respecting the corporation’s best interests is so removed from the realm of reason (e.g., corporate waste), or a belief as to the sufficiency of the director’s preparation to make an informed judgment is so unreasonable as to fall outside the permissible bounds of sound discretion (e.g., if the director has undertaken no preparation and is completely uninformed), the director’s judgment will not be sustained.

d. SECTION 831(a)(2)(iii) – LACK OF OBJECTIVITY OR INDEPENDENCE

If the matter at issue involves a director’s transactional interest, such as a “director’s conflicting interest transaction” in which a “related person is involved (see Section 860), it will be governed by Section 860; otherwise, a lack of objectivity due to a relationship’s influence on the director’s judgment will be evaluated, in the context of the pending challenge of the director’s conduct under Section 831. If the matter at issue involves lack of independence, the proof of domination or control and its influence on the director’s judgment will typically entail different (and perhaps more convincing) evidence than what may be involved in a lack of objectivity case. The variables are manifold, and the facts must be sorted out and weighed on a case-by-case basis. For example, the closeness or nature of the relationship with the person allegedly exerting influence on the director could be a factor. If the director is required under section 831(a)(2)(iii)(B) to establish that the action taken by the director was reasonably believed to be in the best interests of the corporation, the inquiry will involve the elements of actual subjective belief and objective reasonableness similar to those found in Sections 831(a)(2)(ii) Section 830(a). To call into question the director’s objectivity or independence on the basis of a person’s relationship with, or exertion of dominance over, the director, the person must have a material interest in the challenged conduct.

In the typical case, analysis of another’s interest would first consider the materiality of the transaction or conduct at issue – in most cases, any transaction or other action involving the attention of the board of directors or a board committee will cross the materiality threshold, but not always – and would then consider the materiality of that person’s interest in the matter. The possibility that a director’s judgment would be adversely affected by another’s interest in a transaction or conduct that is not material, or that another’s immaterial interest in a transaction or conduct, is sufficiently remote that it should not be made subject to judicial review.

In situations where there may be a lack of objectivity, domination, a conflict of interest or divided loyalty, or even where there may be grounds for the issue to be raised, the better course to follow where board or committee action is required is usually for the director to disclose the facts and circumstances posing the possible issue, and then to withdraw from the meeting (or, in the alternative, to abstain from the deliberations and voting). The directors free of any possible taint may then take appropriate action as contemplated by section 830 (or section 860, if
If this course is followed, the director’s conduct respecting the matter in question should be beyond challenge.

e. SECTION 831(a)(2)(iv) – FAILURE TO DEVOTE ATTENTION

The director’s role involves two fundamental components: the decision-making function and the oversight function. In contrast with the decision-making function, which generally involves action taken at a point in time, the oversight function under Section 801(b) involves ongoing monitoring of the nonprofit corporation’s activities and affairs over a period of time. Although the facts will be outcome-determinative, deficient conduct involving a sustained failure to exercise oversight – where found actionable – has typically been characterized by the courts in terms of abdication and continued neglect by a director to devote attention, not a brief distraction or temporary interruption. Also, embedded in the oversight function is the need to inquire when suspicions are aroused. This need to inquire is not a component of ongoing oversight, and does not entail proactive vigilance, but arises under Section 831(a)(2)(iv) when, and only when, particular facts and circumstances of material concern (e.g., evidence of embezzlement at a high level or the discovery of significant inventory shortages) surface.

f. SECTION 831(a)(2)(v) – IMPROPER FINANCIAL BENEFIT AND OTHER BREACHES OF DUTIES

The first clause of Section 831(a)(2)(v) should be read in conjunction with Section 860, which deals with directors’ transactional interests. Section 860’s coverage of those interests is exclusive and its procedures provide shelter from legal challenges based on interest conflicts, when properly observed, will establish a director’s entitlement to any financial benefit gained from the transactional event.

Unauthorized use of a nonprofit corporation’s assets also would provide a basis for a proper challenge of a director’s conduct. There can be other forms of improper financial benefit not involving a transaction with the corporation or use of its facilities, such as where a director profits from unauthorized use of proprietary information.

There is no materiality threshold that applies to a financial benefit to which a director is not properly entitled. The act observes this principle in several places, for example, the exception to liability elimination prescribed in section 202(b)(4)(i) and the indemnification restriction in section 851(d)(2), as well as the liability standard in section 831(a)(2)(v).

The second clause of Section 851(a)(2)(v) is, in part, a catchall provision that implements the intention to make Section 831 a generally inclusive provision but, at the same time, to recognize the existence of other breaches of common law principles that can give rise to liability for directors. As developed in the case law, these actionable breaches may include unauthorized use of corporate property or information (which as noted above, might also be characterized as receipt of an improper financial benefit), unfair competition with the nonprofit corporation or the taking of a corporate opportunity. In the case of corporate opportunity, if the director is alleged to have wrongfully diverted a business opportunity as to which the corporation had a prior right, the act provides two possible safe harbors. First, any duty to offer the business opportunity to the
corporation may have been limited or eliminated pursuant to a provision in the articles of
corporation authorized by section 202(b)(10). Second, section 870(a)(1) provides a safe harbor
procedure for a director who wishes to pursue or take advantage of a business opportunity,
regardless of whether such opportunity would be characterized as a “corporate opportunity”
under existing case law. Note that section 870(b) provides that the fact that a director did not
employ the safe harbor procedure of section 870(a)(1) does not create an implication that the
opportunity should have first been presented to the corporation or alter the burden of proof
otherwise applicable to establish a breach of the director’s duty to the corporation.

3. Section 831(b)

Whether a nonprofit corporation or its members have suffered harm and whether a
particular director’s conduct was the proximate cause of that harm may be affected by the
collective nature of board action. Proper performance of the relevant duty through the action
taken by the director’s colleagues can overcome the consequences of his or her deficient
conduct. For example, where a director’s conduct can be challenged under Section
831(a)(2)(ii)(B) by reason of having been uninformed about the decision – he or she did not read
the merger materials distributed before the meeting or arrived late at the board meeting just in
time for the vote but, nonetheless, voted in favor solely because the others were in favor – the
favorable action by a quorum of properly informed directors would ordinarily protect the director
against liability, either because there was no harm or the offending director’s actions were not
the proximate cause of the harm. Although the concept of “proximate cause” is a term of art that
is basic to tort law, for purposes of Section 831(b)(1), a useful approach for the concept’s
application would be that the challenged conduct must have been a “substantial factor in
producing the harm.”

4. Section 831(c)

Section 831(c) expressly disclaims any shift of the burden of proof otherwise applicable
where the question of the fairness of a transaction or other challenged conduct is at issue. This is
the case whether the question of fairness arises under another section of the Act, such as Section
860, under existing case law, under a judicial requirement in a particular instance or otherwise.
Similarly, Section 831 does not affect liability under other sections of the Act. It also does not
foreclose any rights of the nonprofit corporation or its members under other laws. In addition,
directors can have liability to persons other than the corporation and its members, such as
liability to employee benefit plan participants and beneficiaries (who may or may not be
members), if the directors are determined to be fiduciaries under other applicable laws, to
government agencies for regulatory violations or to individuals claiming damages for injury
governed by tort law concepts (e.g., libel or slander). Section 831 is not intended to change the
standards applicable under these other laws or legal principles.

§ 832. DIRECTORS’ LIABILITY FOR UNLAWFUL DISTRIBUTIONS

(a) A director who votes for or assents to a distribution made in violation of this [Act]
is personally liable to the nonprofit corporation for the amount of the distribution that exceeds
what could have been distributed without violating this [Act] if the party asserting liability establishes that, when taking the action, the director did not comply with Section 830 (standards of conduct for directors).

(b) A director held liable under subsection (a) for an unlawful distribution is entitled to:

(1) contribution from every other director who could be held liable under subsection (a) for the unlawful distribution; and

(2) recoupment from each person of the pro-rata portion of the amount of the unlawful distribution the person received, whether or not the person knew the distribution was made in violation of this [Act].

(c) A proceeding to enforce:

(1) the liability of a director under subsection (a) is barred unless it is commenced within two years after the date on which the distribution was made; or

(2) contribution or recoupment under subsection (b) is barred unless it is commenced within one year after the liability of the claimant has been finally adjudicated under subsection (a).


CROSS-REFERENCES

Article provision limiting liability, § 202(c).
Compensation and other permitted payments, § 641.
Director duties in dissolution, § 1109.
Distributions prohibited, § 640.
Indemnification, §§ 202(b)(8), 850 through 858.
Standards of conduct for directors, § 830.

OFFICIAL COMMENT

Section 832 has limited application to nonprofit corporations because most do not make distributions.

A director whose conduct, in voting for or assenting to a distribution, is challenged under Section 832 will have no liability unless the complaining party establishes a breach of the relevant standards of Section 830, for example a failure to act with the care required by Section 830(b) or reliance on persons or information unwarranted under Section 830(d) or Section 830(e). Although no attempt has been made in the act to work out in detail the relationship between the right of recoupment from other persons and the right of contribution from directors,
a court may equitably apportion the obligations and benefits arising from the application of the principles set forth in Section 832.

Section 832(c) limits the time within which a proceeding may be commenced against a director for an unlawful distribution and the time within which a proceeding for contribution or recoupment may be made. The one-year period specified in Section 832(c)(2) may end within or extend beyond the two-year period specified in Section 832(c)(1).

This section also applies to a designated body pursuant to Section 812.

§ 833. LOANS TO OR GUARANTEES FOR DIRECTORS AND OFFICERS

(a) A nonprofit corporation may not lend money to or guarantee the obligation of a director or officer of the corporation.

(b) This section does not apply to:

(1) an advance to pay reimbursable expenses reasonably expected to be incurred by a director or officer;

(2) an advance to pay premiums on life insurance if the advance is secured by the cash value of the policy;

(3) advances pursuant to [Subchapter] 8E (indemnification and advancement of expenses);

(4) loans or advances pursuant to employee benefit plans;

(5) a loan secured by the principal residence of an officer; or

(6) a loan to pay relocation expenses of an officer.

(c) The fact that a loan or guarantee is made in violation of this section does not affect the borrower’s liability on the loan.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.32.

OFFICIAL COMMENT

Section 833 is an optional section that prohibits all loans to and guarantees for directors and officers. Whether the potential abuse in this area is so great as to warrant prohibiting all loans and guarantees for the benefit of directors and officers is a policy judgment that individual states will need to make. Some members of the drafting committee for the act believe that having the ability to makes loans and guarantees may be beneficial to a nonprofit corporation, such as
when they are used to facilitate the recruitment of an executive from another area of the country
who will have substantial moving expenses. Other members of the drafting committee believe
that the potential abuses justify prohibiting all loans and guarantees notwithstanding the possible
benefits under certain circumstances.

If this section is not adopted in a particular state, the making of loans and guarantees will
still be subject to scrutiny under Sections 831 and 860.

[Subchapter] D
OFFICERS

§ 840. Officers.
§ 841. Functions of officers.
§ 842. Standards of conduct for officers.
§ 843. Resignation and removal of officers.

§ 840. OFFICERS

(a) A nonprofit corporation has the officers provided for in its articles of
incorporation or bylaws, and such other officers as the board of directors may provide or may
authorize other officers to appoint.

(b) The manner in which officers are appointed or elected must be in accordance with
any applicable provisions of the articles of incorporation or bylaws. Except as provided in the
articles or bylaws, the board of directors may elect individuals to fill any office of a nonprofit
corporation. An officer may appoint one or more officers if authorized by the articles of
incorporation or bylaws or the board of directors.

(c) The articles of incorporation or bylaws or the board of directors must assign to an
officer responsibility for maintaining and authenticating the records of the corporation required
to be kept under Sections 401(a) (corporate records).

(d) Except as provided in the articles of incorporation or bylaws, the same individual
may simultaneously hold more than one office in a nonprofit corporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
Revision), § 8.40.

CROSS-REFERENCES

Agents of corporation, § 302.
Contract rights of officers, § 844.
“Designated body” defined, § 102.
Functions of officers, § 841.
Section 840 permits every nonprofit corporation to designate the officers it will have. No particular officers are required except as provided in Section 840(c).

The board of directors, as well as duly authorized officers, employees, or agents, may also appoint other agents for the nonprofit corporation. In addition, a board of directors has the intrinsic power to organize its own internal affairs, including designating officers of the board.

The officer who has the responsibility to maintain the minutes and authenticate the corporate records referred to in Section 401(a) is referred to as the “secretary” of the nonprofit corporation throughout the act. See Section 102. The person who is designated has authority to bind the corporation by that officer’s authentication under this section. This assignment of authority, traditionally vested in the corporate “secretary,” allows third persons to rely on authenticated records without inquiry as to their truth or accuracy.

The powers of the board of directors under this section may be vested by the articles of incorporation or bylaws in a designated body. See Sections 202(b)(2) and 812.

§ 841. FUNCTIONS OF OFFICERS

Each officer has the authority and the obligation to perform the functions set forth in the articles of incorporation or bylaws or, to the extent consistent with the articles and bylaws, the functions prescribed by the board of directors or by direction of an officer authorized by the board to prescribe the functions of other officers.


CROSS-REFERENCES

“Officer” defined, § 102.
Officers, § 840.
Officer as employee of corporation, see definition of “employee” in § 102.
“Secretary” defined, § 102.
Standards of conduct for directors, § 830.
Standards of conduct for officers, § 842.
OFFICIAL COMMENT

The methods of investing officers with formal authority in Section 841 do not exhaust the sources of an officer’s actual or apparent authority. Specific officers, particularly the chief executive officer, may have implied authority to take certain actions on behalf of the nonprofit corporation merely by virtue of their positions. This authority, which may overlap the express authority granted to an officer, generally has been viewed as extending only to transactions in the ordinary course of operations. Officers may also be vested with apparent authority by reason of corporate conduct on which third persons reasonably rely.

In addition to express, implied, or apparent authority, a nonprofit corporation is bound by unauthorized acts of officers if the unauthorized acts are ratified by the board of directors. Generally, ratification may extend only to acts that could have been authorized as an original matter. Ratification may itself be express or implied and may in some cases serve as the basis of apparent authority.

The powers of the board of directors under this section may be vested by the articles of incorporation or bylaws in a designated body. See Sections 202(b)(2) and 812.

§ 842. STANDARDS OF CONDUCT FOR OFFICERS

(a) An officer, when performing in that capacity, has the duty to act:

(1) in good faith;

(2) with the care that a person in a like position would reasonably exercise under similar circumstances; and

(3) in a manner the officer reasonably believes to be in the best interests of the corporation.

(b) The duty of an officer includes the obligation:

(1) to inform the superior officer to whom, or the board of directors or the board committee to which, the officer reports of information about the affairs of the nonprofit corporation known to the officer, within the scope of the officer’s functions, and known to the officer to be material to the superior officer, board, or committee; and

(2) to inform his or her superior officer, or another appropriate person within the nonprofit corporation, or the board of directors, or a board committee, of any actual or probable material violation of law involving the corporation or material breach of duty to the corporation by an officer, employee, or agent of the corporation, that the officer believes has occurred or is likely to occur.
(c) In discharging his or her duties, an officer who does not have knowledge that makes reliance unwarranted is entitled to rely on:

(1) the performance of properly delegated responsibilities by one or more employees of the nonprofit corporation whom the officer reasonably believes to be reliable and competent in performing the responsibilities delegated;

(2) information, opinions, reports, or statements, including financial statements and other financial data, prepared or presented by one or more officers or employees of the corporation whom the officer reasonably believes to be reliable and competent in the matters presented, or legal counsel, public accountants, or other persons retained by the corporation as to matters involving skills or expertise the officer reasonably believes are matters:

(i) within the particular person’s professional or expert competence, or

(ii) as to which the particular person merits confidence; or

(3) in the case of a corporation engaged in religious activity, religious authorities and ministers, rabbis, imams, or other persons whose positions or duties the officer reasonably believes justify reliance and confidence and whom the officer believes to be reliable and competent in the matters presented.

(d) An officer is not liable to the nonprofit corporation or its members for any decision to take or not to take action, or any failure to take any action, as an officer, if the duties of the office are performed in compliance with this section. Whether an officer who does not comply with this section shall have liability will depend in such instance on applicable law, including those principles of Section 831 (standards of liability for directors) that have relevance.


CROSS-REFERENCES

Appointment of officers, § 840.
Duties of officers, § 841.
Indemnification and advance of expenses, §§ 850 through 858.
Resignation and removal of officers, § 843.
Standards of conduct for directors, § 830.
Standards of liability for directors, § 831.

OFFICIAL COMMENT

Under Section 842(a), an officer, when performing in such officer’s official capacity, is required to meet standards of conduct generally specified for directors under Section 830 modified as appropriate to reflect the different role of officers. Section 842 is not intended to
modify, diminish or qualify the duties or standards of conduct that may be imposed upon specific
officers by other law or regulation. Section 842 applies to all officers, whether or not they are
also employees.

A duty on the part of officers and key employees to disclose to their superiors material
information relevant to the affairs of the corporation is implicit in, and embraced under, the
broader standard of Section 842(a), but Section 842(b) sets forth this disclosure obligation
explicitly. Section 842(b)(1) specifies that business information shall be transmitted through the
officer’s regular reporting channels. Section 842(b)(2) specifies the reporting responsibility
differently with respect to actual or probable material violations of law or material breaches of
duty. The use of the term “appropriate” in Section 842(b)(2) accommodates any normative
standard that the corporation may have prescribed for reporting potential violations of law or
duty to a specified person, such as an ombudsperson, ethics officer, internal auditor, general
counsel, or the like, as well as situations where there is no designated person but the officer’s
immediate superior is not appropriate (for example, because the officer believes that individual is
complicit in the unlawful activity or breach of duty).

Section 842(b)(1) should not be interpreted so broadly as to discourage efficient
delegation of functions. It addresses the flow of information to the board of directors and to
superior officers necessary to enable them to perform their decision-making and oversight
functions. See the Official Comment to Section 831. The officer’s duties under Section 842(b)
may not be negated by agreement; however, their scope under Section 842(b)(1) may be shaped
by prescribing the scope of an officer’s functional responsibilities.

With respect to the duties under Section 842(b)(2), codes of conduct or codes of ethics
may prescribe the circumstances in which and mechanisms by which officers and employees
may discharge their duty to report material information to superior officers or the board of
directors, or to other designated persons.

The term “material” modifying violations of law or breaches of duty in Section 842(b)(2)
denotes a qualitative as well as quantitative standard. It relates not only to the potential direct
financial impact on the nonprofit corporation, but also to the nature of the violation or breach.
For example, an embezzlement of $10,000, or even less, would be material because of the
seriousness of the offense, even though the amount involved might not be material to the
financial position or results of operations of the corporation.

The duty under Section 842(b)(2) is triggered by an officer’s subjective belief that a
material violation of law or breach of duty actually or probably has occurred or is likely to occur.
This duty is not triggered by objective knowledge concepts, such as whether the officer should
have concluded that such misconduct was occurring. The subjectivity of the trigger under
Section 842(b)(2), however, does not excuse officers from their obligations under Section 842(a)
to act in good faith and with due care in the performance of the functions assigned to them,
including oversight duties within their respective areas of responsibility. There may be occasions
when the principles applicable under Section 830(c) limiting the duty of disclosure by directors
where a duty of confidentiality is overriding may also apply to officers. See the Official
Comment to Section 830(c).
An officer’s ability to rely on others in meeting the standards prescribed in Section 842 may be more limited, depending upon the circumstances of the particular case, than the measure and scope of reliance permitted a director under Section 830, in view of the greater obligation the officer may have to be familiar with the affairs of the nonprofit corporation. The proper delegation of responsibilities by an officer, separate and apart from the exercise of judgment as to the delegatee’s reliability and competence, is concerned with the procedure employed. This will involve, in the usual case, sufficient communication such that the delegatee understands the scope of the assignment and, in turn manifests to the officer a willingness and commitment to undertake its performance. The entitlement to rely upon employees assumes that a delegating officer will maintain a sufficient level of communication with the officer’s subordinates to fulfill his or her supervisory responsibilities. The definition of “employee” in Section 102 includes an officer who is otherwise employed by the corporation; accordingly, Section 842 contemplates the delegation of responsibilities to other officers as well as to non-officer employees.

Although under Section 842(d), performance meeting that section’s standards of conduct will eliminate an officer’s exposure to any liability to the corporation or its shareholders, failure by an officer to meet that section’s standards will not automatically result in liability. Deficient performance of duties by an officer, depending upon the facts and circumstances, will normally be dealt with through intracorporate disciplinary procedures, such as reprimand, compensation adjustment, delayed promotion, demotion or discharge. These procedures may be subject to (and limited by) the terms of an officer’s employment agreement. See Section 844.

In some cases, failure to observe relevant standards of conduct can give rise to an officer’s liability to the nonprofit corporation or its members. A court review of challenged conduct will involve an evaluation of the particular facts and circumstances in light of applicable law. In this connection, Section 842(d) recognizes that relevant principles of Section 831, such as duties to deal fairly with the corporation and its members and the challenger’s burden of establishing proximately caused harm, should be taken into account. In addition, the business judgment rule will normally apply to decisions within an officer’s discretionary authority. Liability to others can also arise from an officer’s own acts or omissions (e.g., violations of law or tort claims) and, in some cases, an officer with supervisory responsibilities can have risk exposure in connection with the acts or omissions of others.

The Official Comment to Section 830 supplements this Official Comment to the extent that it can be appropriately viewed as generally applicable to officers as well as directors.

§ 843. RESIGNATION AND REMOVAL OF OFFICERS

(a) An officer may resign at any time by delivering notice to the board of directors, or its chair, or to the appointing officer or secretary. A resignation is effective when the notice is delivered unless the notice provides for a delayed effectiveness, including effectiveness determined upon a future event. If effectiveness of a resignation is stated to be delayed and the board of directors or the appointing officer accepts the delay, the board of directors or the
appointing officer may fill the pending vacancy before the delayed effectiveness but the new officer may not take office until the vacancy occurs.

(b) Except as provided in the articles of incorporation or bylaws, an officer may be removed at any time with or without cause by:

(1) the board of directors;

(2) the appointing officer, unless the article of bylaws of the board of directors provides otherwise; or

(3) any other officer authorized by the articles, the bylaws, or the board.

(c) In this section, “appointing officer” means the officer (including any successor to that officer) who appointed the officer resigning or being removed.


CROSS-REFERENCES

Contract rights of officers, § 844.
“Deliver” defined, § 102.
Effective date of notice, § 103(e).
Notice to the corporation, § 103.
“Secretary” defined, § 102.

OFFICIAL COMMENT

In part because of the unlimited power of removal under Section 843(b), a nonprofit corporation may enter into an employment agreement with the holder of an office that gives the officer rights in the event of removal or failure to be reelected or reappointed to office. This type of contract is binding on the corporation even if the articles of incorporation or bylaws provide that officers are elected for a term shorter than the period of the employment contract. Such an employment agreement does not override the removal power set forth in Section 843(b) and may give the officer the right to damages, but not specific performance, if employment is terminated before the end of the contract term.

Section 843(b) provides the corporation with the flexibility to determine when, if ever, an officer will be permitted to remove another officer. To the extent that the corporation wishes to permit an officer, other than the appointing officer, to remove another officer, the bylaws or the action by the board should set forth clearly the persons having removal authority.

A person may be removed from office irrespective of contract rights or the presence or absence of “cause” in a legal sense.
The powers of the board of directors under this section may be vested by the articles of incorporation or bylaws in a designated body. See Sections 202(b)(2) and 812.

§ 844. CONTRACT RIGHTS OF OFFICERS

(a) The election or appointment of an officer does not itself create contract rights.

(b) An officer’s removal does not affect the officer’s contract rights, if any, with the nonprofit corporation. An officer’s resignation does not affect the corporation’s contract rights, if any, with the officer.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.44. Cf. Model Business Corporation Act (2016 Revision), § 8.44.

CROSS-REFERENCES

Appointment of officers, § 840.
Resignation or removal of officers, § 843.

OFFICIAL COMMENT

The removal of an officer with contract rights is without prejudice to the officer’s rights in a proceeding seeking for damages for breach of contract. See the Official Comment to Section 843. Similarly, an officer with an employment contract who prematurely resigns may be in breach of the officer’s employment contract. The mere election or appointment of an officer for a term does not create a contractual obligation on the officer’s part to complete the term.

[Subchapter] E

INDEMNIFICATION AND ADVANCEMENT OF EXPENSES

§ 850. Subchapter definitions.
§ 851. Permissible indemnifications.
§ 852. Mandatory indemnification.
§ 853. Advancement of expenses.
§ 854. Court-ordered indemnification and advancement of expenses.
§ 855. Determination and authorization of indemnification.
§ 856. Indemnification of officers.
§ 857. Insurance.
§ 858. Variation of indemnification.
§ 859. Exclusivity of subchapter.

INTRODUCTORY COMMENT
The substance of this subchapter is based almost entirely on the 2016 revision to the Model Business Corporation Act ("MBCA"). Thus, the act closely follows the law with respect to indemnification of directors and officers of business corporations and advancement of their litigation expenses. This is consistent with the view that the relationship of directors to a nonprofit corporation is more akin to that of directors of business corporations than to that of trustees to their beneficiaries. Stern v. Lucy Webb Hayes National Training School for Deaconesses and Missionaries, 381 F.Supp. 1003 (D.D.C. 1974).

The only differences in the area of indemnification between this act and the MBCA are that this act (i) changes the rule in Section 852, (ii) omits Section 859 of the MBCA, and (iii) treats members of a designated body vested with some of the powers, authority, or functions of the board of directors, as directors. The change in Section 852 is explained in the Official Comment to that section. Omitted Section 859 of the MBCA provides that a business corporation "may provide indemnification or advancement of expenses to a director or officer only as permitted by" Sections 850 through 859. The omission from this act of a provision analogous to Section 859 of the MBCA means that the provisions of this Subchapter 8E will not be the exclusive basis for providing indemnification and advancement of expenses to directors and officers of nonprofit corporations. Defining "director" in Section 850(2) to include a member of a designated body is consistent with the role of designated bodies as provided in Section 812.

1. Policy Issues Raised by Indemnification and Advancement of Expenses

Indemnification (including advancement of expenses) provides financial protection by the nonprofit corporation for its directors against exposure to expenses and liabilities that may be incurred by them in connection with legal proceedings based on an alleged breach of duty in their service to or on behalf of the corporation.

The concept of indemnification recognizes that there will be situations in which even though the director does not satisfy all of the elements of the standard of conduct set forth in section 830(a) or the requirements of some other applicable law, the nonprofit corporation should nevertheless be permitted (or required) to absorb the economic costs incurred by the director in any ensuing litigation.

Subchapter 8E is an integrated treatment of indemnification and advancement of expenses and strikes a balance among important public policies. It would be difficult to persuade responsible persons to serve as directors if they were compelled to bear personally the cost of vindicating the propriety of their conduct in every instance in which it might be challenged. If permitted too broadly, however, indemnification may violate equally basic tenets of public policy. For example, a director who intentionally inflicts harm on the nonprofit corporation should not expect to receive assistance from the corporation for legal or other expenses and should be required to satisfy from that director’s personal assets not only any adverse judgment but also expenses incurred in connection with the proceeding. A similar policy issue is raised in connection with indemnification against liabilities or sanctions imposed under state or federal civil or criminal statutes. A shift of the economic cost of these liabilities from the individual director to the corporation by way of indemnification may in some instances frustrate the public policy of those statutes.
Some of the same policy considerations apply to the indemnification of officers and, in many cases, employees and agents. The indemnification of officers, whose functions are specified in Section 841, is dealt with separately in section 856. The indemnification of employees and agents, whose duties are prescribed by sources of law other than corporation law (e.g., contract and agency law), is beyond the scope of this subchapter. Section 858(d), however, makes clear that subchapter E does not limit a corporation’s power to indemnify or advance expenses to employees and agents in accordance with applicable law.

2. Relationship of Indemnification to Other Policies Established in the Act

Indemnification is closely related to the standards of conduct for directors and officers established elsewhere in Chapter 8. The structure of the act is based on the assumption that if a director acts consistently with the standards of conduct described in Section 830 or with the standards of a liability-limitation provision in the articles of incorporation (as authorized by Section 202(c)), the director will not have exposure to liability to the nonprofit corporation or to members and any expenses necessary to establish a defense will be borne by the corporation (under Section 852). The converse, however, is not necessarily true. The basic standards for indemnification set forth in Section 851 for a civil action, in the absence of an indemnification provision in the corporation’s articles (as authorized by Section 202(b)(8)), are good faith and reasonable belief that the conduct was in or not opposed to the best interests of the corporation. See Section 851. In some circumstances, a director or officer may be found to have violated a statutory or common law duty and yet be able to establish eligibility for indemnification under these standards of conduct. In addition, Subchapter E permits a director or officer who is held liable for violating a statutory or common law duty, but who does not meet the relevant standard of conduct, to petition a court to order indemnification under Section 854 if the court determines that it would be fair and reasonable to do so.

3. Application of Amendments to Prior Conduct

Each jurisdiction adopting amendments to its indemnification statutes should consider the extent to which the statutes, as amended, should apply to conduct occurring prior to the effective time of the amendments. Absent constitutional or statutory provisions dealing generally with retroactivity of statutory amendments, resolution of this issue may be made to depend upon whether a claim for indemnification was made prior to (and was pending at) the effective time of the amendment. Alternatively, the amended statute can specifically provide that it applies to conduct occurring before or after the effective time.

§ 850. SUBCHAPTER DEFINITIONS

In this [Subchapter]:

“Corporation” includes any domestic or foreign predecessor entity of a nonprofit corporation in a merger, conversion, or domestication.
“Director” or “officer” means an individual who is or was a director or officer, respectively, of a nonprofit corporation or who, while a director or officer of the corporation, is or was serving at the corporation’s request as a director, officer, manager, partner, trustee, employee, or agent of another domestic or foreign entity or employee benefit plan. A director or officer is considered to be serving an employee benefit plan at the corporation’s request if the individual’s duties to the corporation also impose duties on, or otherwise involve services by, the individual to the plan or to participants in or beneficiaries of the plan. “Director” includes a member of a designated body vested with some of the powers, authority, or functions of the board of directors. “Director” or “officer” includes, unless the context requires otherwise, the estate or personal representative of a director or officer.

“Disinterested director” means a director who, at the time of a vote referred to in Section 853(c) (advancement of expenses) or a vote or selection referred to in Section 855(b) or (c) (determination and authorization of indemnification), is not:

(i) a party to the proceeding; or
(ii) an individual having a familial, financial, professional, or employment relationship with the director whose indemnification or advancement of expenses is the subject of the decision being made, which relationship would, in the circumstances, reasonably be expected to exert an influence on the director’s judgment when voting on the decision being made.

“Liability” means the obligation to pay a judgment, settlement, penalty, fine (including an excise tax assessed with respect to an employee benefit plan), or expenses incurred with respect to a proceeding.

“Official capacity” means the office of director in a nonprofit corporation or the office in a corporation held by an officer. The term does not include service for any other domestic or foreign corporation, employee benefit plan, or other entity.

“Party” means an individual who was, is, or is threatened to be made, a defendant or respondent in a proceeding.


CROSS-REFERENCES

Act definitions, § 102.
Effect of merger, § 1226.
“Entity” defined, § 102.
“Expenses” defined, § 102.
Officers, § 840.
“Proceeding” defined, § 102.
The definitions set forth in Section 850 apply only to Subchapter 8E and have no application elsewhere in the act (except for the use of “liability in Section 202(b)(8)).

1. Corporation

Subchapter 8E’s definition of “corporation” includes predecessor entities that have been absorbed in mergers to negate any argument that a different result might be reached under Section 1226 (effect of merger), which provides for the assumption of liabilities by operation of law upon a merger. The express responsibility of successor entities for the liabilities of their predecessors under this subchapter is broader than under Section 1226 and may impose liability on a successor although Section 1226 does not. The definition of “corporation” in Section 850 is thus an essential aspect of the protection provided by this subchapter for persons eligible for indemnification. The definition of “corporation” similarly makes clear that predecessor entities in a conversion or domestication are included within the definition.

2. Director and Officer

A special definition of “director” and “officer” is included in Subchapter 8E to cover individuals who are made parties to proceedings because they are or were directors or officers or, while serving as directors or officers, also serve or served at the nonprofit corporation’s request in another capacity for another entity. The purpose of the latter part of this definition is to give directors and officers the benefits of the protection of this Subchapter 8E while serving at the corporation’s request in a responsible position for employee benefit plans, trade associations, nonprofit or charitable entities, domestic or foreign entities, or other kinds of profit or nonprofit ventures. To avoid misunderstanding, it is good practice from both the corporation’s and director’s or officer’s viewpoint for this type of request to be evidenced by board minutes, memorandum, or other writing.

Even without such a formal action, the second sentence of the definition of “director” or “officer” in Section 850 addresses the question of liabilities arising under the Employee Retirement Income Security Act of 1974 (ERISA). It makes clear that a director or officer who is serving as a fiduciary of an employee benefit plan is automatically viewed for purposes of this subchapter as having been requested by the nonprofit corporation to act in that capacity. Special treatment is believed necessary because of ERISA’s broad definition of “fiduciary” and the requirement that a “fiduciary” must discharge that individual’s duties “solely in the interest” of the participants and beneficiaries of the employee benefit plan. Decisions by a director or officer, who is serving as a fiduciary under the plan on questions regarding, for example (i) eligibility for benefits, (ii) investment decisions, or (iii) interpretation of plan provisions respecting (a) qualifying service, (b) years of service, or (c) retroactivity, are all subject to the protections of Subchapter 8E. See also the “official capacity” in Section 850.

In the last sentence of the definition of “director” or “officer” in Section 850, the phrase “unless the context requires otherwise” is intended to clarify that the estate or personal
representative does not have the right to participate in decisions by directors authorized in this subchapter.

3. Disinterested Director

This term identifies, for purposes of Subchapter 8E, those members of the board who are eligible to make, in the first instance, the authorizations and determinations required in connection with decisions on advancement of expenses and indemnification. It is used only in Sections 853(c) and 855(b) and (c) and is not applicable to any other sections of the act.

To be a “disinterested director,” a member of the board must not be a party to the proceeding at the time the board makes the determination or authorization and that director must not be the subject of the request for advance or indemnification with respect to which action is being taken. That director also must not have a familial, financial, professional, or employment relationship that could reasonably be expected to influence that director’s decision. The fact that a director was nominated for the board by directors who are parties to the proceeding or are interested in the request or that a director is also a director of another corporation of which the director who is a party to the proceeding or is interested in the request is also a director should not, absent unusual circumstances, constitute a disqualifying relationship.

4. Liability

“Liability” is defined for convenience to avoid repeated references to recoverable items throughout the subchapter. Even though the definition of “liability” includes amounts paid in settlement or to satisfy a judgment, indemnification against certain types of settlements and judgments is not allowed under several provisions of Subchapter 8E. For example, indemnification in suits brought by or in the right of the nonprofit corporation is limited to expenses (see Section 851(d)(1)), unless indemnification for a settlement is ordered by a court under Section 854(a)(3).

The definition of “liability” permits the indemnification of “expenses.” The definition of “expenses” in Section 102 limits expenses to those that are reasonable. The result is that any portion of expenses which is not reasonable should not be advanced or indemnified. In contrast, amounts paid to settle or satisfy substantive claims are not subject to a reasonableness test. Since payment of these amounts is permissive – mandatory indemnification is available under Section 852 only where the defendant is “wholly successful” – a limitation of “reasonableness” for settlements is inappropriate.

The definition of “liability” is intended to cover every type of monetary obligation that may be imposed upon a director, including civil penalties, restitution, and the levy of excise taxes under the Internal Revenue Code pursuant to ERISA.

5. Official Capacity

The term “official capacity” is used in determining which of the two alternative standards of conduct set forth in Section 851(a)(1)(ii) applies: If the action was taken in an “official
capacity,” the individual to be indemnified must have reasonably believed that the individual was acting in the best interests of the nonprofit corporation. In contrast, if the action in question was not taken in an “official capacity,” the individual need only have reasonably believed that the conduct was not opposed to the best interests of the corporation. See also the Official Comment to Section 851(a).

6. Party

The definition of “party” includes present and former parties in addition to individuals currently or formerly threatened with being made a party. An individual who is only called as a witness is not a “party” within this definition, but as specifically provided in Section 858(e), payment or reimbursement of witness expenses is not limited by this subchapter.

§ 851. PERMISSIBLE INDEMNIFICATION

(a) Except as otherwise provided in this section, a nonprofit corporation may indemnify an individual who is a party to a proceeding because the individual is or was a director against liability incurred in the proceeding if:

(1) (i) the director conducted himself or herself in good faith; and

(ii) the director reasonably believed:

(A) in the case of conduct in an official capacity, that the conduct was in the best interests of the corporation; and

(B) in all other cases, that his or her conduct was at least not opposed to the best interests of the corporation; and

(iii) in the case of any criminal proceeding, had no reasonable cause to believe his or her conduct was unlawful; or

(2) the director engaged in conduct for which broader indemnification has been made permissible or obligatory under a provision of the articles of incorporation (as authorized by Section 202(b)(8) (articles of incorporation)).

(b) A director’s conduct with respect to an employee benefit plan for a purpose the director reasonably believed to be in the interests of the participants in and the beneficiaries of the plan is conduct that satisfies the requirement of Section 851(a)(1)(ii)(B).

(c) The termination of a proceeding by judgment, order, settlement, or conviction, or upon a plea of nolo contendere or its equivalent, is not, of itself, determinative that the director did not meet the relevant standard of conduct described in this section.
(d) Unless ordered by a court under Section 854(a)(3) (court-ordered indemnification and advancement of expenses), a nonprofit corporation may not indemnify a director:

(1) in connection with a proceeding by or in the right of the corporation, except for expenses incurred in connection with the proceeding if it is determined that the director has met the relevant standard of conduct under Section 851(a); or

(2) in connection with any proceeding with respect to conduct for which the director was adjudged liable on the basis of receiving a financial benefit to which he or she was not entitled, regardless of whether it involved action in the director’s official capacity.


**CROSS-REFERENCES**

Advancement of expenses, § 853.
Conflicting interest transactions; voidability, § 860.
“Corporation” defined, § 850.
Court-ordered indemnification and advancement of expenses, § 854.
Derivative proceedings, Ch. 5.
Determination and authorization of indemnification, § 855.
“Director” defined, § 850.
Exclusivity of subchapter, § 859.
“Expenses” defined, § 102.
“Liability” defined, § 850.
Liability-limitation for charitable corporations, § 831(d).
Limiting director liability by provision in articles of incorporation, § 202(c)
Limits on indemnification for a predecessor of the corporation, § 858(c).
Mandatory indemnification, § 852.
Obligatory indemnification, §§ 202(b)(8) and 858.
“Officer” defined, § 850.
Officer indemnification, § 856.
“Official capacity” defined, § 850.
“Party” defined, § 850.
“Proceeding” defined, §§ 102 and 850.
Standards of conduct for directors, § 830.
Standards of liability for directors, § 831.

**OFFICIAL COMMENT**

1. *Section 851(a)*

The standards for indemnification of directors contained in Section 851(a) define the limits of the conduct for which discretionary indemnification is permitted under the act, except to the extent that court-ordered indemnification is available under Section 854(a)(3). Conduct that
falls within these limits does not automatically entitle directors to indemnification, although a nonprofit corporation may obligate itself to indemnify directors to the maximum extent permitted by applicable law. See Section 858(a). Absent such an obligatory provision, Section 852 defines much narrower circumstances in which directors are entitled as a matter of right to indemnification.

The standards of conduct in Section 851(a) are not dependent on the type of proceeding in which the claim arises. These standards are closely related, but not identical, to the standards of conduct imposed by Section 830 on directors when discharging the duties of a director: good faith, reasonable belief that the best interests of the corporation are being served, and appropriate care (i.e., that which a person in a like position would reasonably believe appropriate under similar circumstances).

As in the case of Section 830, where the concept of good faith is also used, Section 851 provides no definition for that term. The concept involves a subjective test, which would permit indemnification for an unwise decision or “a mistake of judgment.” even though made negligently by objective standards. Section 851 also requires, as does Section 830, a “reasonable” belief that conduct when acting in the director’s official capacity was in the nonprofit corporation’s best interests. It then adds a provision, not found in Section 830, relating to criminal proceedings that requires the director to have had no “reasonable cause” to believe that the conduct was unlawful. These both involve objective standards applicable to the director’s belief concerning the effect of the conduct in question. Conduct includes both acts and omissions.

In Section 851(a)(1)(ii)(B) the words “at least” qualify “not opposed to” and make clear that this standard is for conduct other than in an official capacity. Although this provision deals with indemnification by the nonprofit corporation, a director serving another entity at the request of the corporation remains subject to the provisions of the law governing service to that other entity, including provisions dealing with conflicts of interest. Should indemnification from the requesting corporation be sought by a director for acts done while serving another entity, which acts involved breach of a duty owed to that other entity, nothing in Section 851(a)(1)(ii)(B) would preclude the requesting corporation from considering, in assessing its own best interests, whether the fact that its director had engaged in a violation of the duty owed to the other entity was in fact “opposed to” the interests of the indemnifying corporation.

If the relevant standards are met, Section 851 also permits indemnification in connection with a proceeding involving an alleged failure to satisfy legal standards other than the standards of conduct in Section 830, e.g., violations of antitrust, environmental or securities laws.

In addition to indemnification under Section 851(a)(1), Section 851(a)(2) permits indemnification under the standard of conduct set forth in a provision of the articles of incorporation adopted pursuant to Section 202(b)(8). Based on such a provision, Section 851(a)(2) permits indemnification in connection with claims by third parties and, through Section 856, applies to officers as well as directors. (This goes beyond the scope of a provision of the articles of incorporation adopted pursuant to Section 202(c), which can only limit liability of directors against claims by the corporation or its members.) Section 851(a)(2) is subject to the
prohibition of Section 851(d)(1) against indemnification of settlements and judgments in derivative suits, except as ordered by a court under Section 854(a)(3). It is also subject to the prohibition of Section 851(d)(2) against indemnification for receipt of an improper financial benefit; however, this prohibition is already subsumed in the exception contained in Section 202(b)(8)(i).

2. Section 851(b)

As discussed in the Official Comment to the definition of “director” or “officer” in Section 850, ERISA requires that a “fiduciary” (as defined in ERISA) discharge the fiduciary’s duties “solely in the interest” of the participants in and beneficiaries of an employee benefit plan. The standard in Section 851(b) for indemnification of a director who is serving as a trustee or fiduciary for an employee benefit plan under ERISA is arguably an exception to the more general standard that conduct not in an official corporate capacity is indemnifiable if it is “at least not opposed to” the best interests of the nonprofit corporation. However, a corporation that causes a director to undertake fiduciary duties in connection with an employee benefit plan should expect the director to act in the best interests of the plan’s beneficiaries or participants. Thus, Section 851(b) establishes and provides a standard for indemnification that is consistent with the statutory policies embodied in ERISA. See Official Comment to Section 850(2).

3. Section 851(c)

Section 851(c) rejects the argument that indemnification is automatically improper whenever a proceeding has been concluded on a basis that does not exonerate the director claiming indemnification. However, any judicial determination of substantive liability should be taken into account in determining whether the standards of Section 851(a) were met. By the same token, it is clear that the termination of a proceeding by settlement or plea of no contest should not of itself create a presumption either that conduct met or did not meet the relevant standard of Section 851(a), since a settlement or plea of no contest may be agreed to for many reasons unrelated to the merits of the claim. On the other hand, a final determination of non-liability (including one based on a liability-limitation provision adopted under Section 202(c) or an acquittal in a criminal case automatically entitles the director to indemnification of expenses under Section 852.

4. Section 851(d)

Section 851(d) does not permit indemnification of settlements and judgments in derivative proceedings which would give rise to a circularity in which the nonprofit corporation receiving payment of damages by the director in the settlement or judgment (less attorneys’ fees) would then immediately return the same amount to the director (including attorneys’ fees) as indemnification. Thus, the corporation would be in a poorer economic position than if there had been no proceeding. Further, in many case, the director may be protected (i) by a provision in the articles of incorporation under Section 202(c) limiting liability, (ii) because liability of directors of a charitable corporation is limited by Section 831(d), or (iii) because a proceeding was dismissed under Section 505.
The prohibition on indemnification of a settlement or a judgment in a derivative proceeding, however, does not extend to the related expenses incurred in the proceeding so long as the director meets the relevant standard of conduct set forth in Section 851(a). In addition, indemnification and advance of expenses may be ordered by a court under Section 854(a)(3), even if the relevant standard was not met.

Indemnification under Section 851 is also prohibited if there has been an adjudication that a director received a financial benefit to which the director is not entitled, even if, for example, the director acted in a manner not opposed to the best interests of the nonprofit corporation. For example, improper use of inside information for financial benefit should not be an action for which the corporation may elect to provide indemnification, even if the corporation was not thereby harmed. Given the express language of Section 202(b)(8) establishing the outer limit of an indemnification provision contained in the articles of incorporation, a director found to have received an improper financial benefit would not be permitted indemnification under Section 851(a)(2). Although it is unlikely that a director found to have received an improper financial benefit could meet the standard in Section 851(a)(1)(ii)(B), this limitation is made explicit in Section 851(d)(2). Section 854(a)(3) permits a director found liable in a proceeding referred to in Section 851(d)(2) to petition a court for a judicial determination of entitlement to indemnification for expenses. The language of Section 851(d)(2) parallels Section 202(c)(1) and, thus, the same standards should be used in interpreting the application of both provisions. Although a settlement may create an obligation to pay money, it should not be construed for purposes of Subchapter 8E as an adjudication of liability.

§ 852. MANDATORY INDEMNIFICATION

A nonprofit corporation must indemnify a director to the extent the director was successful, on the merits or otherwise, in the defense of any proceeding to which the director was a party because the director was a director of the corporation against expenses incurred by the director in connection with the proceeding.


CROSS-REFERENCES

“Corporation” defined, § 850.
Court-ordered indemnification and advancement of expenses, § 854.
“Director” defined, § 850.
“Expenses” defined, § 102.
Limits on indemnification for a predecessor of the corporation, § 858(c).
“Party” defined, § 850.
Permissible indemnification, § 851.
“Proceeding” defined, §§ 102 and 850.

OFFICIAL COMMENT
Section 852 creates a right of indemnification in favor of the director who meets its requirements. Enforcement of this right by judicial proceeding is specifically contemplated by Section 854(a)(1). Section 854(b) gives the director a right to recover expenses incurred by him in enforcing his statutory right to indemnification under Section 852.

The basic standard for mandatory indemnification is that the director has been “wholly successful, on the merits or otherwise,” in the defense of the proceeding. A defendant is “wholly successful” only if the entire proceeding is disposed of on a basis which does not involve a finding of liability. A director who is precluded from mandatory indemnification by this requirement may still be entitled to permissible indemnification under section 851(a) or court-ordered indemnification under section 854(a)(3).

Although the standard “on the merits or otherwise” may result in an occasional defendant becoming entitled to indemnification because of procedural defenses not related to the merits, e.g., the statute of limitations or disqualification of the plaintiff, it is unreasonable to require a defendant with a valid procedural defense to undergo a possibly prolonged and expensive trial on the merits to establish eligibility for mandatory indemnification.

§ 853. ADVANCEMENT OF EXPENSES

(a) A nonprofit corporation may, before final disposition of a proceeding, advance funds to pay for or reimburse the expenses incurred in connection with the proceeding by an individual who is a party to the proceeding because that individual is or was a director, if the director delivers to the corporation an undertaking in a record to repay any funds advanced if:

(1) the director is not entitled to mandatory indemnification under Section 852 (mandatory indemnification); and
(2) it is ultimately determined under Section 854 (court-ordered indemnification and advancement of expenses) or 855 (determination and authorization of indemnification) that the director is not entitled to indemnification.

(b) The undertaking required by subsection (a) must be an unlimited general obligation of the director, but need not be secured and may be accepted without reference to the financial ability of the director to make repayment.

(c) Authorizations under this section shall be made:

(1) by the board of directors:
(i) if there are two or more disinterested directors, by a majority vote of all the disinterested directors (a majority of whom will constitute a quorum for that purpose) or by a majority of the members of a committee of two or more disinterested directors appointed by such a vote; or
(ii) if there are fewer than two disinterested directors, by the vote necessary for action by the board in accordance with Section 824(c) (quorum and voting), in which authorization directors who do not qualify as disinterested directors may participate; or

(2) by the members.


CROSS-REFERENCES

Committees of the board, § 825.
“Corporation” defined, § 850.
Court-ordered advancement of expenses, § 854.
Determination and authorization of indemnification, § 855.
“Director” defined, § 850.
“Disinterested director” defined, § 850.
“Expenses” defined, § 102.
Limits on advancement of expenses, § 858(c).
“Party” defined, § 850.
“Proceeding” defined, §§ 102 and 850.
Quorum of directors, § 824(a).
Standard for indemnification, § 851.

OFFICIAL COMMENT

Section 853 authorizes, but does not require, a nonprofit corporation to advance or reimburse a director’s reasonable expenses, subject to delivery of the repayment undertaking required by Section 853(a) and any limitations set forth in the articles of incorporation or bylaws pursuant to Section 858(d). The repayment undertaking required by section 853 is also required in connection with obligatory advancement pursuant to section 858(a).

Section 853 recognizes an important difference between indemnification and an advancement of expenses: indemnification is retrospective and, therefore, enables the persons determining whether to indemnify to do so on the basis of known facts, including the outcome of the proceeding. Indemnification may include reimbursement for expenses that were not advanced. Advancement of expenses is necessarily prospective and, in situations where advancement is not obligatory, the individuals making the decision whether to authorize expense advancement generally have fewer known facts on which to base their decision.

Section 853 reflects a determination that it is sound public policy to permit the nonprofit corporation to advance (by direct payment or by reimbursement) the defense expenses of a director so long as the director agrees to repay any amounts advanced, if it is ultimately determined that the director is not entitled to indemnification. This policy is based upon the view that an individual who serves an entity in a representative capacity should not be required to
finance that individual’s own defense of actions taken in that capacity. Moreover, adequate legal
representation often involves substantial expenses during the course of the proceeding and many
individuals are willing to serve as directors only if they have the assurance that the corporation
will advance these expenses. Accordingly, many corporations enter into contractual obligations
(e.g. by a provision in the articles of incorporation or bylaws or by individual agreements) to
advance expenses for directors. See Section 858(a).

A single undertaking by the director pursuant to Section 853(a) may cover all funds
advanced from time to time in connection with a proceeding. The theory underlying Section
853(b) is that wealthy directors should not be favored over directors whose financial resources
are modest. The undertaking must be made by the director and not by a third party. If the director
or the nonprofit corporation wishes some third party to be responsible for the director’s
obligation in this regard, either is free to make those arrangements separately with the third
party.

If advancement is not obligatory, the standards of section 830 should, in general, govern
the decision of directors acting on a request for advancement. In making such a decision, the
directors may consider any matters that they deem appropriate and may condition the advance of
expenses on compliance with any requirements that they believe are appropriate, including, for
example, an affirmation of a requesting director’s good faith belief that the director is entitled to
indemnification under section 851.

A nonprofit corporation may obligate itself pursuant to Section 858(a) to advance
expenses under Section 853 by means of a provision set forth in the articles of incorporation or
bylaws, by action of its members or board of directors, or by an agreement. Unless provided
otherwise, Section 858(a) deems a general obligatory provision requiring indemnification to the
fullest extent permitted by law to include advancement of expenses to the fullest extent permitted
by law, even if not specifically mentioned, subject to providing the required repayment
undertaking. No other procedures are required or contemplated, although obligatory
arrangements may include notice and any other requirements that the directors believe are
appropriate.

If advancement is not obligatory, the decision to advance expenses is required to be made
only one time with respect to each proceeding rather than each time a request for payment of
expenses is received by the nonprofit corporation. The directors are, however, free to reconsider
the decision at any time, (e.g., upon a change in the financial ability of the corporation to pay the
amounts in question). The decision as to the reasonableness of any expenses may be made by
any officer or agent of the corporation duly authorized to do so.

The procedures set forth in Section 853(c) for authorizing an advancement of expenses
parallel the procedures set forth in Section 855(b) for selecting the person or persons to make the
determination that indemnification is permissible. If the advancement of expenses is not
authorized by the members under Section 853(c)(2), the applicable procedure specified in
Section 853(c)(1) must be used.
Under Section 853(c)(1)(ii), which is available only if Section 853(c)(1)(i) is not available, the action of the board of directors must be taken in accordance with Sections 820 or 821, as the case may be, and directors who are not disinterested directors may participate in the vote. Allowing directors who at the time are not disinterested directors to participate in the authorization decision, if there is no or only one disinterested director, is based on the concept that if, there are not at least two disinterested directors, then it is preferable to return the power to make the decision to the full board (even though it includes non-disinterested directors) than to leave it to one disinterested director.

Illustration 1: The board consists of 15 directors, 4 of whom are interested. Of the 11 disinterested directors, 9 are present at the meeting at which the authorization is to be made (or the committee is to be appointed).

Under Section 853(c)(1)(i), a quorum is present and at least 6 of the 9 disinterested directors present at the board meeting must authorize any advancement of expenses because 6 is an absolute majority of the 11 disinterested directors. Alternatively, 6 of the 9 disinterested directors present at the board meeting may appoint a committee of 2 of the disinterested directors to decide whether to authorize the advance. Action by the committee would require the vote of a majority of committee.

Illustration 2: The board consists of 15 directors, only one of whom is a disinterested director.

Section 853(c)(1)(i) is not available because the number of disinterested directors, one, is less than two. Accordingly, the decision must be made by the board under Section 853(c)(1)(ii) (or, as is always permitted, by the members under Section 853(c)(2)).

The fact that there has been an advancement of expenses does not determine whether a director is entitled to indemnification. A proceeding often will terminate without a judicial or other determination as to whether the director’s conduct met the applicable standard of conduct in Section 851. Nevertheless, the board of directors should make, or cause to be made, an affirmative determination of entitlement to indemnification at the conclusion of the proceeding. This decision should be made in accordance with the procedures set forth in Section 855.

Judicial enforcement of rights granted by or pursuant to Section 853 is specifically contemplated by Section 854.

§ 854. COURT-ORDERED INDEMNIFICATION AND ADVANCEMENT OF EXPENSES

(a) A director who is a party to a proceeding because he or she is or was a director may apply for indemnification or an advancement of expenses to the court conducting the proceeding or to another court of competent jurisdiction. After receipt of an application and after giving any notice it considers necessary, the court shall:
(1) order indemnification if the court determines that the director is entitled to mandatory indemnification under Section 852 (mandatory indemnification);

(2) order indemnification or advancement of expenses if the court determines that the director is entitled to indemnification or advancement of expenses pursuant to a provision authorized by Section 858(a) (variation of indemnification); or

(3) order indemnification or advancement of expenses if the court determines, in view of all the relevant circumstances, that it is fair and reasonable:

(a) to indemnify the director, or

(b) to advance expenses to the director, even if, in the case of clause (1) or (2), he or she has not met the relevant standard of conduct set forth in Section 851(a) (permissible indemnification), failed to comply with Section 853 (advancement of expenses) or was adjudged liable in a proceeding referred to in Section 851(d)(1) or (d)(2), but if the director was adjudged so liable indemnification shall be limited to expenses incurred in connection with the proceeding.

(b) If the court determines that the director is entitled to indemnification under subsection (a)(1) or to indemnification or advancement of expenses under subsection (a)(2), it shall also order the nonprofit corporation to pay the director’s expenses incurred in connection with obtaining court-ordered indemnification or advancement of expenses. If the court determines that the director is entitled to indemnification or advancement of expenses under subsection (a)(3), it may also order the corporation to pay the director’s expenses to obtain court-ordered indemnification or advancement of expenses.


CROSS-REFERENCES

Advancement of expenses, § 853.
“Corporation” defined, § 850.
“Director” defined, § 850.
“Expenses” defined, § 102.
Limits on indemnification and advancement of expenses, § 858(c).
Mandatory indemnification, § 852.
Obligatory indemnification, § 858(a).
“Party” defined, § 850.
Permissible indemnification, § 851.
“Proceeding” defined, §§ 102 and 850.

OFFICIAL COMMENT
In determining whether indemnification or advancement of expenses would be “fair and reasonable” under Section 854(a)(3), a court should give appropriate deference to an informed decision of the board of directors or committee made in good faith and based upon full information. Ordinarily, a court should not determine that it is “fair and reasonable” to order indemnification or expense advance where the director has not met conditions and procedures to which the director agreed.

A director seeking court-ordered indemnification or advancement of expenses under Section 854(a)(3) must show that there are facts peculiar to the director’s situation that make it fair and reasonable to both the nonprofit corporation and to the director to override an intra-corporate declination or any otherwise applicable statutory prohibition against indemnification, e.g., Sections 851(a) or (d).

Apart from the provisions of Section 854(a)(3), there are no statutory outer limits on the court’s power to order indemnification under that subsection. In an appropriate case, a court may wish to refer to the provisions of Section 202(b)(8) establishing the outer limits of a liability-limiting provision in the articles of incorporation. It would be unusual for a court to provide indemnification going beyond the limits of Section 202(b)(8), but the court is permitted to do so.

Among the factors a court may want to consider under Section 854(a)(3) are the gravity of the offense, the financial impact upon the nonprofit corporation, or, in the case of an advancement of expenses, the inability of the director to finance his defense. A court may want to give special attention to certain other issues. For example, has the corporation joined in the application to the court for indemnification or an advancement of expenses? This factor may be particularly important where under Section 851(d) indemnification is not permitted for an amount paid in settlement of a proceeding brought by or in the right of the corporation. Also, in a case where indemnification would have been available under Section 851(a)(2) if the corporation had adopted a provision authorized by Section 202(b)(8), was the decision to adopt such a provision presented to and rejected by the members; and, if not, would exculpation of the director’s conduct have resulted under a Section 202(b)(8) provision? Additionally, in connection with considering indemnification for expenses under Section 851(d)(2) in a proceeding in which a director was adjudged liable for receiving a financial benefit to which the director was not entitled, was the financial benefit insubstantial – particularly in relation to the other aspects of the transaction involved – and what was the degree of the director’s involvement in the transaction and the corporate decision to participate?

Under Section 854(b), if a director successfully sues to enforce the right to indemnification under Section 854(a)(1) or to indemnification or advancement of expenses under Section 854(a)(2), the court is required to order the nonprofit corporation to pay the director’s expenses in the enforcement proceeding. However, if a director successfully sues for indemnification or expense advancement under Section 854(a)(3), the court may (but is not required to) order the corporation to pay those expenses. The basis for the distinction is that the corporation breached its obligation in the first two cases but not in the third.

Application for indemnification under Section 854 may be made either to the court in which the proceeding was heard or to another court of appropriate jurisdiction. For example, a
defendant in a criminal proceeding who has been convicted but believes that indemnification would be proper could apply either to the court which heard the criminal proceeding or bring an action against the nonprofit corporation in another forum.

A decision by the board of directors not to oppose a request for indemnification is governed by the general standards of conduct of Section 830. Even if the nonprofit corporation does not oppose the request, the court must satisfy itself that the person seeking indemnification is entitled to or otherwise deserving of receiving it under Section 854.

As provided in Section 858(d), a nonprofit corporation may limit the rights of a director under Section 854 by a provision in the articles of incorporation. In the absence of such a provision, the court has general power to exercise the authority granted under this section.

§ 855. DETERMINATION AND AUTHORIZATION OF INDEMNIFICATION

(a) A nonprofit corporation may not indemnify a director under Section 851 (permissible indemnification) unless authorized for a specific proceeding after a determination has been made that indemnification is permissible because the director has met the relevant standard of conduct set forth in Section 851.

(b) The determination shall be made:

(1) if there are two or more disinterested directors, by the board of directors by a majority vote of all the disinterested directors (a majority of whom shall constitute for this purpose a quorum), or by a majority of the members of a committee of two or more disinterested directors appointed by such a vote;

(2) by special legal counsel:

(i) selected in the manner prescribed in subsection (b)(1); or

(ii) if there are fewer than two disinterested directors, selected by the board of directors (in which selection directors who are not disinterested directors may participate); or

(3) by the members.

(c) Authorization of indemnification shall be made in the same manner as the determination that indemnification is permissible, except that if there are fewer than two disinterested directors or if the determination is made by special legal counsel, authorization of indemnification shall be made by those entitled to select special legal counsel under subsection (b)(2)(ii).

CROSS-REFERENCES

Advancement of expenses, § 853.
Committees of the board, § 825.
“Corporation” defined, § 850.
“Director” defined, § 850.
“Disinterested director” defined, § 850.
“Party” defined, § 850.
“Proceeding” defined, §§ 102 and 850.
Quorum of directors, § 824.
Standard for indemnification, § 851.

OFFICIAL COMMENT

Section 855 distinguishes between a “determination” that indemnification is permissible and an “authorization” of indemnification. A “determination” involves a decision by individuals or groups described in Section 855(b) whether, under the circumstances, the person seeking indemnification has met the relevant standard of conduct under Section 851 and is therefore eligible for indemnification. After a favorable “determination” has been made, the nonprofit corporation must decide whether to “authorize” indemnification except to the extent that an obligatory provision under Section 858(a) is applicable. This decision includes a review of the reasonableness of the expenses, the financial ability of the nonprofit corporation to make the payment, and the judgment whether limited financial resources should be devoted to this or some other use by the corporation.

Although special legal counsel may make the “determination” of eligibility for indemnification, counsel may not “authorize” the indemnification. A pre-existing obligation under Section 858(a) to indemnify if the director is eligible for indemnification dispenses with the second-step decision to authorize indemnification.

Section 855(b) establishes procedures for selecting the person or persons who will make the determination of permissibility of indemnification. The committee of disinterested directors referred to in Section 855(b)(1) may include a committee to which has been delegated the power to determine whether to indemnify a director, so long as the appointment and composition of the committee members comply with Section 855(b)(1). In selecting special legal counsel under Section 855(b)(2), directors who are parties to the proceeding may participate in the decision if there are insufficient disinterested directors to satisfy Section 855(b)(1). Directors who are not eligible to act as disinterested directors may also participate in the decision to “authorize” indemnification on the basis of a favorable “determination” if necessary to permit action by the board. The authorization of indemnification is the decision that results in payment of any amounts to be indemnified. This limited participation of interested directors in the authorization decision is justified by the principle of necessity.
Under Section 855(b)(1), the vote required when the disinterested directors act as a group is an absolute majority of their number. A majority of the disinterested directors constitutes a quorum for board action for this purpose.

If there are not at least two disinterested directors, then the determination of entitlement to indemnification must be made by special legal counsel or by the members.

The phrase “special legal counsel” is not defined in the act, and it is important that the process be sufficiently flexible to permit selectin of counsel in light of the particular circumstances. In many instances, however, it may be important that the “special legal counsel” be counsel having no prior professional relationship with those seeking indemnification, be retained for the specific purpose, and not be or have been either inside counsel or regular outside counsel to the nonprofit corporation. Among other factors that may be considered are whether “special legal counsel” has any familial, financial or other relationship with any of those seeking indemnification that would, in the circumstances, reasonably be expected to exert an influence on counsel in making the determination.

Section 855 is subject to Section 858(a), which authorizes and arrangement obligating the nonprofit corporation in advance to provide indemnification or to advance expenses. Although such an arrangement may effectively provide an authorization of indemnification, the determination requirements of Sections 855(a) and (b) must still be satisfied.

§ 856. INDEMNIFICATION OF OFFICERS

(a) A nonprofit corporation may indemnify and advance expenses under this [Subchapter] to an officer who is a party to a proceeding because he or she is an officer:

(1) to the same extent as a director; and

(2) if he or she is an officer but not a director, to such further extent as may be provided by the articles of incorporation, the bylaws, an action of the board of directors or a contract approved by the board of directors or members except for:

(i) liability in connection with a proceeding by or in the right of the corporation other than for expenses incurred in connection with the proceeding, or

(ii) liability arising out of conduct that constitutes:

(A) receipt by the officer of a financial benefit to he or she is not entitled,

(B) an intentional infliction of harm on the corporation or the members, or

(C) an intentional violation of criminal law.
Subsection (a)(2) shall apply to an officer who is also a director if he or she is made a party to the proceeding based on an act or omission solely as an officer.

An officer of a nonprofit corporation who is not a director is entitled to mandatory indemnification under Section 852 (mandatory indemnification), and may apply to a court under Section 854 (court-ordered indemnification and advancement of expenses) for indemnification or an advancement of expenses, in each case to the same extent to which a director may be entitled to indemnification or advancement of expenses under those sections.


CROSS-REFERENCES

Advancement of expenses, § 853.
“Corporation” defined, § 850.
“Director” defined, § 850.
“Expenses” defined, § 102.
Indemnification of employees and agents, § 858.
“Liability” defined, § 850.
Limits on rights to indemnification and advancement of expenses, § 858.
Obligatory indemnification, §§ 202(b)(8) and 858(a).
“Officer” defined, § 850.
Officer standards of conduct, § 842.
“Party” defined, § 850.
“Proceeding” defined, §§ 102 and 850(8).
Volunteers, indemnification of and advance of expenses for, § 858(f).

OFFICIAL COMMENT

in general

Section 856 correlates the general legal principles relating to the indemnification of officers of the nonprofit corporation with the limitations on indemnification in Subchapter 8E. This correlation may be summarized in general terms as follows.

An officer of a corporation who is not a director may be indemnified by the nonprofit corporation on a discretionary basis to the same extent as though the individual were a director; and, in addition, may have additional indemnification rights apart from Subchapter 8E, but subject to the limits set forth in Section 856(a)(2) the outer limits of such rights are specified. See Section 856(a)(2) and (c).

An officer who is also a director is entitled to the indemnification rights of a director; and, if the conduct that is the subject of the proceeding was solely in that individual’s
capacity as an officer, also to any of the rights of an officer who is not a director. See the
preceeding paragraph.

(3) An officer who is not a director has the right of mandatory indemnification
granted to directors under Section 852 and the right to apply for court-ordered indemnification
under Section 854. See Section 856(c).

Section 856 does not deal with indemnification of employees and agents because the
corns of self-dealing that arise when directors provide for their own indemnification and
advance of expenses (and sometimes for senior executive officers) are not present when
directors (or officers) provide for indemnification and expense advance for employees and agents
who are not directors or officers.

Subchapter 8E is silent with respect to employees, agents and volunteers, Section 858(e)
specifically states that Subchapter 8E does not limit the nonprofit corporation’s power to
indemnify and advance expenses to employee, agents, and volunteers. Employees, agents, and
volunteers may be indemnified using broad grants of powers to corporations under Section 302,
including powers to make contracts, appoint, and fix the compensation of employees and agents,
and to make payments furthering the activities and affairs of the corporation. Many corporations
provide for the exercise of these powers in the same provisions in the articles, bylaws or
otherwise in which they provide for advancement of expenses and indemnification for directors
and officers.

Indemnification also may be provided to protect employees or agents from liabilities
incurred while serving at a nonprofit corporation’s request as a director, officer, partner, trustee,
or agent of another commercial, charitable, or nonprofit venture.

Although employees and agents are not covered by Subchapter 8E, the principles and
procedures set forth in the subchapter for indemnification and advancement of expenses for
directors and officers may be helpful to counsel and courts in dealing with indemnification and
expense advance for employees and agents.

Careful consideration should be given to extending mandatory maximum indemnification
and expense advance to employees and agents. The same considerations that may favor
mandatory maximum indemnification for directors and officers — e.g., encouraging qualified
individuals to serve — may not be present in the cases of employees and agents. Many nonprofit
corporations may prefer to retain the discretion to decide, on a case-by-case basis, whether to
indemnify and advance expenses to employees, agents, and volunteers (and perhaps even
officers, especially nonexecutive officers) rather than binding themselves in advance to do so.

2. Officers Who Are Not Directors

Although Section 856 does not prescribe the standards governing the rights of officers to
indemnification, Section 856(a) does set outer limits beyond which the nonprofit corporation
may not indemnify. These limits for officers (see Section 856(a)(2)) are substantially the same as
the outer limits on the corporation’s power to indemnify directors. Since officers are held to
substantially the same standards of conduct as directors (see Section 842), there does not appear to be any reasoned basis for granting officers greater indemnification rights as a substantive matter. Procedurally, however, there is an important difference. To permit greater flexibility, officers may be indemnified (within the above-mentioned limits) with respect to conduct that does not meet the standards set by Section 851(a)(1) simply by authorization of the board of directors, whereas directors’ indemnification can reach beyond those standards, as contemplated by Section 851(a)(2), only with a provision included in the articles pursuant to Section 202(b)(8). This procedural difference reflects the reduced risk of self-dealing as to officers.

The broad authority in Section 856(a)(2) to grant indemnification may be limited by appropriate provisions in the articles of incorporation. See Section 858(c).

3. Officers Who Are Also Directors

Section 856(b) provides, in effect, that an officer of the nonprofit corporation who is also a director is subject to the same standards of indemnification as other directors and cannot take advantage of the provisions of Section 856(a) unless the act or omission that is the subject of the proceeding was committed solely in the capacity as officer. Thus, a vice president for development who is also a director and whose actions failed to meet Section 851(a) standards could be indemnified if the officer’s conduct was within the outer limits of Section 856(a)(2) and involved only the individual’s officer capacity.

This more flexible approach for situations where the individual is not acting as a director seems appropriate as a matter of fairness. There are many instances where officers, who also serve as directors, assume responsibilities and take actions in their non-director capacities for which indemnification may be appropriate.

For a director-officer to be indemnified under Section 851 for conduct in the individual’s capacity as a director when the individual has not satisfied the standards of Section 851(a), a provision in the articles of incorporation under Section 202(b)(8) is required. If such a provision is included in the articles, the standards for indemnification are those specified in the articles, subject to the limitations in Section 202(b)(8). For a director-officer to be indemnified for conduct solely in the capacity as an officer, even though the director-officer has not satisfied the standards of Section 856(a), only a bylaw or action by the board authorizing such indemnification is required, rather than a provision in the articles. If such a bylaw or action applies, the standards for indemnification are those specified in Section 856(a)(2). However, when a director-officer seeks indemnification or expense advance under Section 856(b) and Section 856(a)(2) on the basis of having acted solely in the capacity as an officer, indemnification or expense advance must be approved through the same procedures as set forth in Sections 855 or 853(c), as the case may be, for approval of indemnification or expense advance for a director when acting in the capacity of a director.

§ 857. INSURANCE
A nonprofit corporation may purchase and maintain insurance on behalf of an individual who is a director or officer of the corporation, or who, while a director or officer of the corporation, serves at the corporation’s request as a director, officer, partner, trustee, employee, or agent of another domestic or foreign corporation, or a joint venture, trust, employee benefit plan, or other entity, against liability asserted against or incurred by the individual in that capacity or arising from the individual’s status as a director or officer, regardless of whether the corporation would have power to indemnify or advance expenses to the individual against the same liability under this [Subchapter].


CROSS-REFERENCES

“Corporation” defined, § 850.
“Director” defined, § 850.
Employees, agents, and volunteers, § 858(e).
“Expenses” defined, § 102.
“Liability” defined, § 850.
“Officer” defined, § 850.
“Official capacity” defined, § 850.
Standard for indemnification, § 851.

OFFICIAL COMMENT

In authorizing a nonprofit corporation to purchase and maintain insurance on behalf of directors and officers, Section 857 sets no limits on the type of insurance which a corporation may maintain or the type of persons who are covered. Insurance is not limited to claims against which a corporation is entitled to indemnify under this subchapter. Such insurance can provide protection to directors and officers in addition to the rights of indemnification created by or pursuant to Subchapter 8E (as well as typically protecting the individual insureds against the corporation’s failure to pay indemnification required or permitted by this subchapter) and can also provide a source of reimbursement for a corporation that indemnifies its directors and others for conduct covered by the insurance.

Although Section 857 does not include employees and agents for the reasons stated in the Official Comment to Section 856, the nonprofit corporation has the power under Section 302 to purchase and maintain insurance on their behalf. This power is confirmed in Section 858(f).

§ 858. VARIATION OF INDEMNIFICATION

(a) A nonprofit corporation may, by a provision in its articles of incorporation or bylaws or in an action taken or a contract approved by the board of directors or members, obligate itself in advance of the act or omission giving rise to a proceeding to provide indemnification in accordance with Section 851 (permissible indemnification) or advance funds
to pay for or reimburse expenses in accordance with Section 853 (advancement of expenses). Any such obligatory provision shall be deemed to satisfy the requirements for authorization referred to in Sections 853(c) and 855(c) (determination and authorization of indemnification). Any such provision that obligates the corporation to provide indemnification to the fullest extent permitted by law shall be deemed to obligate the corporation to advance funds to pay for or reimburse expenses in accordance with Section 853 to the fullest extent permitted by law, unless the provision expressly provides otherwise.

(b) A right of indemnification or advancement of expenses created by this [Subchapter] or under Section 858(a) and in effect at the time of an act or omission is not eliminated or impaired with respect to the act or omission by an amendment of the articles of incorporation or bylaws adopted, or action taken by the board of directors or members, after the occurrence of the act or omission, unless, in the case of a right created under Section 858(a), the provision creating such right and in effect at the time of the act or omission explicitly authorizes such elimination or impairment after the act or omission has occurred.

(c) Any provision pursuant to Subsection 858(a) does not obligate the nonprofit corporation to indemnify or advance expenses to a director of a predecessor of the corporation, pertaining to conduct with respect to the predecessor, unless otherwise expressly provided. Any provision for indemnification or advancement of expenses in the organic records, articles of incorporation, bylaws, or an action of the governors, board of directors, members or interest holders of a predecessor of the corporation in a fundamental transaction, or in a contract to which the predecessor is a party, existing at the time the fundamental transaction takes effect is governed by Section 1226(a)(4) (effect of merger).

(d) Subject to subsection (b), a nonprofit corporation may, by a provision in its articles of incorporation or bylaws, limit any of the rights to indemnification or advancement of expenses created by or pursuant to this [Subchapter].

(e) This [Subchapter] does not limit a nonprofit corporation’s power to pay or reimburse expenses incurred by a director or an officer in connection with appearing as a witness in a proceeding at a time when he or she is not a party.

(f) This [Subchapter] does not limit a nonprofit corporation’s power to indemnify, advance expenses to, or provide or maintain insurance on behalf of an employee, agent, or volunteer.


CROSS-REFERENCES

Advancement of expenses, § 853.
“Corporation” defined, § 850.
“Director” defined, § 850.
Effect of articles amendment, § 909.
Section 858(a) authorizes a nonprofit corporation to make obligatory the permissive provisions of Subchapter 8E in advance of the conduct giving rise to the request for indemnification or advancement of expenses. An obligatory provision satisfies the requirements for authorization in Sections 853(c) and 855(c), but the requirements for determination of eligibility for indemnification in Sections 853(a), 853(b), 855(a) and 855(b) must still be met.

If a nonprofit corporation provides for obligatory indemnification and not for obligatory advancement of expenses, the provision should be reviewed to ensure that it properly reflects the intent in view of the third sentence of Section 858(a). Also, a corporation should consider whether obligatory expense advance is intended for direct suits by the corporation as well as for derivative suits in the right of the corporation. In the former case, assuming compliance with Sections 853(a) and (b), the corporation could be required to fund the defense of a defendant director even where the board of directors has already concluded that the director has engaged in significant wrongdoing. See Official Comment to Section 853.

Although Section 858(d) permits a nonprofit corporation to limit the right of the corporation to indemnify or advance expenses by a provision in its articles of incorporation, as provided in Section 909(a), no such limitation will affect rights in existence when the provision becomes effective pursuant to Section 163.

Section 858(e) makes clear that Subchapter 8E deals only with actual or threatened defendants or respondents in a proceeding, and that expenses incurred by a director in connection with appearance as a witness may be indemnified without regard to the limitations of Subchapter E. Indeed, most of the standards described in Sections 851 and 854(a) by their own terms can have no meaningful application to a director whose only connection with a proceeding is that he has been called as a witness.

Subchapter 8E does not regulate the power of the nonprofit corporation to indemnify or advance expenses to employees and agents. That subject is governed by the law of agency and related principles and frequently by contractual arrangements between the corporation and the employee or agent. Section 858(f) makes clear that, although indemnification, advancement of expenses, and insurance for employees and agents are beyond the scope of Subchapter E, the elaboration in Subchapter E of standards and procedures for indemnification, expense advance, and insurance for directors and officers is not in any way intended to cast doubt on the power of the corporation to indemnify or advance expenses to or purchase and maintain insurance for employees and agents under Section 302 or otherwise.
[Subchapter] F
CONFLICTING INTEREST TRANSACTIONS

§ 860. Conflicting interest transactions; voidability.

§ 860. CONFLICTING INTEREST TRANSACTIONS; VOIDABILITY

(a) A contract or transaction between a nonprofit corporation and one or more of its members, directors, members of a designated body, or officers or between a nonprofit corporation and any other entity in which one or more of its directors, members of a designated body, or officers are directors or officers, hold a similar position, or have a financial interest, is not void or voidable solely for that reason, or solely because the member, director, member of a designated body, or officer is present at or participates in the meeting of the board of directors that authorizes the contract or transaction, or solely because his or their votes are counted for that purpose, if:

(1) the material facts as to the relationship or interest and as to the contract or transaction are disclosed or are known to the board of directors and the board in good faith authorizes the contract or transaction by the affirmative votes of a majority of the disinterested directors even though the disinterested directors are less than a quorum;

(2) the material facts as to the relationship or interest of the member, director, or officer and as to the contract or transaction are disclosed or are known to the members entitled to vote thereon, if any, and the contract or transaction is specifically approved in good faith by vote of those members; or

(3) the contract or transaction is fair as to the corporation as of the time it is authorized, approved, or ratified by the board of directors or the members.

(b) Common or interested directors may be counted in determining the presence of a quorum at a meeting of the board that authorizes a contract or transaction specified in subsection (a).

(c) This section is applicable except as otherwise restricted in the articles of incorporation or bylaws.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 8.60.

CROSS-REFERENCES

“Designated body” defined, § 102.
“Director” defined, § 102.
Directors’ liability for unlawful distributions, § 832.
“Entity” defined, § 102.
Section 860 applies to all contracts and transactions between a nonprofit corporation and one or more of its members, directors, members of a designated body, or officers, or between a corporation and any other entity in which one or more of its members, directors, members of a designated body, or officers hold a similar position or have a financial interest. A contract or transaction subject to this section may be permissible under this act yet be prohibited as an excess benefit transaction or otherwise under standards applicable to charitable corporations under the Internal Revenue Code.

Section 860, like Subchapter 8C regarding the standards of conduct of directors, rejects the trustee standard regarding interested transactions in favor of the corporate standard. The trustee standard prohibits any transaction between a trust and a trustee. That standard was considered overly-restrictive for nonprofit corporations. This section also rejects the concept that a director may not obtain any profit from a transaction involving that director’s corporation. If the requirements of Section 860 are met, a director can make a profit from a transaction involving the corporation, subject to other applicable provisions of law.

§ 870. Business opportunities.

(a) If a director or officer pursues or takes advantage of a business opportunity directly or indirectly through or on behalf of another person, that action may not be the subject of equitable relief, or give rise to an award of damages or other sanctions against the director, officer, or other person, in a proceeding by or in the right of the nonprofit corporation on the ground that the opportunity should have first been offered to the corporation, if:

(1) before the director, officer, or other person becomes legally obligated respecting the opportunity, the director or officer brings it to the attention of the corporation and either action by the members or the directors disclaiming the corporation’s interest in the opportunity is taken in compliance with the same procedures as are set forth in Section 860 (conflicting interest transactions; voidability), as if the decision being made concerned a conflicting interest transaction; or
(2) the duty to offer the corporation the business opportunity has been limited or eliminated pursuant to a provision of the articles of incorporation adopted in accordance with Section 202(b)(10) (articles of incorporation).

(b) In any proceeding seeking equitable relief or other remedies, based upon an alleged improper pursuit or taking advantage of a business opportunity by a director or officer, directly, or indirectly through or on behalf of another person, the fact that the director or officer did not employ the procedure described in subsection (a)(1) before pursuing or taking advantage of the opportunity shall not create an implication that the opportunity should have been first presented to the nonprofit corporation or alter the burden of proof otherwise applicable to establish that the director or officer breached a duty to the corporation in the circumstances.

(c) As used in this section, “director” includes a member of a designated body.


CROSS-REFERENCES
Conflicting interest transactions; voidability, § 860.
Standards of conduct for directors, § 830.
Standards of conduct for officers, § 842.
Standards of liability for directors, § 831.

OFFICIAL COMMENT
Section 870(a) provides a safe harbor for a director or officer weighing possible involvement with a prospective business opportunity that might constitute a “corporate opportunity.” The phrase “directly, or indirectly through or on behalf of another person” recognizes the need to cover transactions pursued or effectuated either directly by the director or officer or indirectly through or on behalf of another person.

By action of the board of directors or members of the nonprofit corporation under Section 870(a), the director or officer can obtain a disclaimer of the corporation’s interest in the matter before proceeding with such involvement. In the alternative, the corporation may, among other things, (i) decline to disclaim its interest, (ii) delay a decision respecting granting a disclaimer pending receipt from the director or officer of additional information (or for any other reason), or (iii) attach conditions to the disclaimer it grants under Section 870(a).

The safe harbor provided under section 870(a)(1) may be utilized only for a specific business opportunity. A broader advance safe harbor for any, or one or more classes or categories of, business opportunities must meet the requirements of section 202(b)(10). Section 870(a)(2) confirms that if the duty of an officer or director to present an opportunity has been limited or eliminated by a provision in the articles of incorporation under section 202(b)(10) a safe harbor exists in connection with the pursuit or taking of the opportunity. The common law doctrine of “corporate opportunity” has long been recognized as a part of the director’s duty of
loyalty; and, under court decisions, extends to officers. See Section 842(a) and its Official
Comment. The doctrine recognizes that the nonprofit corporation has a right prior to that of its
directors or officers to act on certain business opportunities that come to the attention of the
directors or officers. In such situations, a director or officer who acts on the opportunity for the
benefit of the director or officer or another person without having first presented it to the
corporation can be held to have “usurped” or “intercepted” a right of the corporation. A
defendant director or officer who is found by a court to have violated the duty of loyalty in this
regard, as well as related or other persons involved in the transaction, may be subject to damages
or possible equitable remedies, including injunction, disgorgement or the imposition of a
constructive trust in favor of the corporation. Although the doctrine’s concept is easily described,
whether it will be found to apply in a given case depends on the facts and circumstances of the
particular situation and is thus frequently unpredictable.

In recognition that the nonprofit corporation need not pursue every business opportunity
of which it becomes aware, an opportunity coming within the doctrine’s criteria that has been
properly presented to and declined by the corporation may then be pursued or taken by the
presenting director or officer without breach of the duty of loyalty.

The fact-intensive nature of the corporate opportunity doctrine resists statutory definition.
Instead, Subchapter G employs the broader notion of “business opportunity” that encompasses
any opportunity, without regard to whether it would come within the judicial definition of a
“corporate opportunity” as it may have been developed by courts in a jurisdiction. When
properly employed, Subchapter G provides a safe-harbor mechanism enabling a director or
officer to pursue an opportunity directly, or indirectly through or on behalf of another person,
free of possible challenge claiming conflict with the director’s or officer’s duty on the ground
that the opportunity should first have been offered to the corporation.

1. Section 870(a)(1).

Section 870(a)(1) describes the safe harbor available to a director or officer who elects to
subject a business opportunity, regardless of whether the opportunity would be classified as a
“corporate opportunity,” to the disclosure and approval procedures set forth in that section The
safe harbor provided is as broad as that provided for a director’s conflicting interest transaction
in Section 860. If the director or officer makes the prescribed disclosure of the facts specified
and the nonprofit corporation’s interest in the opportunity is disclaimed by director action or
member action, the director or officer has foreclosed any claimed breach of the duty of loyalty
and may not be subject to equitable relief, damages or other sanctions if the director or officer
thereafter pursues or takes the opportunity for that individual’s own account or through or for the
benefit of another person.

The safe harbor concept contemplates that the nonprofit corporation’s decision maker
will have full freedom of action in deciding whether the corporation should take over a proffered
opportunity or disclaim the corporation’s interest in it. If the director or officer could seek
ratification after the legal obligation respecting the opportunity arises, the option of taking over
the opportunity would, in most cases, be foreclosed to the corporation. The safe harbor’s benefit
is available only when the corporation can entertain the opportunity in a fully objective way.
2. Section 870(b).

The concept of “business opportunity” under Section 870 is not defined but is intended to be broader than what might be regarded as an actionable “corporate opportunity.” This approach reflects the fact-intensive nature of the corporate opportunity doctrine, with the result that a director or officer may be inclined to seek safe harbor protection under Section 870 before pursuing an opportunity that may or may not be a “corporate opportunity.” Likewise, a director or officer may conclude that a business opportunity is not a “corporate opportunity” under applicable law and choose to pursue it without seeking a disclaimer by the nonprofit corporation under Section 870(a)(1). Accordingly, Section 870(b) provides that a decision not to seek the safe harbor offered by Section 870(a)(1) neither creates a negative implication nor alters the burden of proof in any subsequent proceeding seeking damages or equitable relief based upon an alleged improper taking of a “corporate opportunity.”

3. Section 870(c).

Section 870(c) extends the procedures and protections of this section to members of a designated body.

[Chapter] 9

AMENDMENT OF ARTICLES OF INCORPORATION AND BYLAWS

Subchapter

A. Amendment of Articles of Incorporation

B. Amendment of Bylaws

C. Special Rights

[Subchapter] A

AMENDMENT OF ARTICLES OF INCORPORATION

§ 901. Authority to amend.

§ 902. Amendment before issuance of memberships.

§ 903. Amendment of articles of membership corporation.

§ 904. Voting on amendments by voting groups.

§ 905. Amendment of articles of nonmembership corporation.

§ 906. Articles of amendment.

§ 907. Restated articles of incorporation.

§ 908. Amendment pursuant to reorganization.

§ 909. Effect of amendment to articles.

§ 901. AUTHORITY TO AMEND
(a) A nonprofit corporation may amend its articles of incorporation at any time to add
or change a provision that is required or permitted in the articles as of the effective date of the
amendment or to delete a provision that is not required to be contained in the articles.

(b) Except as provided in the articles of incorporation, a member of a nonprofit
corporation does not have a vested property right resulting from any provision in the articles,
including provisions relating to management, control, purpose, or duration of the corporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.01. Cf. Model Business Corporation Act (2016 Revision), § 10.01.

CROSS-REFERENCES

Amendment:
- before issuance of memberships, § 902.
- membership corporation, § 903.
- nonmembership corporation, § 905.
- pursuant to court ordered reorganization, § 908.

Articles of incorporation, § 202.
Duration of corporation existence, § 302.
Effective date of amendment, § 163.
Powers of corporation, § 302.
Restatement of articles, § 907.
Voting by voting groups, §§ 724, 725, and 904.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 901(a) authorizes a nonprofit corporation to amend its articles of incorporation by
adding a new provision, modifying an existing provision, or deleting a provision in its entirety.
The sole test for the validity of an amendment is whether the provision could lawfully have been
included in (or in the case of a deletion, omitted from) the articles as of the effective date of the
amendment.

Section 903 requires most amendments to be approved by a majority of the votes cast on
the proposed amendment at a meeting at which a quorum consisting of at least a majority of the
votes entitled to be cast is present. This requirement is supplemented by Section 904, which
governs voting by voting groups on amendments that directly affect a single class of members,
and by Section 726, which governs amendments that change the voting requirements for future
amendments.

A provision in the articles of incorporation is subject to amendment under Section 901(a)
even though the provision is described, referred to, or stated in a membership certificate or other
document issued by the nonprofit corporation that reflects provisions of the articles.

Section 901(a) does not concern obligations of a nonprofit corporation to its members
based upon contracts independent of the articles of incorporation. An amendment permitted by
this section may constitute a breach of such a contract or of a contract between the members
themselves. A member with contractual rights (or who otherwise is concerned about possible
onerous amendments) may obtain complete protection against these amendments by establishing
procedures in the articles or bylaws that limit the power of amendment without the member’s
consent. In appropriate cases, a member may be able to enjoin an amendment that constitutes a
breach of a contract.

Section 901(b) expressly rejects the concept that an otherwise lawful amendment to the
articles of incorporation might be restricted or invalidated because it modified particular rights
conferred on members by the original or prior version of the articles. Similarly, under Section
107, nonprofit corporations and their members are subject to subsequent amendments of the act.

§ 902. AMENDMENT BEFORE ISSUANCE OF MEMBERSHIPS

If a membership corporation has not yet issued memberships, the board of directors, or
the incorporators if it has no board, may adopt one or more amendments to the articles of
incorporation.

Source Note: Model Nonprofit Corporation Act, 3rd Ed.
(2008), § 10.02. Cf. Model Business Corporation Act
(2016 Revision), § 10.02.

CROSS-REFERENCES

Articles of amendment, § 906.
Effective date of amendment, § 163.
Incorporators, § 201.
“Membership corporation” defined, § 102.
Organization of corporation, § 205.
Restated articles of incorporation, § 907.

OFFICIAL COMMENT

Section 902 provides that, before any memberships are issued, amendments may be made
by the persons empowered to complete the organization of a membership corporation.

The authority of the board of directors under this Section 902 to amend the articles of
incorporation may be vested in a designated body by the articles or bylaws. See Section 812.

§ 903. AMENDMENT OF ARTICLES OF MEMBERSHIP CORPORATION

(a) An amendment to the articles of incorporation of a membership corporation must
be adopted in the following manner:
(1) Except as provided in Section 903(a)(3), the proposed amendment must first be adopted by the board of directors. The board of directors may set conditions for the approval of the amendment by the members or the effectiveness of the amendment.

(2) Except as provided in Sections 905 (amendment of articles of nonmembership corporation), 907 (restated articles of incorporation), and 908 (amendment pursuant to reorganization), the amendment must then be approved by the members entitled to vote on the amendment. In submitting the proposed amendment to the members for approval, the board of directors must recommend that the members approve the amendment, unless the board of directors makes a determination that because of conflicts of interest or other special circumstances it should not make such a recommendation, in which case the board of directors must inform the members of the basis for that determination.

(3) Except as provided in the articles, an amendment may be proposed by 10% or more of the members entitled to vote on the amendment or by such greater or lesser number of members as is specified in the articles. Section 903 (a)(1) does not apply to an amendment proposed by the members under this Section 903(a)(3).

(4) If the amendment is required to be approved by the members, and the approval is to be given at a meeting, the corporation must notify each member entitled to vote on the amendment of the meeting of members at which the amendment is to be submitted for approval. The notice must state that the purpose, or one of the purposes, of the meeting is to consider the amendment and contain or be accompanied by a copy of the amendment.

(5) Unless the articles or bylaws, or the board of directors acting pursuant to Section 903(a)(1), requires a greater vote or a greater number of members to be present, the approval of an amendment requires the approval of the members at a meeting at which a quorum exists, and, if any class of members is entitled to vote as a separate group on the amendment, the approval of each such separate voting group at a meeting at which a quorum of the voting group exists.

(6) In addition to the adoption and approval of an amendment by the board of directors and members as required by this section, an amendment must also be approved by a designated body whose approval is required by the articles or bylaws.

(b) Unless the articles of incorporation provide otherwise, the board of directors of a membership corporation may adopt amendments to the corporation’s articles without approval of the members to:

(1) extend the duration of the corporation if it was incorporated at a time when limited duration was required by law;

(2) delete the names and addresses of the initial directors or members of a designated body;
(3) delete the name and address of the initial registered agent or registered office, if a statement of change is on file with the secretary of state;

(4) change the corporation name by substituting or deleting the word “corporation,” “incorporated,” “company,” “limited,” or the abbreviation “corp.,” “inc.,” “co.,” or “ltd.,” for a similar word or abbreviation in the name; or

(5) restate without change all of the then operative provisions of the articles.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.03. Cf. Model Business Corporation Act (2016 Revision), § 10.03.

CROSS-REFERENCES

Articles of amendment, § 906.
Designated body, § 812.
Director standards of conduct, § 830.
“Membership corporation” defined, § 102.
Notice, § 103.
Notice of members’ meeting, § 705.
Quorum at members’ meeting, § 724.
Restatement of articles of incorporation, § 907.
Supermajority quorum and voting requirements, § 726.
Voting by voting group, §§ 7.24, 7.25, and 904.
Voting entitlement of members generally, § 721.
“Voting group” defined, § 102.

OFFICIAL COMMENT

1. IN GENERAL

If a nonprofit corporation has issued memberships, Section 903 requires that a proposed amendment to the articles of incorporation first be adopted by the board of directors except as provided in Section 903(a)(3). Thereafter, the board must submit the amendment to the members for their approval, except as provided in Sections 905, 907, and 908.

The functions and powers of the board of directors under Section 903 may be vested in a designated body by the articles of incorporation or bylaws.

2. SUBMISSION TO THE MEMBERS

When submitting the amendment to the members for approval, the board of directors must make a recommendation to the members that the amendment be approved, unless the board makes a determination that because of conflicts of interest or other special circumstances it should make no recommendation. For example, the board may make such a determination when there is not a sufficient number of directors free of a conflicting interest to approve the
amendment or because the board is evenly divided as to the merits of an amendment but is able
to agree that members should be permitted to consider the amendment. If the board makes such a
determination, it must describe the conflict of interest or special circumstances, and
communicate the basis for the determination, when submitting the amendment to the members.

Section 903(a)(1) permits a board of directors to condition its submission of an
amendment on any basis. Among the conditions that a board might impose are that the
amendment will not be deemed approved unless it is approved by a specified vote of the
members, or by one or more specified classes of members, voting as a separate voting group, or
by a specified percentage of disinterested members. The board is not limited to conditions of
these types.

3. QUORUM AND VOTING

Section 903(a)(5) provides that approval of an amendment requires approval of the
members at a meeting at which a quorum consisting of at least a majority of the votes entitled to
be cast on the amendment exists, including, if any class of members is entitled to vote as a
separate group, at a meeting at which a similar quorum of the voting group exists. If a quorum
exists, then under Sections 724 and 725 the amendment will be approved if more votes are cast
in favor of the amendment than against it by the voting group or separate voting groups entitled
to vote on the plan.

If an amendment would affect the voting requirements on future amendments, it must be
approved by the vote required by Section 726.

4. APPROVAL BY BOARD OF DIRECTORS ALONE

The amendments described in Section 903(b) do not require approval by the members
because they are so routine and “housekeeping” in nature that they do not affect substantive
rights in any meaningful way.

§ 904. VOTING ON AMENDMENTS BY VOTING GROUPS

(a) Except as provided in the articles of incorporation or bylaws, if a nonprofit
corporation has more than one class of members, the members of each class are entitled to vote
as a separate voting group (if member voting is otherwise required by this [Act]) on a proposed
amendment to the articles of incorporation if the amendment would:

(1) effect an exchange or reclassification of all or part of the memberships of
the class into memberships of another class;

(2) effect an exchange or reclassification, or create the right of exchange, of
all or part of the memberships of another class into memberships of the class;
(3) change the rights, preferences, or limitations of all or part of the memberships of the class in a manner different than the amendment would affect another class;

(4) change the rights, preferences, or limitations of all or part of the memberships of the class by changing the rights, preferences, or limitations of another class;

(5) increase or decrease the number of memberships authorized for that class;

(6) increase the number of memberships authorized for another class; or

(7) authorize a new class of memberships.

(b) If a class of members will be divided into two or more classes by an amendment to the articles of incorporation, the amendment must be approved by a majority of the members of each class that will be created.

(c) If a proposed amendment would affect less than all of the members of a class in one or more of the ways described in subsection (a), the members so affected are entitled to vote as a separate voting group on the proposed amendment.


CROSS-REFERENCES

Classes of members, § 601.
Quorum for members’ meeting to amend articles, § 903(5).
Voting by voting groups generally, §§ 724 and 725.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 904(a) requires separate approval by voting groups for certain types of amendments to the articles of incorporation where the nonprofit corporation has more than one class of members. Members are entitled to vote as separate voting groups under Section 904(a) even though they are designated as nonvoting members in the articles of incorporation or bylaws, unless the articles or bylaws specifically deny them the right to vote on a proposed amendment that would otherwise give them the right to vote under this section.

Section 904(a) does not make the right to vote by separate voting group dependent on an evaluation of whether the amendment is detrimental to the class; if the amendment is one of those described, the class is automatically entitled to vote as a separate voting group on the amendment. The question whether an amendment is detrimental is often a question of judgment, and approval by the affected class is required irrespective of whether the board or other members believe it is beneficial or detrimental to the affected class.
Sections 724 and 725 set forth the mechanics of voting by multiple voting groups.

The functions and powers of the board of directors under this section may be vested by the articles of incorporation or bylaws in a designated body. See Section 812.

§ 905. AMENDMENT OF ARTICLES OF NONMEMBERSHIP CORPORATION

Except as otherwise provided in the articles of incorporation, the board of directors of a nonmembership corporation may adopt amendments to the corporation’s articles. An amendment adopted by the board under this section must also be approved:

(1) by a designated body whose approval is required by the articles or bylaws;

(2) if the amendment changes or deletes a provision regarding the appointment of a director by persons other than the board, by those persons as if they constituted a voting group; and

(3) if the amendment changes or deletes a provisions regarding the designation of a director, by the individual designated at the time as that director.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.05.

CROSS-REFERENCES

Action by board of directors, §§ 820 through 824.

Articles of amendment, § 906.

Duration of corporate existence, § 302.

Effective date of amendment, § 163.

Extrinsic facts, § 105.

Name of corporation, Subch. 2B.

“Nonmembership corporation” defined, § 102.

Registered office and agent, Subch. 2C.

Restatement of articles, § 907

OFFICIAL COMMENT

Section 905 only applies to nonmembership corporations. The procedures for amending the articles of incorporation of a membership corporation are found in Sections 902 through 904.

Amendments provided for in Section 905 may be included in restated articles of incorporation under Section 907 or in the various types of articles filed to effectuate fundamental transactions under Chapter 12.

The authority of the board of directors under Section 905 to amend the articles of incorporation may be vested in a designated body by the articles of incorporation or bylaws.
§ 906. ARTICLES OF AMENDMENT

(a) After an amendment to the articles of incorporation has been adopted and approved in the manner required by this [Act] and by the articles, the nonprofit corporation must deliver to the secretary of state, for filing, articles of amendment, which must set forth:

(1) the name of the corporation;

(2) the text of each amendment adopted;

(3) if the amendment provides for an exchange, reclassification, or cancellation of memberships, provisions for implementing the amendment if not contained in the amendment itself, (which may be made dependent upon facts objectively ascertainable outside the articles of amendment in accordance with Section 105 (extrinsic facts in filed record));

(4) the date of each amendment’s adoption; and

(5) if the amendment:

(i) was adopted by the incorporators, board of directors, or a designated body without member approval, a statement that the amendment was adopted by the incorporators, the board of directors, or a designated body, as the case may be, and that member approval was not required; or

(ii) required approval by the members, a statement that the amendment was duly approved by the members in the manner required by this [Act] and by the articles of incorporation and bylaws.

(b) Articles of amendment shall take effect on the effective date determined in accordance with Section 163 (effective time and date of filing).

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.06. Cf. Model Business Corporation Act (2016 Revision), § 10.06.

CROSS-REFERENCES

Amendment by:
board of directors, § 905.
incorporators or initial directors, § 902.
members, §§ 903 and 904.
Deliver” defined, § 102.
Effective date of amendment, § 163.
Extrinsic facts, § 105.
Filing fees, § 162.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 906(a)(3) requires the articles of amendment to contain a statement of the manner in which an exchange, reclassification, or cancellation of memberships is to be put into effect, if not set forth in the amendment itself. This requirement avoids any possible confusion that may arise as to how the amendment is to be put into effect and also permits the amendment itself to be limited to provisions of permanent applicability, with transitional provisions having no long-range effect appearing only in the articles of amendment.

§ 907. RESTATED ARTICLES OF INCORPORATION

(a) The board of directors of a nonprofit corporation may restate its articles of incorporation at any time, without approval by the members or any other person, to consolidate all amendments into a single document without substantive change.

(b) If restated articles of a membership corporation include one or more new amendments that require member approval, the amendments must be adopted and approved as provided in Sections 903 (amendment of articles of membership corporation) and 904 (voting on amendments by voting groups).

(c) A nonprofit corporation that restates its articles of incorporation must deliver to the secretary of state for filing articles of amendment under Section 906 (articles of amendment) which include a statement that the articles of amendment are a restatement that consolidates all amendments into a single record.

(d) Duly filed restated articles of incorporation supersede the original articles of incorporation and all amendments thereto.

(e) The secretary of state shall certify restated articles of incorporation as the articles of incorporation currently in effect.


CROSS-REFERENCES

Amendment of articles of incorporation:
before issuance of memberships, § 902.
by board of directors, § 905.
by board of directors and by members, § 903.
“Deliver” defined, § 102.
Effective date of restatement, § 163.
Filing fees, § 162.
Restated articles of incorporation permit articles of incorporation that have been amended over time, or are being concurrently amended, to be consolidated into a single document. A nonprofit corporation that is restating its articles may concurrently amend the articles, and include the new amendments in the restated articles. In such a case, the provisions of Chapter 9 that govern amendments of the articles would apply to the new amendments. If it is unclear whether a provision of a restatement of the articles might be deemed to be an amendment, rather than a consolidation, the prudent course for the corporation is to treat that provision as an amendment, and follow the procedures that apply to amendments under Chapter 9.

The authority of the board of directors under Section 907 to restate the articles of incorporation may be vested by the articles or bylaws under Section 812.

§ 908. AMENDMENT PURSUANT TO REORGANIZATION

(a) A nonprofit corporation’s articles of incorporation may be amended without action by the board of directors, a designated body, or the members to carry out a plan of reorganization ordered or decreed by a court of competent jurisdiction under the authority of a law of the United States.

(b) A person designated by the court to implement the plan of reorganization must deliver to the secretary of state for filing articles of amendment setting forth:

(1) the name of the corporation;
(2) the text of each amendment approved by the court;
(3) the date of the court’s order or decree approving the articles of amendment;
(4) the title of the reorganization proceeding in which the order or decree was entered; and
(5) a statement that the court had jurisdiction of the proceeding under federal statute.

(c) This section does not apply after entry of a final decree in the reorganization proceeding even though the court retains jurisdiction of the proceeding for limited purposes unrelated to consummation of the reorganization plan.
OFFICIAL COMMENT

Section 908 provides a simplified method of conforming corporate documents filed under state law with the federal statutes relating to corporate reorganization. If a federal court confirms a plan of reorganization that requires articles of amendment to be filed, those amendments may be prepared and filed by a person designated by the court and no approval is required from the members, the board of directors, or a designated body.

Section 908 applies only to amendments in articles of incorporation approved before the entry of a final decree in the reorganization.

§ 909.  EFFECT OF AMENDMENT TO ARTICLES

(a) Except as provided in Section 909(b) and (c), an amendment to the articles of incorporation does not affect a cause of action existing against or in favor of the nonprofit corporation, a proceeding to which the corporation is a party, or the existing rights of persons other than members of the corporation or persons referred to in the articles. An amendment changing a corporation’s name does not affect a proceeding brought by or against the corporation in its former name.

(b) Property held in trust by a nonprofit corporation or otherwise dedicated to a charitable purpose may not be diverted from its purpose by an amendment of its articles of incorporation unless the corporation obtains an appropriate order of [court] [the attorney general] to the extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the nondiversion of charitable assets.

(c) A person that is a member or otherwise affiliated with a charitable corporation may not receive a direct or indirect financial benefit in connection with an amendment of the articles of incorporation unless the person is itself a charitable corporation or an unincorporated entity with a charitable purpose. This subsection does not apply to the receipt of reasonable compensation for services rendered.

OFFICIAL COMMENT

Section 909(a) confirms that amendments to articles of incorporation of a nonprofit corporation do not interrupt the corporate existence and do not abate a proceeding by or against the corporation even though the amendment changes the name of the corporation.

Section 909(b) prevents the diversion of property held in trust by a nonprofit corporation or that is a charitable asset without appropriate review. Section 909(c) also prohibits the receipt of direct or indirect financial benefit by a member or person otherwise affiliated with a charitable corporation as a result of an amendment of the articles of incorporation. The only exception is if the member or person otherwise affiliated with a charitable corporation is itself a charitable corporation or an unincorporated entity with a charitable purpose.

[Subchapter] B

AMENDMENT OF BYLAWS

§ 920. Authority to amend.

§ 921. Amendment to quorum or voting requirement for board of directors or designated body.

§ 922. Bylaw amendments requiring member approval.

§ 923. Effect of amendment to bylaws.

§ 920. AUTHORITY TO AMEND

(a) The members of a membership corporation may amend or repeal the corporation’s bylaws except as provided in the articles of incorporation or bylaws.

(b) The board of directors of a membership corporation or nonmembership corporation may amend or repeal the corporation’s bylaws, except as provided in the articles of incorporation or bylaws or Sections 921 (bylaw increasing quorum or voting requirement for board of directors or designated body) or 922 (bylaw amendments requiring member approval).

(c) A member of a nonprofit corporation does not have a vested property right resulting from any provision of the bylaws, including provisions relating to management, control, or purpose of the corporation except as provided in the articles of incorporation or bylaws.

CROSS-REFERENCES

Action by:

board of directors, §§ 820 through 824.

members, §§ 724 and 725.

“Membership corporation” defined, § 102.

“Nonmembership corporation” defined, § 102.

Supermajority requirements for directors or designated body, § 921.

OFFICIAL COMMENT

The power to amend or repeal bylaws may be exercised by either the board of directors or the members in a membership corporation except as provided in the articles of incorporation, the bylaws, or Sections 921 and 922. The powers of the board of directors or members under Section 920 may be vested by the articles or bylaws in a designated body.

Section 921 limits the power of directors of a membership corporation to adopt or amend supermajority provisions in the bylaws. See Section 921 and the Official Comment thereto.

§ 921. AMENDMENT TO QUORUM OR VOTING REQUIREMENT FOR BOARD OF DIRECTORS OR DESIGNATED BODY

(a) A provision of the bylaws that includes a higher quorum or voting requirement for the board of directors or a designated body may be amended or repealed:

(1) if originally adopted by the members, only by the members, unless the bylaws otherwise provide;

(2) if adopted by the board of directors or designated body, either by the members, the board of directors or a designated body.

(b) A provision of the bylaws adopted or amended by the members that includes a higher quorum or voting requirement for the board of directors or a designated body may provide that it can be amended or repealed only by a specified vote of either the members, the board of directors or a designated body.

(c) Action by the board of directors or a designated body under subsection (a) to amend or repeal a bylaw that changes the quorum or voting requirement for the board of directors or a designated body must meet the same quorum requirement and be adopted by the same vote required to take action under the quorum and voting requirement then in effect or proposed to be adopted, whichever is greater.

CROSS-REFERENCES

Quorum and voting of directors, § 824.
Increased quorum and voting requirements for members, § 726.

OFFICIAL COMMENT

Without specific authorization in the articles of incorporation, provisions that increase a quorum or voting requirement for the board of directors or a designated body over the requirement that would otherwise apply under this act or that was previously set forth in the bylaws ("supermajority requirements") may be placed in the bylaws of the nonprofit corporation. See Section 8.24(a) and (c). Like other bylaw provisions, these provisions may be adopted either by the members, the board of directors or a designated body. See Section 920. Such provisions may be amended or repealed as provided in this section.

Section 921(a)(1) provides that if a supermajority requirement is imposed by a bylaw adopted by the members, only the members may amend or repeal it. Under Section 921(b), such a bylaw may impose restrictions on the manner in which it may be thereafter amended or repealed by the members. If a supermajority requirement is imposed in a bylaw adopted by the board of directors or a designated body, the bylaw may be amended either by the members, the board of directors or a designated body (see Section 921(a)(2)). If such an amendment is amended by the board of directors or a designated body, however, Section 921(c) requires approval by the supermajority requirement then in effect or proposed to be adopted, whichever is greater. Compare Section 726.

§ 922. BYLAW AMENDMENTS REQUIRING MEMBER APPROVAL

(a) Except as provided in the articles of incorporation or bylaws, the board of directors or a designated body of a membership corporation that has one or more members at the time may not adopt or amend a bylaw under:

(1) Section 610 (differences in rights and obligations of members) providing that some of the members shall have different rights or obligations than other members with respect to voting, dissolution, transfer of memberships or other matters;

(2) Section 613 (member’s liability for dues, assessments, and fees) levying dues, assessments, or fees on some or all of the members;

(3) Section 621 (termination and suspension) relating to the termination or suspension of members;

(4) Section 622 (purchase of memberships) authorizing the purchase of memberships;
(5) Section 808(a) (removal of directors by members or other persons):

(i) requiring cause to remove a director; or

(ii) specifying what constitutes cause to remove a director;

(6) Section 808(e) relating to the removal of a director who is designated in a manner other than election or appointment; or

(7) Section 8.12 (designated body).

(b) The board of directors or designated body of a membership corporation may not amend the articles of incorporation or bylaws to vary the application of subsection (a) to the corporation.

(c) If a nonprofit corporation has more than one class of members, the members of a class are entitled to vote as a separate voting group on an amendment to the bylaws that:

(1) is described in subsection (a) if the amendment would affect the members of that class differently than the members of another class; or

(2) has any of the effects described in Section 904 (voting on amendments by voting groups).

(d) If a class of members will be divided into two or more classes by an amendment to the bylaws, the amendment must be approved by a majority of the members of each class that will be created.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.22.

CROSS-REFERENCES

Class voting by members, § 724.
“Designated body” defined, § 102.
“Member” defined, § 102.

OFFICIAL COMMENT

Section 922(a) prohibits the board of directors or a designated body from amending bylaws on certain subjects without the approval of the members except as otherwise permitted by the articles of incorporation or bylaws. The subjects requiring member approval were considered so important to members that their consent should be required, unless the members have in effect agreed that they will not have a vote by accepting membership in a nonprofit corporation whose articles or bylaws dispense with the required vote.
§ 923. EFFECT OF BYLAW AMENDMENT

(a) Property held in trust by a nonprofit corporation or otherwise dedicated to a charitable purpose may not be diverted from its purpose by an amendment of its bylaws unless the corporation obtains an appropriate order of [court] [the attorney general] to the extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the nondiversion of charitable assets.

(b) A person that is a member or otherwise affiliated with a charitable corporation may not receive a direct or indirect financial benefit in connection with an amendment of the bylaws unless the person is itself a charitable corporation or an unincorporated entity with a charitable purpose. This subsection does not apply to the receipt of reasonable compensation for services rendered.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.23.

OFFICIAL COMMENT

Because the act generally permits the bylaws to contain the same types of provisions for the governance of a nonprofit corporation as the articles of incorporation, Section 923 makes applicable to amendments of the bylaws the same restrictions that apply to amendments of the articles under Section 909.

[Subchapter] C
SPECIAL RIGHTS

§ 930. Approval by third persons.

§ 930. APPROVAL BY THIRD PERSONS

(a) The articles of incorporation may require that an amendment to the articles be approved in a record by a specified person or group of persons in addition to the board of directors and members.

(b) The articles of incorporation or bylaws may require that an amendment to the bylaws be approved in a record by a specified person or group of persons in addition to the board of directors and members.

(c) A requirement in the articles of incorporation or bylaws described in subsection (a) or (b) may only be amended with the approval in a record of the specified person or group of persons.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 10.30.
Section 930 provides a nonprofit corporation flexibility in control over amendments to its articles of incorporation or bylaws by allowing parent or affiliated corporations, government bodies, and others to exercise a veto power over such amendments.

A person given the right to approve an amendment under Section 930 is not a designated body because the approval required under this section is in addition to the otherwise required approvals by the board of directors and members. A situation where a person other than the board of directors is given the power to approve an amendment and approval by the board is not also required, does not implicate this section because in that situation the person will be a designated body.

The act also provides that a person or group of persons whose approval must be obtained to amend the articles of incorporation or bylaws must also consent to a merger, membership exchange, or a sale of all, or substantially all, of the property of a nonprofit corporation other than in the regular course of its activities. See Sections 11.04 and 12.02.

[Chapter] 10
DISPOSITION OF ASSETS

§ 1001. Disposition of assets not requiring member approval.

§ 1002. Member approval of certain dispositions.

§ 1003. Restrictions on dispositions of assets.

§ 1001. DISPOSITION OF ASSETS NOT REQUIRING MEMBER APPROVAL

(a) Unless the articles of incorporation or bylaws otherwise provide, no approval of the members of a membership corporation is required:

(1) to sell, lease, exchange, or otherwise dispose of any or all of the corporation’s assets:

(i) in the usual and regular course of its activities; or
(ii) if the corporation, and any entities in which the corporation owns 80% or more of the outstanding interests, retain an activity that represented or was supported by at least 33 percent of total assets at the end of the most recently completed fiscal year;

(2) to mortgage, pledge, dedicate to the repayment of indebtedness (whether with or without recourse), or otherwise encumber any or all of the corporation’s assets, whether or not in the usual and regular course of its activities; or

(3) to transfer any or all of the corporation’s assets to one or more corporations or other entities all of the memberships or interests of which are owned by the corporation.

(b) See Section 1003 (restrictions on dispositions of assets).


CROSS-REFERENCES

Director standards of conduct, § 830.
Distributions to members, § 640.
Member approval of certain dispositions, § 1002.

OFFICIAL COMMENT

Section 1001 provides generally that member approval is not required for a sale, lease, exchange or other disposition by a nonprofit corporation that would leave the corporation with a significant continuing activity.

Section 1001(a)(1)(ii) provides a safe harbor under which member approval is not required if a nonprofit corporation retains a continuing activity that represents at least 33 percent of the total assets of the corporation and its subsidiaries on a consolidated basis for the most recent full fiscal year. Adoption of that safe harbor represents a policy judgment that a greater measure of certainty than is provided by interpretations of the current case law is highly desirable. The application of this bright-line safe-harbor test should, in most cases, produce a reasonably clear result substantially in conformity with the approaches taken in the better case law developing the “quantitative” and “qualitative” analyses. The test is to be applied to assets for the most recent fiscal year ended immediately before the decision by the board of directors to make the disposition in question.

If a nonprofit corporation disposes of assets for the purpose of reinvesting the proceeds of the disposition in substantially the same activity in a somewhat different form (for example, by selling the corporation’s only building for the purpose of buying or building a replacement building), the disposition and reinvestment should be treated together, so that the transaction should not be deemed to leave the corporation without a significant continuing activity.
In determining whether member approval of a disposition of assets is required, the subsidiaries of a nonprofit corporation that are or should be consolidated with the parent under generally accepted accounting principles are included in the calculation of whether the safe harbor in Section 1001(a)(1)(ii) is met.

The board of directors may base a determination that a retained activity falls within the 33 percent bright-line test of the safe harbor embodied in Section 10.01(a)(1)(ii) either on accounting principles and practices that are reasonable in the circumstances or on a fair valuation or other method that is reasonable in the circumstances.

The utilization of the specific 33 percent safe harbor test for purposes of this section should not be read as implying a standard for the test of significance or materiality for any other purposes under the act or otherwise.

Under Section 1001(a)(1)(i), member approval is not required for a disposition of the nonprofit corporation’s assets in the usual and regular course of its activities, regardless of the size of the transaction.

Under Section 1001(a)(2), member approval is not required before a nonprofit corporation encumbers its assets, whether or not in the usual and regular course of its activities. Such a transaction often involves a bank or some other lender requiring a corporation to pledge its property as collateral for a loan. Subject to a contrary provision in a corporation’s articles of incorporation or bylaws, an encumbrance may be authorized by the board of directors alone.

§ 1002. MEMBER APPROVAL OF CERTAIN DISPOSITIONS

(a) Except as provided in the articles of incorporation or bylaws, a sale, lease, exchange, or other disposition of assets, other than a disposition described in Section 1001 (disposition of assets not requiring members approval), requires approval of the members of a membership corporation.

(b) A sale, lease, exchange, or other disposition that requires approval of the members under subsection (a) shall be approved in the following manner:

(1) The board of directors must first approve the disposition.

(2) The disposition shall then be approved by the members. In submitting the disposition to the members for approval, the board of directors shall recommend that the members approve the disposition, unless the board of directors makes a determination that because of conflicts of interest or other special circumstances it should not make such a recommendation, in which case the board of directors shall inform the members of the basis for its so proceeding.

(3) The board of directors may set conditions for the approval by the members of a disposition or the effectiveness of the disposition.
(4) If the approval of the members is to be given at a meeting, the corporation shall notify to each member entitled to vote of the meeting of members at which the disposition is to be submitted for approval. The notice must state that the purpose, or one of the purposes, of the meeting is to consider the disposition and must contain a description of the disposition, including the terms and conditions of the disposition and the consideration to be received by the corporation.

(5) Unless the articles of incorporation or bylaws, or the board of directors acting pursuant to paragraph (b)(3), requires a greater vote, or a greater number of votes to be present, the approval of a disposition by the members requires the approval of the members at a meeting at which a quorum exists, and, if any class of members is entitled to vote as a separate group on the disposition, the approval of each such separate voting group at a meeting at which a quorum of the voting group exists.

(c) After a disposition has been approved by the members under paragraph (b)(5), and at any time before the disposition has been consummated, it may be abandoned by the nonprofit corporation without action by the members, subject to any contractual rights of other parties to the disposition.

(d) A disposition of assets in the course of dissolution under [Chapter] 11 (dissolution) is not governed by this section.

(e) The assets of a corporation or other entity in which the nonprofit corporation owns 80% or more on the outstanding interests, directly or indirectly, shall be deemed to be the assets of the nonprofit corporation for the purposes of this section.

(f) In addition to the approval of a disposition of assets by the board of directors and members as required by this section, the disposition must also be approved in a record by any person or group of persons whose approval is required under Section 930 to amend the articles of incorporation or bylaws.

(g) See Section 1003 (restrictions on dispositions of assets).


CROSS-REFERENCES

Director standards of conduct, § 830.
Disposition of assets not requiring member approval, § 1001.
Dissolution, Ch 14.
Notice generally, § 103.
Notice of meeting of members, § 705.
Supermajority quorum and voting requirements, § 726.
OFFICIAL COMMENT

Section 1002(b) requires the board of directors, after having approved a disposition that requires member approval, to submit the disposition to the members for approval. When submitting the disposition to the members, the board of directors must make a recommendation to the members that the disposition be approved, unless the board makes a determination that because of conflicts of interests or other special circumstances it should not make a recommendation. For example, the board of directors may make such a determination where there is not a sufficient number of directors free of a conflicting interest to approve the transaction or because the board of directors is evenly divided as to the merits of a transaction but is able to agree that members should be permitted to consider the transaction. If the board of directors makes such a determination, it must describe the conflicts of interests or special circumstances, and communicate the basis for the determination, when submitting the disposition to the members. The exception for conflicts of interest or other special circumstances is intended to be sparingly available. Generally, members should not be asked to act on a disposition in the absence of a recommendation by the board of directors. The exception is not intended to relieve the board of directors of its duty to consider carefully the proposed transaction and the interests of members.

Section 1002(b)(2) permits the board of directors to condition its submission of a proposed disposition to the members. Among the conditions that a board might impose are that the disposition will not be deemed approved unless it is approved by a specified percentage of the members, or by one or more specified classes of members, voting as a separate voting group, or by a specified percentage of disinterested members.

Section 1002(b)(3) provides that approval of a disposition requires approval of the members at a meeting at which at least a majority of the votes entitled to be cast on the disposition is present. In lieu of approval at a meeting of the members, approval can be given by the consent of all the members entitled to vote on the transaction, under the procedures set forth in Section 704.

The term “subsidiary” or “subsidiaries,” as used in Section 1002, includes both corporate and noncorporate subsidiaries. Accordingly, for example, a limited liability company or a partnership may be a subsidiary for purposes of Section 1002.

§ 1003. RESTRICTIONS ON DISPOSITIONS OF ASSETS

(a) Property held in trust or otherwise dedicated to a charitable purpose may not be diverted from its purpose by a transaction described in Section 1001 (disposition of assets not requiring member approval) or 1002 (member approval of certain dispositions) unless the nonprofit corporation obtains an appropriate order from [court] [the attorney general] to the
extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the
nondiversion of charitable assets.

(b) A person who is a member or otherwise affiliated with a charitable corporation
may not receive a direct or indirect financial benefit in connection with a disposition of assets
unless the person is a charitable corporation or an unincorporated entity that has a charitable
purpose. This subsection does not apply to the receipt of reasonable compensation for services
rendered.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 12.03.

CROSS-REFERENCES

“Charitable corporation” defined, § 140.

OFFICIAL COMMENT

Section 1003(a) protects property held in trust or that is a charitable asset from being
diverted by in a disposition of assets from its restricted purposes. Section 1003(a) does not
apply to all nonprofit corporations; only those that hold charitable assets or are established for a
charitable purpose. A state adopting Section 1003(a) should consider what restrictions and
procedures should apply in a proceeding under that provision.

[Chapter] 11

DISSOLUTION

Subchapter

A. Voluntary Dissolution

B. Judicial Dissolution

C. Miscellaneous

D. Administrative Dissolution

[Subchapter] A

VOLUNTARY DISSOLUTION

§ 1101. Dissolution by incorporators or directors.

§ 1102. Approval of dissolution.

§ 1103. Articles of dissolution.

§ 1104. Revocation of dissolution.

§ 1105. Effect of dissolution.

§ 1106. Known claims against dissolved corporation.

§ 1107. Other claims against dissolved corporation.

§ 1108. Court proceedings.

§ 1109. Limitation on director liability.
§ 1101. DISSOLUTION BY INCORPORATORS OR DIRECTORS

A majority of the incorporators or directors of a nonprofit corporation that has not commenced activity, or of a membership corporation that has not admitted any members, may dissolve the corporation by delivering to the secretary of state of state for filing articles of dissolution that set forth:

(1) the name of the corporation;

(2) the date of its incorporation;

(3) either:
   (i) that the corporation has not commenced activity; or
   (ii) that the corporation is a membership corporation and has not admitted any members;

(4) that no debt of the corporation remains unpaid;

(5) that, except as provided in the articles of incorporation or bylaws, the net assets of the corporation remaining after winding up have been distributed to the members, if members were admitted; and

(6) that a majority of the incorporators or directors authorized the dissolution.


CROSS-REFERENCES

Claims against dissolved corporation, §§ 1106 and 1107.
“Deliver” defined, § 102.
Dissolution by board of directors and members, § 1102.
Effective date of dissolution, § 1103.
Effect of dissolution, § 1105.
Filing fees, § 162.
Filing requirements, § 160.
Incorporators, § 201.
Initial directors, § 205.
Revocation of dissolution, § 1104.

OFFICIAL COMMENT
Under the act, a nonprofit corporation is dissolved on the effective date of its articles of dissolution. The act uses the term “dissolution” in this specialized sense, and not to describe the final step in the liquidation of the corporate activities and assets. Section 1105 provides that dissolution does not terminate the corporation’s existence, but that section does require the corporation to wind up its affairs and liquidate.

Section 1101 provides a simple method of voluntary dissolution for a nonprofit corporation that has not admitted any members or commenced activity. These provisions are alternative: a corporation may utilize Section 1101 if it has not admitted members (even though it has commenced activity) or if it has admitted members but has not commenced activity. Dissolution may be accomplished in either of these situations simply by a majority vote of the incorporators or directors. (See Section 205 and its Official Comment for a discussion of the roles of “incorporators” or “initial directors” in the organization of a corporation.)

This simple method of dissolution is likely to be used by name-holding corporations or by nonprofit corporations formed for the initiation of a new venture when the reasons for the initial creation of the corporation have been completely realized or will never come to fruition.

The form of articles of dissolution provided in Section 1101 takes account of the fact that a nonprofit corporation may utilize this section even though it has received contributions from the admission of members or has incurred liabilities either from the commencement of activity without admitting members or from its organization; hence the articles must state that no debts remain unpaid, and that the net assets of the corporation remaining after winding up have been distributed to the members, if members have been admitted, subject to any provision of the articles of incorporation or bylaws restricting the distribution of assets.

The authority of the board of directors under this section may be vested by the articles of incorporation or bylaws in a designated body. See Section 812.

§ 1102. APPROVAL OF DISSOLUTION

(a) The board of directors of a membership corporation may propose dissolution for submission to the members by first approving the dissolution.

(b) For a proposal to dissolve to be adopted:

(1) the board of directors must recommend dissolution to the members, unless the board of directors determines that because of conflict of interest or other special circumstances it should make no recommendation and communicates the basis for its determination to the members; and

(2) the members entitled to vote must approve the proposal to dissolve as provided in subsection (e).
(c) The board of directors may set conditions for the approval of the proposal for dissolution by the members or the effectiveness of the dissolution.

(d) A membership corporation must give notice to each member entitled to vote of the proposed meeting of members. The notice must also state:

   (1) that the purpose, or one of the purposes, of the meeting is to consider dissolving the corporation; and

   (2) how the assets of the corporation will be distributed after all creditors have been paid, or how the distribution of assets will be determined.

(e) Unless the articles of incorporation, the bylaws, or the board of directors acting pursuant to subsection (c), requires a greater vote or a greater number of members to be present, the adoption of the proposal to dissolve by the members requires the approval of the members at a meeting at which a quorum exists, and, if any class of members is entitled to vote as a separate group on the proposal, the approval of each such separate voting group at a meeting at which a quorum of the voting group exists.

(f) If a nonprofit corporation does not have any members entitled to vote on its dissolution, a proposal to dissolve shall be deemed adopted by the corporation when it has been adopted by the board of directors.

(g) A charitable corporation must give the attorney general notice in a record that it intends to dissolve before the time it delivers articles of dissolution to the secretary of state.


CROSS-REFERENCES

Director standards of conduct, § 8.30.
Dissolution by consent of members, § 704.
Effect of dissolution, § 1105.
Notice generally, § 103.
Notice of members’ meeting, § 705.
Quorum at members’ meeting, § 725.
Revocation of dissolution, § 1104.
Voting by voting group, §§ 724 and 725.
Voting entitlement of members generally, § 721.
“Voting group” defined, § 102.

OFFICIAL COMMENT

As noted in the Official Comment to Section 1101, a nonprofit corporation is dissolved under the act on the effective date of its articles of dissolution. The act uses the term
“dissolution” in this specialized sense, and not to describe the final step in the liquidation of the corporate activities and assets. Section 1105 provides that dissolution does not terminate the corporation’s existence, but that section does require the corporation to wind up its affairs and liquidate.

Section 1102(b) requires the board of directors, after approving a proposal to dissolve, to submit the proposal to the members entitled to vote thereon, if any, for their approval. When submitting the proposal the board of directors must make a recommendation to the members that the plan be approved, unless the board of directors makes a determination that because of conflicts of interest or other special circumstances it should make no recommendation. For example, the board of directors may make a determination to refrain from a recommendation because a majority of directors have personal interests in the dissolution or the board is evenly divided as to the merits of the proposal but is able to agree that the members should be permitted to consider dissolution. If the board of directors makes such a determination, it must describe the conflict of interest or special circumstances, and communicate the basis for the determination, when submitting the proposal to dissolve to the members. The exception for conflicts of interest or other special circumstances is intended to be sparingly available. Generally, members should not be asked to act on a proposal for dissolution in the absence of a recommendation by the board of directors. The exception is not intended to relieve the board of directors of its duty to consider carefully the proposed dissolution and the interests of the corporation and its members.

Section 1102(c) permits the board of directors to condition its submission of a proposal for dissolution on any basis. Among the conditions that a board might impose are that the proposal will not be deemed approved unless it is approved by a specified vote of the members, by one or more specified classes of members, voting as a separate voting group, or by a specified percentage of disinterested members. The board of directors is not limited to conditions of these types.

Section 1102(d) provides that if the proposal is required to be approved by the members, and if the approval is to be given at a meeting, the nonprofit corporation must give notice to each member entitled to vote of the meeting of members at which the proposal is to be submitted. Requirements concerning the timing and content of a notice of meeting are set out in Section 705. The explanation of how the distribution of assets will be determined may be in general terms if the board will have the authority to make those determinations.

Section 1102(e) provides that approval of a proposal for dissolution requires approval of the members at a meeting at which a quorum consisting of a majority of the votes entitled to be cast on the proposal exists. If a quorum is present, then under Sections 724 and 725 the proposal will be approved if more votes are cast in favor of the proposal than against it by each voting group entitled to vote on the proposal.

The act does not mandate separate voting by voting groups in relation to dissolution proposals on the theory that, upon dissolution, the rights of all classes of members are fixed by the articles of incorporation or bylaws. Of course, group voting rights may be conferred by the articles or bylaws or by the board of directors, acting pursuant to Section 1102(c).
The authority of the board of directors or members under this section may be vested by the articles of incorporation or bylaws in a designated body. See Section 812.

When a proposal to dissolve is being prepared, consideration should be given to including in the proposal the provision permitted by Section 1104(b) that dissolution may be revoked by action of the board of directors alone.

§ 1103. ARTICLES OF DISSOLUTION

(a) At any time after dissolution is authorized, the nonprofit corporation may dissolve by delivering to the secretary of state for filing articles of dissolution setting forth:

(1) the name of the corporation;
(2) the date that dissolution was authorized; and
(3) if dissolution was approved by the members, a statement that the proposal to dissolve was duly approved by the members in the manner required by this [Act] and by the articles of incorporation and bylaws.

(b) The articles of dissolution shall take effect at the effective date determined in accordance with Section 163 (effective time and date of filing). A nonprofit corporation is dissolved upon the effective date of its articles of dissolution.

(c) For purposes of this [Subchapter], “dissolved corporation” means:

(1) a nonprofit corporation whose articles of dissolution have become effective, and includes a successor entity to which the remaining assets of the corporation are transferred subject to its liabilities for purposes of liquidation; or
(2) a corporation whose period of duration stated in its articles of incorporation has expired.


CROSS-REFERENCES

“Deliver” defined, § 102.
Dissolution by board of directors and members, § 1102.
Dissolution by consent of members, § 704.
Effect of dissolution, § 1105.
Effective time and date of filing, § 163.
Filing fees, § 162.
Filing and signature requirements, § 160.
Revocation of dissolution, § 1104.
Voting by voting group, §§ 724 and 725.
“Voting group” defined, § 102.

OFFICIAL COMMENT

The act of filing the articles of dissolution makes the decision to dissolve a matter of public record and establishes the time when the nonprofit corporation must begin the process of winding up and cease carrying on its activities except to the extent necessary for winding up. If dissolution was approved by the members, the articles of dissolution must state that dissolution was duly approved by the members in the manner required by the act and the articles of incorporation and bylaws of the corporation.

Articles of dissolution may be filed at the commencement of winding up or at any time thereafter. This is the only filing required for voluntary dissolution. No filing is required to mark the completion of winding up since the existence of the nonprofit corporation continues for certain purposes even after its activities are wound up and all of its assets have been distributed. No time limit for filing the articles is specified, and it may sometimes be desirable to postpone filing until winding up is far along or even complete.

A nonprofit corporation is dissolved on the date the articles of dissolution are effective. After this date the corporation is referred to as a “dissolved corporation,” although its existence continues under Section 1105 for purposes of winding up.

Section 1103(c) defines “dissolved corporation” for purposes of Subchapter 11A to include successor entities to which assets are transferred subject to liabilities for purposes of liquidation. This provision covers the situation where a liquidating trust or other successor entity is used to complete the liquidation, but it is not intended to include an interest holder or transferee to which assets are permanently transferred as a distribution or for consideration.

§ 1104. REVOCATION OF DISSOLUTION

(a) A nonprofit corporation may revoke its dissolution after:

(1) the effective date of its articles of dissolution; or

(2) the date stated in its articles of incorporation as the end of its period of duration.

(b) Revocation of dissolution under subsection (a)(1) must be authorized in the same manner as the dissolution was authorized unless that authorization permitted revocation by action of the board of directors alone, in which event the board of directors may revoke the dissolution without action by the members.
(c) After the revocation of dissolution is authorized under subsection (a)(1), the nonprofit corporation may revoke the dissolution by delivering to the secretary of state for filing articles of revocation of dissolution, together with a copy of its articles of dissolution, that set forth:

1. the name of the corporation at the time of dissolution;
2. a new name of the corporation if its prior name is not available at the time of the filing of the articles of revocation of dissolution;
3. the effective date of the dissolution that was revoked;
4. the date that the revocation of dissolution was authorized;
5. if the corporation was dissolved under Section 1101 (dissolution by incorporators or directors) or the corporation did not have any members entitled to vote at the time of dissolution, a statement that revocation of dissolution was authorized by action of the corporation’s board of directors or incorporators;
6. if the corporation’s board of directors revoked the dissolution as authorized by the members, a statement that revocation was permitted by action of the board of directors alone pursuant to that authorization; and
7. if member action was required to revoke the dissolution, a statement that the revocation was duly approved by the members in the manner required by this [Act] and the articles of incorporation and bylaws.

(d) A nonprofit corporation may revoke its dissolution under subsection (a)(2) by adopting an amendment to its articles of incorporation to delete or change its stated period of duration and delivering articles of amendment to the secretary of state for filing.

(e) Articles of revocation of dissolution shall take effect at the effective date determined in accordance with Section 163 (effective time and date of filing).

(f) Revocation of dissolution is effective upon the effective date of the articles of amendment under subsection (d) or the articles of revocation of dissolution under subsection (e).

(g) When the revocation of dissolution is effective, it relates back to and takes effect as of the effective date of the dissolution and the nonprofit corporation resumes carrying on its activities as if dissolution had never occurred, except for the rights of a person arising out of an action or omission in reliance on the dissolution before the person knew or had reason to know of the revocation.

OFFICIAL COMMENT

Voluntary dissolution may be revoked at any time. As a practical matter, however, revocation should normally occur relatively soon after dissolution. Because of the importance and finality of dissolution, the decision to revoke dissolution generally requires member authorization (unless the dissolution was approved solely by the directors or incorporators under Section 1101). Section 1104(b), however, contemplates that the board of directors may revoke dissolution if it is granted that authority in advance by the members when approving the dissolution. That authorization is often included in proposals to dissolve that are contingent upon the effectuation of another transaction, such as a sale of corporate assets not in the ordinary course.

An amendment adopted under Section 1104(d) changing the period of duration of a nonprofit corporation is adopted in the same manner as other amendments of the corporation’s articles of incorporation.

Articles of revocation of dissolution must be filed to reflect the decision to resume the activities of the nonprofit corporation. The information required in these articles parallels the information required in the original articles of dissolution.

The effect of articles of revocation of dissolution is to eliminate the requirement that the nonprofit corporation cease to conduct its activities except as part of the winding-up process and permit it to resume its activities without limitation and as if dissolution had never occurred. Thus, effectiveness of articles of revocation of dissolution dates back to the effective date of the articles of dissolution.

The authority of the board of directors or members under this section may be vested by the articles of incorporation or bylaws in a designated body. See Section 812.
(a) A dissolved nonprofit corporation continues its corporate existence but the dissolved corporation may not carry on any activities except those appropriate to wind up and liquidate its affairs, including:

1. collecting its assets;
2. disposing of its properties that will not be distributed in kind;
3. discharging or making provision for discharging its liabilities;
4. distributing its remaining property as required by law and its articles of incorporation and bylaws; and otherwise as approved when the dissolution was approved or among the members per capita; and
5. doing every other act necessary to wind up and liquidate its activities and affairs.

(b) Dissolution of a nonprofit corporation does not:

1. transfer title to the corporation’s property;
2. subject its directors, members of a designated body, or officers to standards of conduct different from those prescribed in [Chapter] 8 (directors and officers);
3. change:
   (i) quorum or voting requirements for its board of directors or members;
   (ii) provisions for selection, resignation, or removal of its directors or officers or both;
   (iii) provisions for amending its articles of incorporation or bylaws;
4. prevent commencement of a proceeding by or against the corporation in its corporate name;
5. abate or suspend a proceeding pending by or against the corporation on the effective date of dissolution; or
6. terminate the authority of the registered agent of the corporation.

(c) Property held in trust or otherwise dedicated to a charitable purpose may not be diverted from its purpose by the dissolution of a nonprofit corporation unless and until the corporation obtains an order of [court] [the attorney general] to the extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the nondiversion of charitable assets.
(d) A person who is a member or otherwise affiliated with a charitable corporation may not receive a direct or indirect financial benefit in connection with the dissolution of the corporation unless the person is a charitable corporation, a charitable trust, or an unincorporated entity that has a charitable purpose. This subsection does not apply to the receipt of reasonable compensation for services rendered.


CROSS-REFERENCES

Administrative dissolution, §§ 1140 through 1143.
Claims against dissolved corporation, §§ 1106 and 1107.
Deposit with state treasurer, § 1130.
Dissolution by:
    board of directors and members, § 1102.
    incorporators or directors, § 1101.
“Dissolved corporation” defined, § 1103.
Distributions, §§ 640, 641, and 832.
Effective date of dissolution, § 1103.
Judicial dissolution, §§ 1120 through 1123.
“Proceeding” defined, § 102.
Revocation of dissolution, § 1104.
Service of process on registered agent, § 223.

OFFICIAL COMMENT

Section 1105(a) provides that dissolution does not terminate the corporate existence but simply requires the nonprofit corporation to devote itself to winding up its affairs and liquidating its assets. After dissolution, the corporation may not carry on its activities except as may be appropriate for winding up.

The act uses the term “dissolution” in the specialized sense described above and not to describe the final step in the liquidation of the corporate activities. This is made clear by section 1105(b), which provides that Chapter 11 dissolution does not have any of the characteristics of common-law dissolution, which treated corporate dissolution as analogous to the death of a natural person and abated lawsuits, vested equitable title to corporate property in the members, imposed the fiduciary duty of trustees on directors who had custody of corporate assets, and revoked the authority of the registered agent. Section 1105(b) expressly reverses all of these common-law attributes of dissolution and makes clear that the rights, powers, and duties of members, the directors, members of a designated body, and the registered agent are not affected by dissolution and that suits by or against the corporation are not affected in any way.
A dissolved nonprofit corporation may dispose of the known claims against it by notifying its known claimants of the dissolution at any time after its effective date.

The notice must be in a record and:

1. describe the information that must be included in a claim which must be in a record;
2. provide a mailing address where a claim may be sent;
3. state the deadline, which may not be fewer than 120 days from the effective date of the notice, by which the dissolved nonprofit corporation must receive the claim; and
4. state that the claim will be barred if not received by the deadline.

A claim against the dissolved nonprofit corporation is barred:

1. if a claimant who was given notice under subsection (b) does not deliver the claim to the dissolved corporation by the deadline; or
2. if a claimant whose claim was rejected by the dissolved corporation does not commence a proceeding to enforce the claim within 90 days after the rejection notice is effective.

For purposes of this section, “claim” does not include a contingent liability or a claim based on an event occurring after the effective date of dissolution.


CROSS-REFERENCES

Administrative dissolution, §§ 1140 through 1143.
“Deliver” defined, § 102.
Dissolved corporation, § 1103.
Distributions, §§ 640, 641, and 832.
Effective date of dissolution, § 1103.
Judicial dissolution, §§ 1120 through 1123.
Notice, § 103.
“Proceeding” defined, § 102.
Unknown claims, § 1107.

OFFICIAL COMMENT
Sections 1106 and 1107 provide a simplified system for handling known and unknown claims against a dissolved nonprofit corporation, including claims based on events that occur after the dissolution of the corporation. Section 1106 deals solely with known claims while Section 1107 deals with unknown or subsequently arising claims. A claim can be a "known" claim even if it is unliquidated; a claim that is contingent or has not yet matured or in certain cases has matured but has not been asserted is not a "known" claim (see Section 1106(d)). For example, an unmatured liability under a guarantee or a potential default under a lease would not be a "known" claim.

Known claims are handled in Section 1106 through a process of notice to claimants; the notice must contain the information described in Section 1106(b). Section 1106(c) then provides fixed deadlines by which claims are barred under various circumstances, as follows:

1. If a claimant was given effective notice satisfying Section 1106(b) but fails to file the claim by the deadline specified by the dissolved corporation, the claim is barred by Section 1106(c)(1). See Section 103 as to the effectiveness of notice.

2. If a claimant receives notice satisfying Section 1106(b) and files the claim as required:
   (i) but the dissolved corporation rejects the claim, the claimant must commence a proceeding to enforce the claim within 90 days of the rejection or the claim is barred by Section 1106(c)(2); or
   (ii) if the dissolved corporation does not act on the claim or fails to notify the claimant of the rejection, the claimant is not barred by Section 1106(c) until the dissolved corporation notifies the claimant.

3. If the dissolved corporation publishes notice under Section 1107, a claimant who was not notified in a record is barred unless a proceeding is commenced to enforce the claim within three years after publication of the notice.

4. If the dissolved corporation does not publish notice, a claimant who was not notified in a record is not barred by Section 1106(c) from pursuing the claim.

These principles do not lengthen statutes of limitation applicable under general state law. Thus, claims that are not barred under the foregoing rules—for example, if the corporation does not act on a claim—will nevertheless be subject to the general statute of limitations applicable to claims of that type. The act does not require that a dissolved corporation take the actions set out in Sections 1106 and 1107, but if it does not do so the protections those sections provide are not available to it.

Even though the directors are not trustees of the assets of a dissolved nonprofit corporation (see Section 1105(b)(2)), they must discharge or make provision for discharging the corporation’s liabilities before distributing its remaining assets. See Section 1109.
The nonprofit corporation is free, of course, to negotiate with creditors or claimants and
to compromise some or all of the corporation’s debts or other claims against the corporation.

§ 1107. OTHER CLAIMS AGAINST DISSOLVED CORPORATION

(a) A dissolved nonprofit corporation may publish notice of its dissolution and
request that persons with claims against the dissolved corporation present them in accordance
with the notice.

(b) The notice must:

(1) be:

   (i) published one time in a newspaper of general circulation in the
county where the principal office of the dissolved nonprofit corporation (or, if none in this state,
its registered office) is or was last located; and

   (ii) posted conspicuously for at least 30 days on the dissolved
corporation’s website, if any;

(2) describe the information that must be included in a claim and provide a
mailing address where the claim must be sent; and

(3) state that a claim against the dissolved corporation will be barred unless a
proceeding to enforce the claim is commenced by a stated date which must be at least three years
after the later of the date the notice is published and, if applicable, the 30 day period stated in
Section 1107(b)(1)(ii) has expired.

(c) If the dissolved nonprofit corporation complies with subsection (b), the claim of
each of the following claimants is barred unless the claimant commences a proceeding to enforce
the claim against the dissolved corporation by the date stated in Section 1107(b)(3):

   (1) a claimant who was not given notice under Section 1106 (known claims
against dissolved corporation);

   (2) a claimant whose claim was timely sent to the dissolved corporation but
not acted on by the corporation; or

   (3) a claimant whose claim is contingent or based on an event occurring after
the effective date of dissolution.

(d) A claim that is not barred by subsection (c) or Section 1106(b) may be enforced:

   (1) against the dissolved nonprofit corporation, to the extent of its
undistributed assets; or
(2) except as provided in Section 1108(d) (court proceedings), if the assets have been distributed in liquidation, against any person, other than a creditor of the dissolved corporation, to whom the corporation distributed its property to the extent of the distributee’s pro rata share of the claim or the corporate assets distributed to the distributee in liquidation, whichever is less, but a distributee’s total liability for all claims under this section may not exceed the total amount of assets distributed to the distributee.


CROSS-REFERENCES

Administrative dissolution, § 1140 through 1143.
“Claim” defined, § 1106.
“Deliver” defined, § 102.
“Dissolved corporation” defined, § 1103.
Distributions, §§ 640, 641, and 832.
Effective date of dissolution, § 1103.
Judicial dissolution, § 1120 through 1123.
Known claims, § 1106.
Notice, § 103.
“Principal office”:
defined, § 102.
designated in annual report, § 421.
“Proceeding” defined, § 102.
Registered office:
designated in annual report, § 421.
required, §§ 202 and 220.

OFFICIAL COMMENT

Section 1107 continues the liability of a dissolved nonprofit corporation for claims for a period of three years after it publishes notice of dissolution. It is recognized that a three-year cutoff is itself arbitrary, but it is believed that the bulk of post-dissolution claims that can be estimated will arise during this period. This provision is therefore believed to be a reasonable compromise between the competing considerations of providing a remedy to injured plaintiffs and providing a basis for directors to estimate liabilities so that dissolved corporations may distribute remaining assets free of all claims and distributees may receive them secure in the knowledge that they may not be reclaimed.

Directors must generally discharge or make provision for discharging the nonprofit corporation’s liabilities before distributing the remaining assets. See Section 1109(a). Many claims covered by this section are of a type for which provision may be made by purchasing insurance or setting aside a portion of the assets, thereby permitting prompt distributions in liquidation. Claimants, of course, may always have recourse to the remaining assets of the
dissolved corporation. See Section 1107(d)(1). Further, where unbarred claims arise after distributions have been made in liquidation, Section 1107(d)(2) authorizes recovery against the distributees receiving the earlier distributions. The recovery, however, is limited to the smaller of the distributees’ pro rata share of the claim or the total amount of assets received as liquidating distributions from the corporation. Section 1107(d)(2) ensures that claimants seeking to recover distributions will try to recover from the entire class of distributees rather than concentrating only on the larger distributees and protects the limited liability of members. Members also may be liable to directors for recoupment under Section 832(b)(2).

§ 1108. COURT PROCEEDINGS

(a) A dissolved nonprofit corporation that has published a notice under Section 1107 (other claims against dissolved corporation) may file an application with the court of the county where the dissolved corporation’s principal office (or, if none in this state, its registered office) is located for a determination of the amount and form of security to be provided for payment of claims that are contingent or have not been made known to the dissolved corporation or that are based on an event occurring after the effective date of dissolution but that, based on the facts known to the dissolved corporation, are reasonably estimated to arise after the effective date of dissolution. Provision need not be made for any claim that is or is reasonably anticipated to be barred under Section 1107(c).

(b) Within 10 days after the filing of the application, notice of the proceeding must be given by the dissolved nonprofit corporation to each claimant holding a contingent claim whose contingent claim is shown on the records of the dissolved corporation.

(c) The court may appoint a guardian ad litem to represent all claimants whose identities are unknown in any proceeding brought under this section. The reasonable fees and expenses of the guardian, including all reasonable expert witness fees, must be paid by the dissolved nonprofit corporation.

(d) Provision by the dissolved nonprofit corporation for security in the amount and the form ordered by the court under subsection (a) satisfies the dissolved corporation’s obligations with respect to claims that are contingent, have not been made known to the dissolved corporation, or are based on an event occurring after the effective date of dissolution, and those claims may not be enforced against a person who received assets in liquidation.


CROSS-REFERENCES

“Dissolved corporation” defined, § 1103.
Notice, § 103.
“Principal office”: defined, § 102.
OFFICIAL COMMENT

Section 1108(a) authorizes a court proceeding to establish the provision that should be made for unknown or contingent claims and specifies that provision for unknown and contingent claims can be made only for those claims that are estimated to arise after dissolution that are not expected to be barred by Section 1107(c). The same analysis may be made by the board of directors under Section 1109(a) if court proceedings are not used. As a result, estimates for unknown or contingent claims need be made only for those claims that the court determines are reasonably anticipated to be asserted within three years after dissolution. Estimates of those claims might reasonably be based on the claims experience of the corporation prior to its dissolution.

The notice required by Section 1108(b) includes notice to holders of guarantees made by the corporation.

Section 1108(c) allows the court to appoint a guardian ad litem for unknown claimants but does not make the appointment mandatory. Reasonable fees and expenses of the guardian ad litem are to be paid by the dissolved nonprofit corporation. Section 1108 is designed to permit the court to adopt procedures appropriate to the circumstances.

If the proceeding is completed, Section 1108(d) establishes that the dissolved nonprofit corporation is deemed to have satisfied its obligation to discharge or make provision for discharging its liabilities (that obligation is inferred from the corporation’s power to discharge or make provision for discharging its liabilities, see Section 1105(a)(3)). With respect to claims that have not matured, directors are protected from liability by Section 1109(b), and persons receiving distributions are protected from claims under Section 1108(d).

If a court determines that the nonprofit corporation is dissolving for the primary purpose of avoiding anticipated claims of future tort claimants, it is expected that the court will use its general discretionary powers and deny the protections of Section 1108 to the dissolved corporation.

§ 1109. LIMITATION ON DIRECTOR LIABILITY

Directors of a dissolved nonprofit corporation that has disposed of claims under Sections 1106 (known claims against dissolved corporation), 1107 (other claims against dissolved corporation), or 1108 (court proceedings) are not liable for claims against the dissolved corporation that are barred or satisfied under Sections 1106, 1107, or 1108.
CROSS-REFERENCES

“Claim” defined, § 1106.
Directors’ liability for unlawful distributions, § 832.
“Dissolved corporation” defined, § 1103.
Known claims, § 1106.
Other claims, § 1107.
Proceeding to determine security for contingent claims, § 1108.

OFFICIAL COMMENT

Section 1109 provides that directors of a dissolved nonprofit corporation that complies with Sections 1106, 1107, or 1108 are not liable for claims that are disposed of under those sections. For example, directors need not make provision for claims of known creditors who are barred under Section 1106 for failure to file a claim or commence a proceeding within the specified times, for contingent claimants whose estimated claims are barred by the three-year period after publication, under Section 1107(c), or for claimants such as guarantors if provision for the claims have been approved by a court under Section 1108(d).

Section 1109 leaves unchanged the Section 832 provision that director liability is to the corporation. There are, however, cases that under various theories recognize liability directly to creditors for wrongful payments in liquidation. While there might be circumstances under which direct creditor claims are appropriate, the basic approach of Chapter 11 is that claims for breach of duty of directors in handling claims and claims for recoupment of amounts improperly distributed in liquidation should be mediated through the corporation.

If the articles of incorporation or bylaws vest some or all of the authority of the board of directors with respect to dissolution in a designated body, this section applies to the members of the designated body. See Section 812.

[Subchapter] B

JUDICIAL DISSOLUTION

§ 1120. GROUNDS FOR JUDICIAL DISSOLUTION

The [name or describe court or courts] may dissolve a nonprofit corporation:
(1) in a proceeding by the attorney general, if it is established that:
  
  (i) the corporation obtained its articles of incorporation through fraud;
  
  or

  (ii) the corporation has exceeded or abused, and is continuing to exceed or abuse the authority conferred upon it by law;

(2) except as provided in the articles of incorporation or bylaws, in a proceeding by 50 members or members holding at least 5% of the voting power, whichever is less, or by a director or member of a designated body, if it is established that:

  (i) the directors or a designated body are deadlocked in the management of the corporate affairs, the members, if any, are unable to break the deadlock, and irreparable injury to the corporation or its mission is threatened or being suffered because of the deadlock;

  (ii) the directors or those in control of the corporation have acted, are acting, or will act in a manner that is illegal, oppressive, or fraudulent;

  (iii) the members are deadlocked in voting power and have failed, for a period that includes at least two consecutive annual meeting dates, to elect successors to directors whose terms have, or otherwise would have, expired;

  (iv) the corporate assets are being misapplied or wasted; or

  (v) the corporation has insufficient assets to continue its activities and it is no longer able to assemble a quorum of directors or members;

(3) in a proceeding by a creditor, if it is established that:

  (i) the creditor’s claim has been reduced to judgment, the execution on the judgment returned unsatisfied, and the corporation is insolvent; or

  (ii) the corporation has admitted in a record that the creditor’s claim is due and owing and the corporation is insolvent; or

(4) in a proceeding by the corporation to have its voluntary dissolution continued under court supervision.


CROSS-REFERENCES

Administrative dissolution, §§ 1140 through 1143.
Director action, §§ 820 through 824.
Election of directors, §§ 727 and 804.
Revocation of articles of incorporation by state, § 203.
Member voting, §§ 724 through 727.
Terms of directors, §§ 805 and 806.
Ultra vires acts, § 304.
Voluntary dissolution, §§ 1101 through 1105.

OFFICIAL COMMENT

Section 1120 provides grounds for the judicial dissolution of nonprofit corporations at the request of the state, a member, a creditor, a director, a member of a designated body, or a corporation that has commenced voluntary dissolution. This section states that a court “may” order dissolution if a ground for dissolution exists. Thus, there is discretion on the part of the court as to whether dissolution is appropriate even though grounds exist under the specific circumstances.

1. INVOLUNTARY DISSOLUTION BY STATE

Section 1120(1) preserves long standing and traditional provisions authorizing the state to seek to dissolve involuntarily a nonprofit corporation by judicial decree. While this power has been exercised only rarely in recent years, this right of the state involves a policing action that provides a means by which the state may ensure compliance with, and nonabuse of, the fundamentals of corporate existence. Section 1120(1) limits the power of the state in this regard to grounds that are reasonably related to this objective.

2. INVOLUNTARY DISSOLUTION BY MEMBERS OR OTHERS

Section 1120(2) provides for involuntary dissolution at the suit of a member, director, or member of a designated body under circumstances involving deadlock or significant abuse of power by controlling members or other persons.

a. Deadlock

Dissolution because of deadlock is available if the board of directors or a designated body is deadlocked, but only if (1) the members are unable to break the deadlock, and (2) “irreparable injury” to the corporation or its mission is being threatened or suffered. Dissolution because of deadlock of the board of directors or a designated body is not dependent on the lapse of time during which the deadlock continues.

Dissolution is also available because of deadlock at the members’ level if the members are unable to elect directors over a two-year period. Dissolution under Section 1120(2)(iii) is not dependent on irreparable injury or misconduct by the directors then in office. If injury or misconduct is present, a deadlocked member may proceed under another clause of Section 1120(2).
b. Abuse of power

A member may sue for involuntary dissolution upon proof either that those in control of the nonprofit corporation are acting illegally, oppressively, or fraudulently (Section 1120(2)(ii)) or that the corporate assets are being misapplied or wasted (Section 1120(2)(iv)). The application of these grounds for dissolution to specific circumstances obviously involves judicial discretion in the application of a general standard to concrete circumstances. The court should be cautious in the application of these grounds so as to limit them to genuine abuse rather than instances of acceptable tactics in a power struggle for control of a corporation.

3. DISSOLUTION BY CREDITORS

Creditors may obtain involuntary dissolution only when the nonprofit corporation is insolvent and only in the limited circumstances set forth in Section 1120(3). Typically, a proceeding under the federal Bankruptcy Act is an alternative in these situations, although nonprofit corporations are not subject to involuntary bankruptcy petitions. See 11 U.S.C. § 303(a).

4. DISSOLUTION BY CORPORATION

A nonprofit corporation that has commenced voluntary dissolution may petition a court to supervise its dissolution. That action may be appropriate to permit the orderly liquidation of the corporate assets and to protect the corporation from a multitude of creditors’ suits or suits by dissatisfied members.

§ 1121. PROCEDURE FOR JUDICIAL DISSOLUTION

(a) Venue for a proceeding by the attorney general to dissolve a nonprofit corporation lies in [name the county or counties]. Venue for a proceeding brought by any other party named in Section 1120 (grounds for judicial dissolution) lies in the county where a corporation’s principal office (or, if none in this state, its registered office) is or was last located.

(b) It is not necessary to make members, directors, or members of a designated body parties to a proceeding to dissolve a nonprofit corporation unless relief is sought against them individually.

(c) A court in a proceeding brought to dissolve a nonprofit corporation may issue injunctions, appoint a receiver or custodian during the proceeding with all powers and duties the court directs, take other action required to preserve the corporate assets wherever located, and carry on the activities of the corporation until a full hearing can be held.


CROSS-REFERENCES
OFFICIAL COMMENT

Section 1121 designates the attorney general as the officer to bring suits for involuntary dissolution by the state. The county or counties where these suits must be commenced should be specified; it typically is either the state capital or the county in which the corporation’s principal office is located. See the Official Comment to Section 166.

Section 1121 also sets out other procedures for judicial dissolution generally.

§ 1122. RECEIVERSHIP OR CUSTODIANSHIP

(a) A court in a judicial proceeding brought to dissolve a nonprofit corporation may appoint one or more receivers to wind up and liquidate, or one or more custodians to manage, the affairs of the corporation. The court must hold a hearing, after notifying all parties to the proceeding and any interested persons designated by the court, before appointing a receiver or custodian. The court appointing a receiver or custodian has exclusive jurisdiction over the corporation and all of its property wherever located.

(b) The court may appoint an individual or a domestic or foreign nonprofit corporation or eligible entity as a receiver or custodian. If a foreign corporation or foreign eligible entity is appointed as a receiver or custodian, it must be registered to do business in this state. The court may require the receiver or custodian to post bond, with or without sureties, in an amount the court directs.

(c) Unless otherwise provided in the order appointing the receiver or custodian, the receiver or custodian has the power:

(1) in the case of a receiver to:

(i) dispose of all or any part of the assets of the nonprofit corporation wherever located, at a public or private sale, if authorized by the court; and

(ii) sue and defend in the receiver’s own name as receiver of the corporation in all courts of this state;
(2) in the case of a custodian, to exercise all of the powers of the corporation, through or in place of its board of directors and any designated body, to the extent necessary to manage the affairs of the corporation consistent with its mission and in the best interests of its members, if any, and creditors; and

(3) to exercise such other powers as the court may direct in the appointing order.

(d) During a receivership, the court may redesignate the receiver a custodian, and during a custodianship may redesignate the custodian a receiver, if doing so is consistent with the mission of the nonprofit corporation and in the best interests of the corporation, its members, and creditors. The order appointing a receiver or custodian may be amended from time to time in any other manner the court considers appropriate.

(e) The court from time to time during the receivership or custodianship may order compensation paid, and expenses paid or reimbursed, to the receiver or custodian and counsel from the assets of the nonprofit corporation or proceeds from the sale of the assets.

(f) This section does not apply to a nonprofit corporation that is a religious organization.


CROSS-REFERENCES

Custodianship pendente lite, § 1121.
Notice, § 103.
Receivership pendente lite, § 1121.

OFFICIAL COMMENT

In many states, general statutes or rules of court regulate the appointment of receivers or custodians and define their duties. Section 1122 is designed to supplement these general provisions and grant the court power to take the steps it considers necessary to resolve the internal corporate problem or to effect liquidation of the nonprofit corporation in an efficient manner.

§ 1123. DECREE OF DISSOLUTION

(a) If after a hearing the court determines that one or more grounds for judicial dissolution described in Section 1120 (grounds for judicial dissolution) exist, it may enter a decree dissolving the nonprofit corporation and specifying the effective date of the dissolution.
The clerk of the court must deliver a certified copy of the decree to the secretary of state for filing.

(b) After entering the decree of dissolution, the court may oversee the winding-up and liquidation of the nonprofit corporation’s affairs in accordance with Section 1105 (effect of dissolution) and the notification of claimants in accordance with Sections 1106 (known claims against dissolved corporation) and 1107 (other claims against dissolved corporation).


CROSS-REFERENCES

Claims, §§ 1106 and 1107.
Custodianship, §§ 1121 and 1122.
“Deliver” defined, § 102.
Deposit with state treasurer, § 1130.
Dissolution does not terminate authority of registered agent, § 1105.
Receivership, §§ 1121 and 1122.
Secretary of state’s filing duties, § 165.
Winding-up, § 1105.

OFFICIAL COMMENT

A court decree ordering that a nonprofit corporation be dissolved involuntarily has the same legal effect as articles of dissolution. See Section 1103. Section 1123 requires that the secretary of state receive and file a copy of the decree. Thereafter the corporation’s activities and affairs are to be wound up as provided in Sections 1105, 1106, and 1107.

[Subchapter] C

ADMINISTRATIVE DISSOLUTION

§ 1130. Grounds for administrative dissolution.
§ 1131. Procedure for administrative dissolution.
§ 1132. Reinstatement following administrative dissolution.
§ 1133. Appeal from denial of reinstatement.

§ 1130. GROUNDS FOR ADMINISTRATIVE DISSOLUTION

The secretary of state may commence a proceeding under Section 1131 (procedure for administrative dissolution) to administratively dissolve a nonprofit corporation if:

(1) the corporation does not pay within [six months] after they are due any fees, taxes, interest, or penalties imposed by this [Act] or other law which are collected by the secretary of state;
(2) the corporation does not deliver its annual report to the secretary of state within [six months] after it is due;

(3) the corporation is without a registered agent or registered office in this state for [60] consecutive days or more;

(4) the corporation’s period of duration, if any, stated in its articles of incorporation expires.


CROSS-REFERENCES

OFFICIAL COMMENT
The experience in most states has been that actual or threatened administrative dissolution is an effective enforcement mechanism for a variety of statutory obligations. A requirement of judicial dissolution would be inappropriate for many of these violations because of its cost and the diversion of limited legal resources, particularly because most violations reflect the abandonment of the corporation.

The advantages of administrative dissolution in these circumstances are compelling: it not only reduces the number of records maintained by the secretary of state, but also avoids further wasteful attempts to compel compliance by abandoned nonprofit corporations and returns the corporate name promptly to the status of available names.

§ 1131. PROCEDURE FOR ADMINISTRATIVE DISSOLUTION
(a) In a proceeding to administratively dissolve a nonprofit corporation because the secretary of state has determined that one or more grounds exist under Section 1140 (grounds for administrative dissolution) for dissolving a nonprofit corporation, the secretary of state must serve the corporation with notice in a record of that determination under Section 223 (service on domestic and foreign nonprofit corporations).
(b) If the nonprofit corporation does not correct each ground for dissolution or demonstrate to the reasonable satisfaction of the secretary of state that each ground determined by the secretary of state does not exist within 60 days after service of the notice under Section 223, the secretary of state may administratively dissolve the corporation by signing a certificate of dissolution that recites the ground or grounds for dissolution and its effective date. The secretary of state must file the original of the certificate and serve a copy on the corporation under Section 223.

(c) A nonprofit corporation that is administratively dissolved continues its corporate existence but may not carry on any activities except those necessary to:

(1) wind up and liquidate its activities and affairs under Section 1105 and notify claimants under Sections 1106 (known claims against dissolved corporation) and 1107 (other claims against dissolved corporation); or

(2) apply for reinstatement under Section 1132 (reinstatement following administrative dissolution).

(d) The administrative dissolution of a nonprofit corporation does not terminate the authority of its registered agent.

(e) A person is not liable in contract, tort, or otherwise solely by reason of being a director, member of a designated body, officer, or member of a nonprofit corporation that was dissolved under this [Subchapter], with respect to the activities or affairs of the corporation that have been continued, with or without knowledge of the dissolution.


CROSS-REFERENCES

Appeal from denial of reinstatement, § 1133.
Claims, §§ 1106 and 1107.
Effective date of service, § 223.
Reinstatement following administrative dissolution, § 1132.
Winding up, § 1105.

OFFICIAL COMMENT

Many failures to comply with statutory requirements that may give rise to administrative dissolution under Section 1130 occur because of oversight or inadvertence by corporate officers of nonprofit corporations that are continuing their activities. Those failures are usually corrected promptly when brought to the corporation’s attention. Section 1131(a) and (b) therefore provide a mandatory notice by the secretary of state to each corporation subject to administrative dissolution and a 60-day grace period following the notice before the certificate of administrative dissolution may be filed.
In most instances, the issue of whether the nonprofit corporation is subject to administrative dissolution will not be controverted. If a corporation is administratively dissolved, it may petition the secretary of state for reinstatement under Section 1132 and, if this is denied, it may appeal to the courts under Section 1133.

§ 1142. REINSTATEMENT FOLLOWING ADMINISTRATIVE DISSOLUTION

(a) A nonprofit corporation administratively dissolved under Section 1131 (procedure for administrative dissolution) may apply to the secretary of state for reinstatement. The application must state:

1. the name of the corporation at the time of its administrative dissolution;
2. a new name of the corporation if its prior name is not available at the time of the filing of the application for reinstatement;
3. the address of the principal office of the corporation and the name and address of its registered agent;
4. the effective date of its administrative dissolution; and
5. that the grounds for dissolution either did not exist or have been eliminated.

(b) To be reinstated, a nonprofit corporation must pay all fees, taxes, interest, and penalties that were due to the secretary of state at the time of the corporation’s administrative dissolution and all fees, taxes, interest, and penalties that would have been due to the secretary of state while the corporation was dissolved administratively.

(c) If the secretary of state determines that the application contains the information required by subsection (a), that the information is correct, and that all payments required to be made to the secretary of state by subsection (b) have been made, the secretary of state must:

1. cancel the certificate of dissolution and prepare a certificate of reinstatement that recites that determination and the effective date of reinstatement;
2. file the certificate; and
3. serve a copy on the nonprofit corporation under Section 223 (service on domestic and foreign nonprofit corporations).

(d) When the reinstatement is effective, it relates back to and takes effect as of the effective date of the administrative dissolution and the nonprofit corporation resumes carrying on its activities as if the administrative dissolution had never occurred, except for the rights of a
person arising out of an act or omission in reliance on the dissolution before the person knew or had reason to know of the reinstatement.


CROSS-REFERENCES


OFFICIAL COMMENT

Section 1142 applies when a nonprofit corporation fails to receive or respond to the predissolution notice of default required by Section 1131. A corporation that is reinstated under this section resumes carrying on its business as before dissolution. There is no time limit on when a corporation may apply for reinstatement.

In order to be eligible for reinstatement, a nonprofit corporation must comply with all statutory requirements at the time it seeks reinstatement. It must establish, for example, that all taxes and fees have been paid. Because dissolution makes its name available for use by another person, a corporation may need to change its name when it files the application for reinstatement.

§ 1143. APPEAL FROM DENIAL OF REINSTATEMENT

(a) If the secretary of state denies a nonprofit corporation’s application for reinstatement following administrative dissolution, the secretary of state must serve the corporation under Section 223 (service on domestic and foreign nonprofit corporations) with a notice in a record that explains the reason for denial.

(b) The nonprofit corporation may appeal the denial of reinstatement to the [name or describe] court within [90 days] after service of the notice of denial. The corporation appeals by petitioning the court to set aside the dissolution and attaching to the petition copies of the secretary of state’s certificate of dissolution, the corporation’s application for reinstatement, and the secretary of state’s notice of denial.

(c) The court may summarily order the secretary of state to reinstate the dissolved nonprofit corporation or may take other action the court considers appropriate.

(d) The court’s final decision may be appealed as in other civil proceedings.
CROSS-REFERENCES

Effective date of service, § 223.
Grounds for administrative dissolution, § 1130.
Notice, § 103.
Reinstatement following administrative dissolution, § 1132.

OFFICIAL COMMENT

Section 1133 provides for an appeal from a decision by the secretary of state denying a petition for reinstatement. The court with jurisdiction over an appeal should be specified, and states adopting this section should specify who has the burden of proof on appeal and the standard for judicial review. See the Official Comment to Section 166.

[Chapter] 12
ENTITY TRANSACTIONS

Subchapter
A. Preliminary provisions
B. Merger
C. Interest Exchange
D. Domestication
E. Conversion

[Subchapter] A.
PRELIMINARY PROVISIONS

§ 1201. [Chapter] definitions.
§ 1202. Excluded transactions.
§ 1203. Required approvals.
§ 1204. Appraisal Rights.

§ 1201. [CHAPTER] DEFINITIONS

As used in this [Chapter] 12 (entity transactions):

“Acquired entity” means the domestic corporation or eligible entity, all of one or more classes or series of interests of which are acquired in an interest exchange.

“Acquiring entity” means the entity that acquires all of one or more classes or series of interests of the acquired entity in an interest exchange.
“Conversion” means a transaction pursuant to [Subchapter] 12E (conversion).

“Converted entity” means the converting entity as it continues in existence after a conversion.

“Converting entity” means the domestic nonprofit corporation that approves a plan of conversion pursuant to Section 1252 (approval of conversion) or the eligible entity that approves a conversion to a domestic nonprofit corporation pursuant to the organic law of the eligible entity.

“Domesticated corporation” means the domesticating nonprofit corporation as it continues in existence after a domestication.

“Domesticating corporation” means the domestic nonprofit corporation that approves a plan of domestication pursuant to Section 1242 (approval of domestication) or the foreign corporation that approves a domestication pursuant to the organic law of the foreign corporation.

“Domestication” means a transaction pursuant to [Subchapter] 12D (domestication).

“Enactment date,” as used in a particular [Subchapter], means the first date on which the law of this state authorized an entity to engage in a transaction of the type authorized by that [Subchapter].

“Interest exchange” means a transaction authorized by [Subchapter] 12C (interest exchange).

“Merger” means a transaction in which two or more merging entities are combined into a surviving entity pursuant to a record filed by the secretary of state.

“Merging entity” means an entity that is a party to a merger and exists immediately before the merger becomes effective.

“Protected agreement” means:

(1) a document evidencing indebtedness of a domestic nonprofit corporation or eligible entity and any related agreement in effect immediately before the enactment date;

(2) an agreement that is binding on a domestic corporation or eligible entity immediately before the enactment date;

(3) the articles of incorporation or bylaws of a domestic corporation or the organic rules of a domestic eligible entity, in each case in effect immediately before the enactment date; or
an agreement that is binding on any of the interest holders, directors or
governors of a domestic corporation or eligible entity, in their capacities as such,
immediately before the enactment date.

“Registered foreign eligible entity” means a registered foreign corporation or other
eligible entity registered to conduct business in this state.

“Surviving entity” means the entity that continues in existence after or is created by a
merger under [Subchapter] 12B (merger).

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), §§ 9.01 and 11.01. Cf. Model Business
Corporation Act (2016 Revision), § 9.01.

CROSS-REFERENCES

Articles of incorporation, § 202.

OFFICIAL COMMENT

Section 1201 sets out definitions used in the Act’s provisions on merger, interest
exchange, domestication, and conversion.

Section 1201 defines “protected agreement” as those specified documents and
agreements which were in effect before the laws of the state first provided for interest exchanges,
domestications, or conversions. A person contracting with a corporation or loaning it money, or
which drafted and negotiated special rights relating to mergers or similar transactions, before the
enactment of Chapter 12 (or any similar predecessor law) should not be charged with the
consequences of not having dealt with interest exchanges, domestications, and conversions.
Sections 1230(c), 1240(c) and 1250(e) provide special rules dealing with protected agreements.

§ 1202. EXCLUDED TRANSACTIONS [OPTIONAL]

This [Chapter] may not be used to effect a transaction that:

(1) converts a company organized on the mutual principle to one organized
    on the basis of share ownership;

(2) converts a nonprofit insurance company to a for-profit stock
corporation; or

(3) other examples

(2016 Revision), § 9.02.
OFFICIAL COMMENT

Section 1202 prohibits certain transactions that are subject to a separate statutory or legal framework from being effected under Chapter 12.

§ 1203. RESTRICTIONS AND REQUIRED APPROVALS

(a) If a domestic or foreign nonprofit corporation or eligible entity may not be a party to a merger without the approval of the [attorney general], the [department of banking], the [department of insurance] or the [public utility commission], and the applicable statutes or regulations do not specifically deal with transactions under this [Chapter] 12 but do require approval for mergers, the corporation or entity may not be a party to a transaction under this [Chapter] 12 without the prior approval of that agency or official.

(b) Property held in trust by an entity or that is a charitable asset may not be diverted from its purpose by any transaction under this [Chapter] 12 unless the entity obtains an appropriate order of [court] [the attorney general] specifying the disposition of the property to the extent required by and pursuant to the law of this state on cy pres or otherwise dealing with the nondiversion of charitable assets.

(c) A person that is an interest holder, governor or otherwise affiliated with a charitable corporation or an unincorporated entity with a charitable purpose may not receive a direct or indirect financial benefit in connection with a transaction under this [Chapter] 12 to which the charitable corporation or unincorporated entity is a party unless the person is itself a charitable corporation or unincorporated entity with a charitable purpose. This Section 1203(c) does not apply to the receipt of reasonable compensation for services rendered.

(d) A devise, bequest, gift, grant, or promise contained in a will or other instrument, in trust or otherwise, made before or after a transaction under this [Chapter] 12, to or for a charitable corporation or unincorporated entity with a charitable purpose that is the subject of the transaction, inures to the entity as it continues in existence after the transaction if it is a charitable corporation or unincorporated entity with a charitable purpose, subject to the express terms of the will or other instrument.


CROSS-REFERENCES

Appeal from secretary of state’s refusal to file document, § 166
“Domestic nonprofit corporation” defined, § 102.
Filing duty of secretary of state, § 165.

OFFICIAL COMMENT
Section 1203 ensures that transactions under Chapter 12 will be effected only if required state governmental approvals have been obtained. If other state laws require such approvals in the case of mergers, but do not address approvals in the case of interest exchanges, domestications, and conversions, then Section 1203 requires that transactions under Chapter 12 obtain the same regulatory approvals as mergers. To prevent the procedures in Chapter 12 from being used to avoid restrictions on the use of property held in trust by nonprofit entities or that is a charitable asset, Section 1203 requires approval of the effect of transactions under Chapter 12 by the appropriate arm of government having supervision of nonprofit entities.

§ 1204. APPRAISAL RIGHTS

(a) An interest holder of a domestic merging, acquired, converting, or domesticating eligible entity is entitled to appraisal rights in connection with the transaction if the interest holder would have been entitled to appraisal rights under the entity’s organic law in connection with a merger in which the interest of the interest holder was changed, converted, or exchanged unless:

(1) the organic law permits the organic rules to limit or eliminate the availability of appraisal rights; and
(2) the organic rules provide such a limit or elimination.

(b) An interest holder of a domestic merging, acquired, converting, or domesticating eligible entity is entitled to contractual appraisal rights in connection with a transaction under this [Act] to the extent provided:

(1) in the entity’s organic rules;
(2) in the plan; or
(3) in the case of a business corporation, by action of its governors.

(c) If an interest holder is entitled to contractual appraisal rights under this Section 1204 and the eligible entity’s organic law does not provide procedures for the conduct of an appraisal rights proceeding, [Chapter 13 of the Model Business Corporation Act] applies to the extent practicable or as otherwise provided in the entity’s organic rules or the plan.

[Subchapter] B
MERGER

§ 1220. Merger authorized.
§ 1221. Plan of merger.
§ 1222. Approval of merger.
§ 1220. MERGER AUTHORIZED.

(a) Except as otherwise provided in this Section 1220, by complying with [Subchapter] 12A (preliminary provisions) and this [Subchapter] 12B:

(1) one or more domestic nonprofit corporations may merge with one or more domestic or foreign nonprofit corporations, domestic or foreign business corporations or eligible entities; and

(2) two or more foreign nonprofit corporations or eligible entities may merge into a surviving entity that is a domestic nonprofit corporation created in the merger.

(b) Except as otherwise provided in this Section 1220, by complying with the provisions of [Subchapter] 12A and this [Subchapter] 12B applicable to foreign entities, a foreign entity may be a party to a merger under this [Subchapter] 12B or may be the surviving entity in such a merger if the merger is authorized by the law of the foreign entity’s governing jurisdiction.

(c) If the organic law or organic rules of a domestic eligible entity do not provide procedures for, but do not prohibit, the approval of a merger, a plan of merger may nonetheless be adopted and approved by the unanimous consent of all of the interest holders of the eligible entity, and the merger may thereafter be effected as provided in the other provisions of this [Subchapter] 12B.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 11.02(a) – (c). Cf. Model Business Corporation Act (2016 Revision), § 11.02(a) – (c).

CROSS-REFERENCES

Abandonment of merger, § 1224.
Amendment of articles of incorporation in merger, § 1221.
Approval of plan of merger, § 1222.
Articles of merger, § 1225.
“Corporation “ and “domestic nonprofit corporation” defined, § 102.
Effect of merger, § 1226.
“Eligible entity” defined, § 102.
Extrinsic facts, § 105.
“Foreign corporation” and “foreign nonprofit corporation” defined, § 102.
“Interest holder” defined, § 102.
“Membership” defined, § 102.
“Organic law” and “organic rules” defined, § 102.
“Public organic record” defined, § 102.
Short-form merger, § 1223.

OFFICIAL COMMENT

Section 1220 authorizes a domestic nonprofit corporation to merge with another domestic nonprofit corporation or with a foreign nonprofit corporation. It also authorizes one or more domestic corporations to merge with one or more eligible entities (such as business corporations, limited liability companies, or partnerships). In addition, it provides for the merger of two or more eligible entities, even if no domestic nonprofit corporation is a party to the merger, but only if the survivor is a domestic nonprofit corporation created by the merger.

A foreign nonprofit corporation or foreign eligible entity may be a party to or be the survivor in a merger authorized by Chapter 12 only if the merger is permitted by the laws under which the foreign corporation or eligible entity is organized. Whether and on what terms a foreign corporation or a foreign eligible entity is authorized to merge is governed by those laws. If a foreign corporation or eligible entity is so authorized, it must comply with the applicable provisions of Chapter 12 in addition to the requirements of its own governing laws. For example, Section 1221(a) sets forth certain requirements for the contents of a plan of merger with a domestic corporation, and section 1226(e) provides that upon a merger becoming effective, a foreign corporation or foreign eligible entity that is the survivor may be served with process in the state.

If the law under which a domestic eligible entity is organized does not expressly authorize it to be a party to or survive a merger under Chapter 12, Section 1220(c) provides procedures for such an entity to adopt and effect a plan of merger.

§ 1221. PLAN OF MERGER.

(a) A domestic nonprofit corporation may become a party to a merger under this [Subchapter] 12B by approving a plan of merger. The plan must be in a record and contain:

(1) as to each merging entity, its name, governing jurisdiction, and type of entity;

(2) if the surviving entity is to be created in the merger, a statement to that effect and the entity’s name, governing jurisdiction, and type of entity;

(3) the manner of converting the interests in each party to the merger into interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing;

(4) if the surviving entity exists before the merger, any proposed amendments to:
(i) its public organic record, if any; and

(ii) its private organic rules that are, or are proposed to be, in a record;

(5) if the surviving entity is to be created in the merger:

(i) its proposed public organic record, if any; and

(ii) the full text of its private organic rules that are proposed to be in a record;

(6) the other terms and conditions of the merger; and

(7) any other provision required by the law of a merging entity’s governing jurisdiction or the organic rules of a merging entity.

(b) In addition to the requirements of Section 1221(a), a plan of merger may contain any other provision not prohibited by law.

(c) Terms of a plan of merger may be made dependent on facts objectively ascertainable outside the plan in accordance with Section 105 (extrinsic facts in filed record).

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 11.02(d) and (f). Cf. Model Business Corporation Act (2016 Revision), § 11.02(d) – (f).

OFFICIAL COMMENT

A nonprofit corporation’s articles of incorporation may be amended by a merger, and Section 1221(a)(4) provides that a plan of merger must include any such amendments. If the plan of merger is approved and the survivor is a domestic entity, Section 1226 provides that the amendments will become effective with the merger. If the plan includes amendments to the articles of incorporation of a surviving domestic corporation, Section 1222(a)(5), by reference to the voting requirements of Section 904 relating to amendments of the articles of incorporation, may impose voting requirements by separate voting groups that would not otherwise apply.

Although the plan of merger must include any amendments to the articles of incorporation or public organic record of the survivor, the survivor’s articles of incorporation or public organic record are not otherwise required to be included in the plan unless the survivor is created by the merger. However, if approval of the plan of merger by the members of a domestic corporation is required under Section 1222, Section 1222(a)(3) requires that its members be furnished with a copy or summary of the articles of incorporation or public organic record of the survivor in connection with voting on approval.

§ 1222. APPROVAL OF MERGER.
(a) In the case of a domestic nonprofit corporation that is a party to a merger, the plan of merger must be adopted in the following manner:

(1) The plan of merger must first be adopted by the board of directors. The board may set conditions for the approval of the plan of merger by the members or the effectiveness of the plan of merger. If a domestic nonprofit corporation that is a party to a merger does not have any members entitled to vote thereon, a plan of merger is deemed adopted by the corporation when it has been adopted by the board.

(2) Except as provided in Section 1222(a)(1) (plan of merger), Section 1222(a)(7) and Section 1223 (short-form merger), the plan of merger must then be approved by the members. In submitting the plan of merger to the members for approval, the board must recommend that the members approve the plan unless the board of directors makes a determination that because of conflicts of interest or other special circumstances it should not make such a recommendation, in which case the board must inform the members of the basis for that determination.

(3) If the plan of merger is required to be approved by the members, and if the approval is to be given at a meeting, the corporation must notify each member entitled to vote, of the meeting of members at which the plan is to be submitted for approval. The notice must state that the purpose, or one of the purposes, of the meeting is to consider the plan and must contain or be accompanied by a copy or summary of the plan. If the corporation is not to be the surviving entity, the notice must also include or be accompanied by a copy or summary of the organic rules of the surviving entity as in effect immediately after the merger. If the corporation is to be merged with a domestic or foreign nonprofit corporation or eligible entity and a new domestic or foreign nonprofit corporation or eligible entity is to be created pursuant to the merger, the notice must include or be accompanied by a copy or a summary of the organic rules of the new corporation or eligible entity.

(4) Unless the articles of incorporation, bylaws, or the board of directors acting pursuant to Section 1222 (a)(1), require a greater vote or a greater quorum, approval of the plan of merger requires the approval of the members at a meeting at which a quorum exists consisting of a majority of the votes entitled to be cast on the plan, and, if any class of memberships is entitled to vote as a separate group on the plan of merger, the approval of each such separate voting group at a meeting at which a quorum of the voting group is present consisting of a majority of the votes entitled to be cast on the merger by that voting group.

(5) Subject to Section 1222(a)(6), separate voting by voting groups on a plan of merger is required:

(i) by each class of memberships that:

(A) are to be converted under the plan of merger into securities, interests, or obligations, rights to acquire, securities, or interests; cash, other property, or any combination of the foregoing; or
(B) are entitled to vote as a separate group on a provision in the plan that constitutes a proposed amendment to the articles or bylaws of the surviving corporation that requires action by separate voting groups under Section 904 (voting on amendments by voting groups) or Section 922 (bylaw amendments requiring member approval); or

(ii) if the voting group is entitled under the articles or bylaws to vote as a voting group to approve a plan of merger.

(6) The articles or bylaws may expressly limit or eliminate the separate voting rights provided in Section 1222(a)(5)(i)(A) as to any class of memberships, except when the plan of merger includes what is or would be in effect an amendment subject to Section 1222(a)(5)(i)(B).

(7) Unless the articles or bylaws otherwise provide, approval by the members of a plan of merger is not required if:

(i) the corporation will survive the merger;

(ii) except for amendments permitted by Section 905 (amendment of articles of nonmembership corporation), its articles will not be changed; and

(iii) each member whose membership was outstanding immediately before the effective date of the merger will hold the same membership, with identical preferences, rights and limitations, immediately after the effective date of the merger.

(8) If as a result of a merger, one or more members of a domestic nonprofit corporation would become subject to new interest holder liability, approval of the plan of merger requires the signing in connection with the merger, by each such member, of a separate consent in a record to become subject to such new interest holder liability, unless in the case of a member that already has interest holder liability with respect to the corporation:

(i) the new interest holder liability is with respect to a domestic or foreign nonprofit corporation (which may be a different or the same corporation in which the person is a member); and

(ii) the terms and conditions of the new interest holder liability are substantially identical to those of the existing interest holder liability (other than for changes that eliminate or reduce such interest holder liability).

(9) In addition to the adoption and approval of the plan of merger by the board of directors and members as required by this section, the plan of merger must also be approved in a record by any person or group of persons whose approval is required under Section 930 (approval by third persons) to amend the articles or bylaws.

(b) See Section 1203 (required approvals).
CROSS-REFERENCES

Abandonment of merger, § 1224.
Director standards of conduct, § 830.
Director standards of liability, § 831.
Notice generally, § 103.
Notice of members meeting, § 705.
“Record” defined, § 102.
Supremacy quorum and voting requirements, § 726.
Voting by voting groups generally, §§ 724 and 725.
Voting by voting group on amendment of articles of incorporation, § 904.
Voting entitlement of members generally, § 721.
“Voting group” defined, § 102.
“Voting power” defined, § 102.

OFFICIAL COMMENT

When submitting a plan of merger to the members, Section 1222(a)(2) requires the board of directors to recommend the transaction, subject to two exceptions. The board might exercise the exception where the number of directors having a conflicting interest makes it inadvisable for them to recommend the transaction or where the board is evenly divided as to the merits of the transaction but is able to agree that members should be permitted to consider the transaction. Section 1222(a)(2) permits the board of directors to condition its submission of a plan of merger to the members or the effectiveness of a plan of merger. Among the conditions that a board of directors might impose are that the plan will not be deemed approved unless it is approved by a specified vote of the members, or by one or more specified classes or series of members, voting as a separate voting group, or by a specified percentage of disinterested members.

Section 1222(a)(4) sets forth quorum and voting requirements applicable to a member vote to approve a plan of merger. If a quorum is present, and subject to any greater vote required by the articles of incorporation or the board of directors pursuant to Section 1222(a)(1), under Sections 725 and 726 the plan will be approved if more votes are cast in favor of the plan than against it by the voting group or each separate voting group, as the case may be, entitled to vote on the plan. In lieu of action at a meeting, shareholder approval may be by written consent under the procedures set forth in Section 704.

The approval provisions of Section 1222(a)(8) apply only in situations where a member is becoming subject to new “interest holder liability” as defined in Section 102, for example, where a corporation is merging into a general partnership or a cap on the member’s interest holder liability is increased. The effect of a merger on interest holder liability will be determined as provided in Section 1226(d).
§ 1223. SHORT-FORM MERGER

(a) In the manner provided in Section 1223(b), an entity that holds a membership in a domestic nonprofit corporation that carries at least 80% of the voting power of each class of membership of the corporation that has voting power may merge:

(1) the corporation into itself or into another domestic or foreign nonprofit corporation or eligible entity in which the entity owns at least 80% of the voting power of each class and series of the outstanding interests which have voting power; or

(2) itself into the corporation.

(b) A merger described in Section 1223(a) does not require the approval of the board of directors or members of the domestic nonprofit corporation, unless the organic rules of the entity with voting power in the corporation or the articles of incorporation or bylaws of the corporation otherwise provide. Section 1222(a)(8) (approval of merger) applies to a merger under this Section 1223. The articles of merger relating to a merger under this Section 1223 do not need to be signed by the corporation.

(c) The entity with voting power in the domestic nonprofit corporation shall, within 10 days after the effective date of a merger approved under this Section 1223, notify each of the members of the corporation that the merger has become effective.

(d) Except as provided in this section, a merger under this section shall be governed by the provisions of this [Subchapter] 12B applicable to mergers generally.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 11.05. Cf: Model Business Corporation Act (2016 Revision), § 11.05.

CROSS-REFERENCES

Articles of merger, § 1225.
“Corporation” and “domestic nonprofit corporation” defined, § 102.
Director standards of conduct, § 830.
Director standards of liability, § 831.
“Eligible entity” defined, § 102.
“Voting power” defined, § 102.

OFFICIAL COMMENT

If the conditions of Section 1223 are met, no approval is required by the board of directors or members of a controlled corporation that is merged into a controlling corporation, or other controlled corporation. In other respects, mergers between controlled and controlling corporations are governed by other provisions of Chapter 12, including Section 1222(a)(9).
Section 1223 does not dispense with approval by the members of a nonprofit corporation that is the controlling entity in a merger subject to Section 1223.

Section 1223 only applies to the approvals required with respect to a controlled corporation that is a domestic nonprofit corporation because the approvals that would be required in the case of a subsidiary that is any other form of entity will be determined under the organic law of that entity.

§ 1224. AMENDMENT OR ABANDONMENT OF PLAN OF MERGER.

(a) A plan of merger may be amended only with the consent of each party to the plan, except as otherwise provided in the plan and before articles of merger have taken effect.

(b) A domestic nonprofit corporation, or a merging domestic eligible entity whose organic law does not provide for amendment of a plan of merger, may approve an amendment of a plan of merger:

(1) in the same manner as the plan was approved, if the plan does not provide for the manner in which it may be amended; or

(2) by its governors or interest holders in the manner provided in the plan, but an interest holder that was entitled to vote on or consent to approval of the merger is entitled to vote on or consent to any amendment of the plan that will change:

   (i) the amount or kind of interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing, to be received by the interest holders of any party to the plan;

   (ii) the public organic record, if any, or private organic rules of the surviving entity that will be in effect immediately after the merger becomes effective, except for changes that do not require approval of the interest holders of the surviving entity under its organic law or organic rules; or

   (iii) any other terms or conditions of the plan, if the change would adversely affect the interest holder in any material respect.

(c) After a plan of merger has been approved and before articles of merger are effective, the plan may be abandoned as provided in the plan. Unless prohibited by the plan, the plan may be abandoned in the same manner as the plan was approved by:

(1) a domestic nonprofit corporation; or

(2) a merging domestic eligible entity if the organic law of the entity does not provide for amendment of a plan of merger.
(d) If a plan of merger is abandoned after articles of merger have been delivered to
the secretary of state for filing and before the articles are effective, articles of abandonment,
signed by a party to the plan, must be delivered to the secretary of state for filing before the
articles of merger are effective. The articles of abandonment take effect on filing, and the merger
is abandoned and does not become effective. The articles of abandonment must contain:

1. the name of each party to the plan of merger;
2. the date on which the articles of merger were filed by the secretary of
   state; and
3. a statement that the merger has been abandoned in accordance with this
   Section 1224.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), §§ 11.02(e) and 11.08. Cf. Model Business
Corporation Act (2016 Revision), § 11.02(g) and 11.08.

CROSS-REFERENCES

Approval of merger, § 1222.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Filing requirements, § 160.

OFFICIAL COMMENT

Under Section 1224, unless otherwise provided in the plan of merger, a merging
domestic nonprofit corporation may abandon the transaction without member approval, even
though the transaction has been previously approved by the corporation’s members. Section
1224 also provides default rules for domestic eligible entities to amend or abandon a plan of
merger if the eligible entity’s organic law does not provide for amendment of a plan of merger.
The power of a party under Section 1224 to abandon a transaction without member approval
does not affect any contract rights that other parties may have.

The functions of the board of directors under this section may be vested by the articles of
incorporation or bylaws in a designated body either to the exclusion of, or jointly with, the board
of directors.

§ 1225. ARTICLES OF MERGER; EFFECTIVE DATE OF MERGER.

(a) Articles of merger must be signed by each merging entity, except as provided in
Section 1223 (short-form merger), and delivered to the secretary of state for filing.

(b) Articles of merger must contain:
(1) the name, governing jurisdiction, and type of entity of each merging entity;

(2) the name, governing jurisdiction, and type of entity of the surviving entity;

(3) if the articles of merger are not to be effective upon filing, the later date and time on which they will become effective as determined in accordance with Section 163 (effective time and date of filing);

(4) a statement that the merger was approved by each domestic merging nonprofit corporation if any, in accordance with this [Subchapter] 12B, by each domestic merging entity, if any, in accordance with its organic law and organic rules, and by each foreign merging entity, if any, in accordance with the law of its governing jurisdiction;

(5) if the surviving entity exists before the merger and is a domestic filing entity, any amendment to its public organic record approved as part of the plan of merger;

(6) if the surviving entity is created by the merger and is a domestic filing entity, its public organic record, as an attachment;

(7) if the surviving entity is created by the merger and is a domestic limited liability partnership, its statement of qualification, as an attachment; and

(8) if the surviving entity is a foreign entity that is not a registered foreign entity, a mailing address for the surviving entity to which the secretary of state may send any process served on the secretary of state pursuant to Section 1226(e) (effect of merger).

(c) In addition to the requirements of Section 1225(b), articles of merger may contain any other provision not prohibited by law.

(d) If the surviving entity is a domestic entity, its public organic record, if any, must satisfy the requirements of the law of this state, except that the public organic record does not need to be signed and may omit any provision that is not required to be included in a restatement of the public organic record.

(e) A plan of merger that is signed by all the merging entities and meets all the requirements of Section 1225(b) may be delivered to the secretary of state for filing instead of articles of merger and on filing has the same effect. If a plan of merger is filed as provided in this Section 1225(a), references in this [Subchapter] 12B to articles of merger refer to the plan of merger filed under this Section 1225(e).

(f) Articles of merger are effective on the date and time of filing or the later date and time specified in the articles of merger.
If the surviving entity is a domestic entity, the merger becomes effective when the articles of merger are effective. If the surviving entity is a foreign entity, the merger becomes effective on the later of:

(1) the date and time provided by the organic law of the surviving entity; or
(2) when the articles are effective.


CROSS-REFERENCES

Approval of merger, §1222.
“Corporation” and “domestic nonprofit corporation” defined, §102.
“Eligible entity” defined, §102.
“Filing requirements,” § 160.
“Foreign nonprofit corporation” defined, §102.
Short-form merger, §1223.
“Organic law” and “organic rules” defined, § 102.
“Public organic record” defined, §102.
Voting by voting group, §§ 725 and 726.
“Voting group” defined, §102.

OFFICIAL COMMENT

The filing of articles of merger makes the transaction a matter of public record. Under Section 163, the articles are effective on the date and at the time of filing unless a later effective date is specified in the articles within the limits provided in Section 163. Under Section 163, a delayed effective date may not be later than the 90th day after the date the document is filed.

Section 1225(b)(1) and (2) – The names of foreign entities set forth in the articles of merger will generally be their names in their governing jurisdiction, except that if a foreign entity has been required to adopt a different name in order to register to do business in the adopting state, Chapter 13 requires that when the entity does business in the state it must use the name adopted for purposes of registering to do business. Engaging in a merger under Chapter 12 will be part of the business done by the entity in the state and the name of the entity set forth in the articles of merger will thus need to be the name under which the entity has registered to do business. Use of the name under which the entity has registered to do business will allow the records in the filing office to associate the registration of the entity to do business with the articles of merger.

Section 1225(b)(4) – The statement required by Section 1225(b)(4) that the plan of merger was approved by each entity in accordance with Subchapter 12B necessarily presupposes

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that the plan was approved in accordance with any valid, special requirements in the organic
rules of each merging entity.

Section 1225(b)(6) and (7) – The public organic record of a domestic surviving entity
created by the merger that is attached to the articles of merger becomes the original, officially
filed text of the public organic record of the surviving entity when the articles of merger take
effect. It is not necessary, or appropriate, to make any other filing to create the surviving entity.

Similarly, a statement of qualification for a domestic limited liability partnership created
by the merger that is attached to the articles of merger does not need to be filed separately.

Section 1225(d) – Organic laws typically require an initial filing that creates an entity to
be signed by the person serving as the incorporator or other organizer. Section 1225(d), however,
provides that the public organic record of the surviving entity does not need to be signed since it
is itself attached to a signed record.

Section 1225(d) also permits the public organic record of the surviving entity to omit any
provision that is not required to be included in a restatement of the public organic record.
Pursuant to this provision, for example, the public organic record of a business corporation
created as the surviving entity in the merger would not need to state the name and address of
each incorporator even though that information would be required by Section 2.02(a)(4) of the
Model Business Corporation Act if the corporation were being incorporated outside the context
of the merger.

Section 1225(g) – A merger in which the surviving entity is a domestic entity takes effect
when the articles of merger take effect. A merger in which the surviving entity is a foreign entity
will usually also take effect when the articles of merger take effect because the practice is to
coordinate the filings that need to be made when a merger involves both a domestic entity and
also a foreign entity so that the filings in each jurisdiction take effect at the same time. Because
of the possibility, however, that the filing in the foreign jurisdiction will take effect at a different
time, Section 1225(g) provides that the merger transaction itself will take effect at the later of (i)
when the articles of merger take effect, and (ii) when the merger takes effect under the law of the
foreign jurisdiction. That rule avoids the possibility that the merger will take effect in the
domestic jurisdiction before it takes effect in the foreign jurisdiction, which would produce the
undesirable result that the domestic entity would cease to exist before it has been merged into the
foreign entity.

It is only necessary for the filing office to record the effective date of the statement of
merger and the filing office does not need to be concerned with the effective date of the merger
itself. Persons wishing to determine the effective date of a merger involving both a domestic and
a foreign entity will be able to do so by consulting the records of the filing offices in each
jurisdiction.

Some states require notice to the attorney general of transactions involving specific types
of nonprofit entities, such as health care providers. See, e.g., Model Act for Nonprofit Healthcare
Conversion Transactions prepared by the National Association of Attorneys General. States with
such notice requirements should make sure that they are adequately integrated with the procedures in the Act.

§ 1226. EFFECT OF MERGER.

(a) When a merger under this [Subchapter] 12B becomes effective:

(1) the surviving entity continues or comes into existence;

(2) each merging entity that is not the surviving entity ceases to exist;

(3) all property of each merging entity vests in the surviving entity without transfer, reversion, or impairment;

(4) all debts, obligations, and other liabilities of each merging entity are debts, obligations, and other liabilities of the surviving entity;

(5) except as otherwise provided by law or the plan of merger, all the rights, privileges, immunities, powers, and purposes of each merging entity vest in the surviving entity;

(6) if the surviving entity exists before the merger:

(i) all its property continues to be vested in it without transfer, reversion, or impairment;

(ii) it remains subject to all its debts, obligations, and other liabilities;

and

(iii) all its rights, privileges, immunities, powers, and purposes continue to be vested in it;

(iv) its public organic record, if any, is amended to the extent provided in the articles of merger; and

(v) its private organic rules that are to be in a record, if any, are amended to the extent provided in the plan of merger;

(7) the name of the surviving entity may be substituted for the name of any merging entity that is a party to any pending action or proceeding;

(8) if the surviving entity is created by the merger:

(i) its private organic rules are effective;

(ii) if it is a filing entity, its public organic record is effective; and
(iii) if it is a limited liability partnership, its statement of qualification is effective; and

(9) the interests in each merging entity which are to be converted in the merger are converted, and the interest holders of those interests are entitled only to the rights provided to them under the plan of merger and to any appraisal rights they have under Section 1204 (appraisal rights) and the merging entity’s organic law.

(b) Except as otherwise provided in the organic law or organic rules of a merging entity, a merger under this [Subchapter] 12B does not give rise to any rights that an interest holder, governor, or third party would have upon a dissolution, liquidation, or winding up of the merging entity.

(c) When a merger under this [Subchapter] 12B becomes effective, a person that did not have interest holder liability with respect to any of the merging entities and becomes subject to interest holder liability with respect to a domestic entity as a result of the merger has interest holder liability only to the extent provided by the organic law of that entity and only for those debts, obligations, and other liabilities that are incurred after the merger becomes effective.

(d) When a merger becomes effective, the interest holder liability of a person that ceases to hold an interest in a domestic merging entity with respect to which the person had interest holder liability is subject to the following rules:

(1) The merger does not discharge any interest holder liability under the organic law of the domestic merging entity to the extent the interest holder liability was incurred before the merger became effective.

(2) The person does not have interest holder liability under the organic law of the domestic merging entity for any debt, obligation, or other liability that is incurred after the merger becomes effective.

(3) The organic law of the domestic merging entity continues to apply to the release, collection, or discharge of any interest holder liability preserved under Section 1226(d)(1) as if the merger had not occurred.

(4) The person has whatever rights of contribution from any other person as are provided by law other than this act or the organic rules of the domestic merging entity with respect to any interest holder liability preserved under Section 1226(d)(1) as if the merger had not occurred.

(e) When a merger under this [Subchapter] 12B becomes effective, a foreign entity that is the surviving entity may be served with process in this state for the collection and enforcement of any debts, obligations, or other liabilities of a domestic merging entity in accordance with applicable law.
(f) When a merger under this [Subchapter] 12B becomes effective, the registration to do business in this state of any foreign merging entity that is not the surviving entity is canceled.


CROSS-REFERENCES

“Corporation” and “domestic nonprofit corporation” defined, §102.
“Effective time and date of merger, § 163.
“Eligible entity” defined, §102.
“Foreign nonprofit corporation” defined, §102.
“Governor” defined, §102.
“Organic law” and “organic rules” defined, §102.
“Interest holder liability” defined, §102.
“Proceeding” defined, §102.

OFFICIAL COMMENT

Under Section 1226, in a merger the parties that merge become one. The survivor automatically becomes the owner of all real and personal property and becomes subject to all the liabilities, actual or contingent, of each other party to the merger. A merger is not a conveyance, transfer, or assignment. It does not give rise to claims of reverter or impairment of title based on a prohibited conveyance, transfer, or assignment. It does not give rise to a claim that a contract with a party to the merger is no longer in effect on the ground of nonassignability, unless the contract specifically addresses that issue. All pending proceedings involving either the survivor or a party whose separate existence ceased as a result of the merger are continued.

The statement in Section 1226(a)(9) regarding the rights of former interest holders is not intended to preclude an otherwise proper question concerning the validity of the merger.

Section 1226(d) sets forth the impact of a merger on interest holder liability. Section 1222(a)(9) sets forth when approval of a merger requires the consent of members who would otherwise become subject to new interest holder liability.

[Subchapter] C

INTEREST EXCHANGE

§ 1230. Interest exchange authorized.
§ 1231. Plan of interest exchange.
§ 1232. Approval of interest exchange.
§ 1233. Amendment or abandonment of plan of interest exchange.
§ 1234. Articles of interest exchange; effective date of interest exchange.
§ 1235. Effect of interest exchange.
§ 1230. INTEREST EXCHANGE AUTHORIZED.

(a) Except as otherwise provided in this section, by complying with [Subchapter] 12A (preliminary provisions) and this [Subchapter] 12C:

(1) a domestic nonprofit corporation may acquire all of one or more classes or
series of interests of a domestic or foreign nonprofit corporation or eligible entity in exchange for
interests, securities, obligations, money, other property, rights to acquire interests, or securities,
or any combination of the foregoing; or

(2) all of one or more class of memberships of a domestic membership
corporation may be acquired by another entity in exchange for interests, securities, obligations,
money, other property, rights to acquire interests or securities, or any combination of the
foregoing.

(b) Except as otherwise provided in this Section 1120, by complying with the
provisions of [Subchapter] 12A and this [Subchapter] 12C applicable to foreign eligible entities,
a foreign eligible entity may be the acquiring or acquired entity in an interest exchange under this
[Subchapter] 12C if the interest exchange is authorized by the law of the foreign entity’s
governing jurisdiction.

(c) If a protected agreement of a domestic nonprofit corporation contains a provision
that applies to a merger of the corporation but does not refer to an interest exchange, the
provision applies to an interest exchange in which the corporation is the acquired entity as if the
interest exchange were a merger until the provision is amended after the enactment date.

(d) If the organic law or organic rules of a domestic eligible entity do not provide
procedures for the approval of an interest exchange, a plan of interest exchange may nonetheless
be adopted and approved by the unanimous consent of all of the interest holders of the eligible
entity, and the interest exchange may thereafter be effected as provided in the other provisions of
[Subchapter] 12A and this [Subchapter] 12C;

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 11.03(a) – (c), and (h). Cf. Model Business
Corporation Act (2016 Revision), § (a) – (c).

OFFICIAL COMMENT

Subchapter 12C does not restrict or limit on terms or conditions of an interest exchange,
except for the requirement in Section 1230(a) that the acquiring entity must acquire all the
interests of the acquired class or series of interests. However, interests of the acquired class or
series owned at the effective time of the interest exchange by the acquiring entity or any of its
parents or their wholly owned subsidiaries may be excluded from the exchange.

Section 1230 does not apply, of course, to the acquisition of a nonprofit corporation
without members. In such a case, control of the corporation can be transferred by means of an
amendment to its articles of incorporation or bylaws changing the manner in which the directors
are selected.

§ 1231. PLAN OF INTEREST EXCHANGE.

(a) A domestic nonprofit corporation may be the acquired entity in an interest exchange under this [Subchapter] 12C by approving a plan of interest exchange. The plan must be in a record and contain:

1. the name of the corporation;
2. the name, governing jurisdiction, and type of entity of the acquiring entity;
3. the manner of converting the memberships in the corporation into interests, securities, obligations, money, other property, rights to acquire interests or securities, or any combination of the foregoing;
4. any proposed amendments to:
   (i) the articles of incorporation of the corporation; and
   (ii) the bylaws of the corporation;
5. the other terms and conditions of the interest exchange; and
6. any other provision required by the law of this state or the articles or bylaws of the corporation.

(b) In addition to the requirements of Section 1231(a), a plan of interest exchange may contain any other provision not prohibited by law.

(c) Terms of a plan of interest exchange may be made dependent on facts objectively ascertainable outside the plan in accordance with Section 105 (extrinsic facts in filed record).

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 11.03(d) and (f). Cf. Model Business Corporation Act (2016 Revision), § 11.03(d) and (e).

CROSS-REFERENCES

Abandonment of interest exchange, § 1233.
Approval of plan, § 1232.
Articles of interest exchange, § 1234.
Classes of memberships, § 601.
Effect of interest exchange, § 1235.

OFFICIAL COMMENT
Whether and on what terms a foreign nonprofit corporation or a foreign eligible entity is authorized to enter into a membership exchange with a domestic nonprofit corporation is a matter that is governed by the laws under which that corporation or eligible entity is organized or by which it is governed, not by Subchapter 12C. Therefore, Section 1231 applies only to adoption of a plan of membership exchange by a domestic nonprofit corporation (or a domestic eligible entity as provided in Section 1230(d)).

If the organic law of a domestic eligible entity (including a domestic business corporation) does not expressly authorize it to engage in a membership exchange with a nonprofit corporation, the domestic eligible entity will nonetheless have that power pursuant to Section 1230(a). If the organic law of a domestic eligible entity provides procedures for the adoption, approval, and effectuation of a merger with any type of entity, but not for a membership exchange, the merger procedures will apply to a membership exchange with a nonprofit corporation. If the organic law of a domestic eligible entity does not provide procedures for any type of merger or interest exchange, the procedures of this chapter will apply pursuant to Section 1230(d). If the persons who manage the business and affairs of an eligible entity are the same as its interest holders, then a single approval by those persons will be sufficient under Section 1231.

The terms of a merger involving a nonprofit corporation frequently provide for a contribution to be made by another party either to the nonprofit corporation itself or to a related entity. It is anticipated that a similar practice will develop with respect to membership exchanges, and thus Section 1231(b) permits that type of provision to be included in a plan of membership exchange.

§ 1232. APPROVAL OF INTEREST EXCHANGE.

(a) In the case of a domestic nonprofit corporation that is the acquired entity in an interest exchange, the plan of interest exchange must be adopted in the following manner:

(1) The plan of interest exchange must first be adopted by the board of directors. The board may set conditions for the approval of the plan of interest exchange by the members or the effectiveness of the plan of interest exchange. If the corporation is the acquired entity and does not have any members entitled to vote on the interest exchange, a plan of interest exchange is adopted by the corporation when it has been adopted by the board.

(2) Except as provided in Section 1232(a)(1), the plan of interest exchange shall then be approved by the members. In submitting the plan of interest exchange to the members for approval, the board shall recommend that the members approve the plan unless the board makes a determination that because of conflicts of interest or other special circumstances it should not make such a recommendation, in which case the board must inform the members of the basis for its so proceeding.
(3) If the plan of interest exchange is required to be approved by the members, and if the approval is to be given at a meeting, the corporation shall notify each member entitled to vote of the meeting of members at which the plan is to be submitted for approval. The notice must state that the purpose, or one of the purposes, of the meeting is to consider the plan and must contain or be accompanied by a copy or summary of the plan.

(4) Unless the articles of incorporation, or the board of directors acting pursuant to Section 1232(a)(1), require a greater vote or a greater quorum, approval of the plan of interest exchange requires the approval of the members at a meeting at which a quorum exists consisting of a majority of the votes entitled to be cast on the plan, and, if any class of memberships is entitled to vote as a separate group on the plan of interest exchange, the approval of each such separate voting group at a meeting at which a quorum of the voting group is present consisting of a majority of the votes entitled to be cast on the interest exchange by that voting group.

(5) Subject to Section 1232(a)(6), separate voting by voting groups on a plan of interest exchange is required:

   (i) by each class of memberships that:

      (A) are included in the exchange, with each class constituting a separate voting group; or

      (B) are entitled to vote as a separate group on a provision in the plan that constitutes a proposed amendment to the articles or bylaws that requires action by separate voting groups under Section 904 (voting on amendments by voting groups) or Section 922 (bylaw amendments requiring member approval); or

   (ii) if the voting group is entitled under the articles of incorporation or bylaws to vote as a voting group to approve a plan of interest exchange.

(6) The articles or bylaws may expressly limit or eliminate the separate voting rights provided in Section 1232(a)(5) (i)(A) as to any class of memberships, except when the plan of interest exchange includes what is or would be in effect an amendment subject to Section 1232(a)(5)(i)(B).

(7) Unless the articles of incorporation or bylaws otherwise provide:

   (i) approval of a plan of interest exchange by the members of a domestic nonprofit corporation is not required if the corporation is the acquiring entity in the interest exchange; and

   (ii) memberships that will not be exchanged under the plan of interest exchange are not entitled to vote on the plan.
If as a result of an interest exchange one or more members of a domestic nonprofit corporation would become subject to new interest holder liability, approval of the plan of interest exchange requires the signing in connection with the interest exchange, by each such member, of a separate consent in a record to become subject to such new interest holder liability, unless in the case of a member that already has interest holder liability with respect to the corporation:

(i) the new interest holder liability is with respect to a domestic or foreign nonprofit corporation (which may be a different or the same domestic corporation in which the person is a member); and

(ii) the terms and conditions of the new interest holder liability are substantially identical to those of the existing interest holder liability (other than for changes that eliminate or reduce such interest holder liability).

In addition to the adoption and approval of the plan of interest exchange by the board of directors and members as required by this section, the plan of interest exchange must also be approved in a record by any person or group of persons whose approval is required under Section 930 (approval by third persons) to amend the articles of incorporation or bylaws.

(b) See Section 1203 (required approvals).


CROSS-REFERENCES

Abandonment of interest exchange, § 1233.
Director standards of conduct, § 830.
Director standards of liability, § 831.
Notice generally, § 103.
Notice of members meeting, § 705.
“Record” defined, § 102.
Supermajority quorum and voting requirements, § 726.
Voting by voting groups generally, §§ 724 and 725.
Voting by voting group on amendment of articles of incorporation, § 904.
Voting entitlement of members generally, § 721.
“Voting group” defined, § 102.
“Voting power” defined, § 102.

OFFICIAL COMMENT

Under Section 1232, a plan of merger or interest exchange must be adopted by the board of directors. Thereafter, the board must submit the plan to the members for their approval, except as provided in Section 1232(a)(1). The functions of the board of directors under Section 1232
may be vested by the articles of incorporation or bylaws in a designated body either to the
exclusion of, or jointly with, the board of directors.

Section 1223(a)(2) requires the board of directors of a membership corporation, after
having adopted the plan of interest exchange, to submit the plan to the members for approval,
except as provided in Section 1232(a)(1). When submitting the plan, the board of directors must
make a recommendation to the members that the plan be approved, unless the board of directors
makes a determination that because of conflicts of interest or other special circumstances it
should make no recommendation. For example, the board of directors may make such a
determination where there is not a sufficient number of directors free of a conflicting interest to
approve the transaction or because the board of directors is evenly divided as to the merits of a
transaction but is able to agree that members should be permitted to consider the transaction. If
the board of directors makes such a determination, it must describe the conflict of interest or
special circumstances, and communicate the basis for the determination, when submitting the
plan to the members. The exception for conflicts of interest or other special circumstances is
intended to be sparingly available. Generally, members should not be asked to act on an interest
exchange in the absence of a recommendation by the board of directors. The exception is not
intended to relieve the board of directors of its duty to consider carefully the proposed
transaction and the interests of members.

Section 1231(a)(1) permits the board of directors to condition its submission of a plan of
interest exchange on any basis. Among the conditions that a board might impose are that the plan
will not be deemed approved unless it is approved by a specified vote of the members (which
may be higher than the vote that would otherwise be required), or by one or more specified
classes of members, voting as a separate voting group, or by a specified percentage of
disinterested members. The board is not limited, however, to conditions of these types. If the
members object to a condition imposed by the board, their remedy is to change the members of
the board.

Section 1231(a)(4) provides that approval of a plan of interest exchange requires approval
of the members at a meeting at which a quorum consisting of a majority of the votes entitled to
be cast on the plan exists and, if any class of members are entitled to vote as a separate group on
the plan, the approval of each such separate group at a meeting at which a quorum consisting of
at least a majority of the votes entitled to be cast on the plan by that class exists. If a quorum is
present, then under Sections 724 and 725 the plan will be approved if more votes are cast in
favor of the plan than against it by the voting group or separate voting groups entitled to vote on
the plan.

In lieu of approval at a member meeting, approval can be given by the consent of the
members entitled to vote on the merger or membership exchange, under the procedures set forth
in Section 704.

Section 1231(a)(8) requires any member who will become subject to owner liability to
sign a record consenting to becoming subject to owner liability, which consent must be separate
from the plan of interest exchange. Although the transactions that produce this result will be
infrequent, Section 1231(a)(8) is an important protective provision in those instances where
owner liability may arise. An example of such a transaction is a merger of a nonprofit
corporation into an unincorporated nonprofit association in a state where members of such an
association are not protected from personal liability for debts or obligations of the association.

§ 1233. AMENDMENT OR ABANDONMENT OF PLAN OF INTEREST
EXCHANGE.

(a) A plan of interest exchange may be amended only with the consent of each party
to the plan, except as otherwise provided in the plan and before articles of interest exchange have
taken effect.

(b) A domestic acquired nonprofit corporation may approve an amendment of a plan
of interest exchange:

1. in the same manner as the plan was approved, if the plan does not provide
   for the manner in which it may be amended; or

2. by its board of directors or members in the manner provided in the plan,
   but a member that was entitled to vote on or consent to approval of the interest exchange is
   entitled to vote on or consent to any amendment of the plan that will change:

   i. the amount or kind of interests, securities, obligations, money,
      other property, rights to acquire interests, or securities, or any combination of the foregoing, to
      be received by any of the interest holders of the acquired entity under the plan;

   ii. the articles of incorporation or bylaws that will be in effect
      immediately after the interest exchange becomes effective, except for changes that do not require
      approval of the members under this act, the articles or bylaws; or

   iii. any other terms or conditions of the plan, if the change would
      adversely affect the member in any material respect.

(c) After a plan of interest exchange has been approved and before articles of interest
exchange are effective, the plan may be abandoned as provided in the plan. Unless prohibited by
the plan, a domestic acquired nonprofit corporation may abandon the plan in the same manner as
the plan was approved.

(d) If a plan of interest exchange is abandoned after articles of interest exchange have
been delivered to the secretary of state for filing and before the articles are effective, articles of
abandonment, signed by the acquired entity, must be delivered to the secretary of state for filing
before the articles of interest exchange are effective. The articles of abandonment takes effect on
filing, and the interest exchange is abandoned and does not become effective. The articles of
abandonment must contain:

1. the name of the domestic acquired nonprofit corporation;
the date on which the articles of interest exchange were filed by the secretary of state; and

a statement that the interest exchange has been abandoned in accordance with this section.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), §§ 11.03(e) and 11.08. Cf. Model Business Corporation Act (2016 Revision), §§ 11.03(f) and 11.08.

CROSS-REFERENCES

approval of interest exchange, § 1232.
“Corporation” and “domestic nonprofit corporation” defined, § 102.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Filing requirements, § 160.

OFFICIAL COMMENT

Under Section 1223, unless otherwise provided in the plan of interest exchange, a party to an interest exchange may abandon the transaction without member approval, even though the transaction has been previously approved by the party’s members. The power of a party under Section 1223 to abandon a transaction without member approval does not affect any contract rights that other parties may have.

The functions of the board of directors under this section may be vested by the articles of incorporation or bylaws in a designated body either to the exclusion of, or jointly with, the board of directors.

§ 1234. ARTICLES OF INTEREST EXCHANGE; EFFECTIVE DATE OF INTEREST EXCHANGE.

(a) If a domestic nonprofit corporation, or a domestic eligible entity whose organic law does not provide for interest exchanges, is the acquired entity, articles of interest exchange must be signed by the acquired entity and delivered to the secretary of state for filing.

(b) Articles of interest exchange must contain:

1. the name of the acquired entity;
2. the name, governing jurisdiction, and type of entity of the acquiring entity;
(3) if the articles of interest exchange are not to be effective upon filing, the later date and time on which they will become effective determined in accordance with Section 163 (effective time and date of filing);

(4) a statement that the plan of interest exchange was approved by the acquiring entity in accordance with this [Subchapter] 12C; and

(5) any amendments to the acquired entity’s public organic record approved as part of the plan of interest exchange.

(c) In addition to the requirements of Section 1234(b), articles of interest exchange may contain any other provision not prohibited by law.

(d) A plan of interest exchange that is signed by the acquired entity and meets all the requirements of Section 1234(b) may be delivered to the secretary of state for filing instead of articles of interest exchange and on filing has the same effect. If a plan of interest exchange is filed as provided in this Section 1234(d), references in this [Subchapter] 12C to articles of interest exchange refer to the plan of interest exchange filed under this Section 1234(d).

(e) Articles of interest exchange are effective on the date and time of filing or the later date and time specified in the articles.

(f) An interest exchange in which the acquired entity is a domestic nonprofit corporation becomes effective when the articles of interest exchange are effective.


CROSS-REFERENCES

Approval of interest exchange, § 1232.
Filing fees, § 162.
Filing requirements, § 160.
Voting by voting group, §§ 724 and 725.
“Voting group” defined, § 102.

OFFICIAL COMMENT

The filing of articles of interest exchange makes the transaction a matter of public record. The effective time of the articles is the effective time of their filing, unless otherwise specified. Under Section 163, a document may specify a delayed effective time and date, and if it does so the document become effective at the time and date specified, except that a delayed effective date may not be later than the 90th day after the date the document is filed.
When the articles of interest exchange are effective under Section 1234(e), the interest exchange transaction occurs under Section 1234(f) if the acquired entity is a domestic entity.

Some states require notice to the attorney general of transactions involving specific types of nonprofit entities, such as health care providers. See, e.g., Model Act for Nonprofit Healthcare Conversion Transactions prepared by the National Association of Attorneys General. States with such notice requirements should make sure that they are adequately integrated with the procedures in the act.

§ 1235. EFFECT OF INTEREST EXCHANGE.

(a) When an interest exchange in which a domestic nonprofit corporation, or a domestic eligible entity whose organic law does not provide for interest exchanges, is the acquired entity becomes effective:

(1) the interests in the acquired entity that are the subject of the interest exchange are converted, and the holders of those interests are entitled only to the rights provided to them under the plan of interest exchange;

(2) the acquiring entity becomes the interest holder of the interests in the acquired entity stated in the plan of interest exchange to be acquired by the acquiring entity;

(3) the public organic documents of the acquired entity is amended to the extent provided in the articles of interest exchange; and

(4) the private organic rules of the acquired entity are amended to the extent provided in the plan of interest exchange.

(b) Except as otherwise provided in this act or the organic rules of the acquired entity, the interest exchange does not give rise to any rights that an interest holder or third party would have upon a dissolution, liquidation, or winding up of the acquired entity.

(c) When an interest exchange becomes effective, a person that did not have interest holder liability with respect to the acquired entity and becomes subject to interest holder liability with respect to a domestic entity as a result of the interest exchange has interest holder liability only to the extent provided by the organic law of the entity and only for those debts, obligations, and other liabilities that are incurred after the interest exchange becomes effective.

(d) When an interest exchange becomes effective, the interest holder liability of a person that ceases to hold an interest in the acquired entity with respect to which the person had interest holder liability is subject to the following rules:

(1) The interest exchange does not discharge any interest holder liability under this [Act] to the extent the interest holder liability was incurred before the interest exchange became effective.
(2) The person does not have interest holder liability under this [Act] for any
debt, obligation, or other liability that is incurred after the interest exchange becomes effective.

(3) This [Act] continues to apply to the release, collection, or discharge of any
interest holder liability preserved under Section 1235(d)(1) as if the interest exchange had not
occurred.

(4) The person has whatever rights of contribution from any other person as
are provided by law other than this [Act] or the organic rules of the acquired entity with respect
to any interest holder liability preserved under Section 1235(d)(1) as if the interest exchange had
not occurred.


CROSS-REFERENCES

“Corporation” and “domestic nonprofit corporation” defined, § 102.
Effective time and date of interest exchange, § 163.
“Eligible entity” defined, § 102.
“Foreign nonprofit corporation” defined, § 102.
“Governor” defined, § 102.
“Organic law” and “organic rules” defined, § 102.
“Interest holder liability” defined, § 102.
“Proceeding” defined, § 102.

OFFICIAL COMMENT

In contrast to a merger, an interest exchange does not vest in the acquiring entity the
assets of the acquired entity, or render the acquiring entity liable for the liabilities of the acquired
entity. The statement in Section 1235(a)(1) regarding the rights of former interest holders is not
intended to preclude an otherwise proper question concerning the validity of the interest
exchange.

11 by reason of entering into an agreement that is governed by this chapter.

Section 1235(d) sets forth the impact of an interest exchange on interest holder liability.
Section 1232(a)(8) sets forth when approval of an interest exchange requires the consent of
members who would otherwise become subject to interest holder liability.

[Subchapter] D
DOMESTICATION
§ 1240. Domestication.
§ 1241. Plan of domestication.
§ 1242 Approval of domestication.
§ 1240. DOMESTICATION

(a) By complying with the provisions of [Subchapter] 12A (preliminary provisions) and this [Subchapter] 12D applicable to foreign nonprofit corporations, a foreign nonprofit corporation may become a domestic nonprofit corporation, if the domestication is permitted by the organic law of the foreign corporation.

(b) By complying with the provisions of [Subchapter] 12A and this [Subchapter] 12D, a domestic nonprofit corporation may become a foreign nonprofit corporation pursuant to a plan of domestication, if the domestication is permitted by the organic law of the foreign corporation.

(c) If a protected agreement of a domestic domesticating nonprofit corporation in effect immediately before the domestication becomes effective contains a provision applying to a merger of the corporation and the agreement does not refer to a domestication of the corporation, the provision applies to a domestication of the corporation as if the domestication were a merger until such time as the provision is first amended after the enactment date.

(d) See Sections 1202 (excluded transactions) and 1203 (required approvals).

Source Note: Model Entity Transactions Act (2007) (Last Amended 2013), § 501. Cf. Model Nonprofit Corporation Act, 3rd Ed. (2008), § 9.20(a), (b), and (f); and Model Business Corporation Act (2016 Revision), § 9.20(a), (b), and (f).

CROSS-REFERENCES

Abandonment of domestication, § 1244.
Approval of plan, § 1242.
Articles of domestication, § 1243.
“Domestic nonprofit corporation” defined, § 102.
Effect of domestication, § 1245.
“Enactment date” defined, § 1201.
Excluded transactions, § 1202.
“Interest holder liability” defined, § 102.
“Foreign nonprofit corporation” defined, § 102.
“Organic law” defined, § 102.
“Protected agreement” defined, § 1201.
Required approvals, § 1203.
“Voting group” defined, § 102.

OFFICIAL COMMENT
Subchapter 12D authorizes a foreign nonprofit corporation to become a domestic nonprofit corporation and a domestic nonprofit corporation to become a foreign nonprofit corporation. In each case, the domestication is authorized only if the laws of the foreign jurisdiction permit it. Whether and on what terms a foreign corporation is authorized to domesticate in this state are issues governed by the organic law of the foreign corporation, not by Subchapter 12D. A foreign corporation is not required to have a valid registration to do business in this state under Chapter 13 to domesticate in this state.

A domestication authorized by Subchapter 12D differs from a conversion under Subchapter 12E because a domestication requires that the domesticating entity be the same type of entity as the domesticated entity. In a conversion, by contrast, the converting entity changes its type.

Section 1240(c) provides special rules for “protected agreements”—certain documents and agreements in effect before the “enactment date” as defined in Section 1201.

§ 1241. PLAN OF DOMESTICATION

(a) A domestic nonprofit corporation may become a foreign nonprofit corporation by approving a plan of domestication. The plan of domestication must include:

(1) the name of the domesticating corporation;
(2) the name and governing jurisdiction of the domesticated corporation;
(3) the manner and basis of converting the memberships, if any, of the domesticating corporation into memberships, obligations, rights to acquire memberships, cash, other property, or any combination of the foregoing;
(4) the proposed articles of incorporation and bylaws of the domesticated corporation; and
(5) the other terms and conditions of the domestication.

(b) In addition to the requirements of Section 1241(a), a plan of domestication may contain any other provision not prohibited by law.

(c) The terms of a plan of domestication may be made dependent upon facts objectively ascertainable outside the plan in accordance with Section 105 (extrinsic facts in filed record).

Source Note: Model Entity Transactions Act (2007) (Last Amended 2013), § 502. Cf. Model Nonprofit Corporation Act, 3rd Ed. (2008), § 9.20(c) and (e); and Model
OFFICIAL COMMENT

Under Section 1241(a)(4), a domestic nonprofit corporation’s plan of domestication must include the domesticated corporation’s proposed articles of incorporation and bylaws, which should comply with the organic law of the foreign jurisdiction into which it is domesticating. In the case of a domestic corporation domesticating into a foreign jurisdiction, the Act places no separate limitations on the provisions that the proposed articles of incorporation and bylaws may contain, and they may be substantially identical to or completely different from those of the domesticating corporation. However, the content of the proposed articles may affect the approvals required for the plan of domestication. See the approval requirements in Section 1242(a)(6) with respect to certain changes in the articles of incorporation, and Section 1242(a)(7) with respect to interest holder liability with respect to the domesticated corporation.

§ 1242. APPROVAL OF DOMESTICATION

(a) If a domestic nonprofit corporation is to be the domesticating corporation, the plan of domestication must be adopted in the following manner:

(1) The plan of domestication must first be adopted by the board of directors. The board may set conditions for approval of the plan of domestication by the members or the effectiveness of the plan of domestication. If the domesticating corporation does not have any members entitled to vote on the domestication, a plan of domestication is adopted by the corporation when it has been adopted by the board of directors pursuant to this Section 1242(a)(1).

(2) Except as provided in Section 1242(a)(1), the plan of domestication must then be approved by the members. In submitting the plan of domestication to the members for approval, the board of directors must recommend that the members approve the plan, unless the board of directors makes a determination that because of conflicts of interest or other special circumstances it should not make such a recommendation, in which case the board shall inform the members of the basis for its so proceeding.

(3) If the plan of domestication is required to be approved by the members, and if the approval is to be given at a meeting, the corporation must notify each member entitled to vote of the meeting of the members at which the plan of domestication is to be submitted for approval. The notice must state that the purpose, or one of the purposes, of the meeting is to consider the plan of domestication and must contain or be accompanied by a copy or summary of the plan. The notice must include or be accompanied by a copy of the articles of incorporation and the bylaws as they will be in effect immediately after the domestication.

(4) Unless the articles of incorporation or bylaws, or the board of directors acting pursuant to Section 1242(a)(i), require a greater vote or a greater quorum, approval of the plan of domestication requires the approval of the members at a meeting at which a quorum exists.
consisting of a majority of the votes entitled to be cast on the plan, and, if any class of membership
is entitled to vote as a separate group on the plan of merger, the approval of each class of members
voting as a separate voting group at a meeting at which a quorum of the voting group exists
consisting of a majority of the votes entitled to be cast on the plan by that voting group.

(5) Subject to Section 1242(a)(6), separate voting by voting groups on a plan
of domestication is required:

(i) by each class of memberships that:

(A) one to be converted under the plan of domestication into
security interests, obligations, rights to acquire securities or interests, cash, other property, or any
combination of the foregoing; or

(B) is entitled to vote as a separate group on a provision in the
plan that constitutes a proposed amendment to the articles or bylaws of the domesticated
corporation that requires action by separate voting groups under Section 904 (voting on
amendments by voting groups) or Section 922 (bylaw amendments requiring member approval); or

(ii) if the voting group is entitled under the articles or bylaws to vote
as a group to approve a plan of domestication.

(6) The articles or bylaws may expressly limit or eliminate the separate voting
rights provided in Section 1242(a)(5)(i)(A) as to any class of members, except when the plan
includes what would be in effect an amendment subject to Section 1242(a)(5)(i)(B).

(7) If as a result of a domestication one or more members of the domesticating
corporation would become subject to new interest holder liability, approval of the plan of
domestication requires the signing in connection with the domestication, by each such member,
of a separate consent in a record to become subject to such new interest holder liability, unless in
the case of a member that already has interest holder liability with respect to the domesticating
corporation, the terms and conditions of the new interest holder liability with respect to the
domesticated corporation are substantially identical to those of the existing interest holder
liability (other than for changes that eliminate or reduce such interest holder liability).

(8) In addition to the adoption and approval of the plan of domestication by
the board of directors and members as required by this section, the plan of domestication must
also be approved in a record by any person or group of persons whose approval is required under
Section 930 (approval by third persons) to amend the articles or bylaws.

(b) See Section 1203 (required approvals).

Source Note: Model Entity Transactions Act (2007) (Last
Amended 2013), § 503. Cf. Model Nonprofit Corporation
Act, 3rd Ed. (2008), § 9.21; and Model Business
Corporation Act (2016 Revision), § 9.21.
Section 1242 sets forth the rules for adoption and approval of a plan of domestication of a domestic nonprofit corporation into a foreign jurisdiction. The manner in which the domestication of a foreign corporation into this state must be adopted and approved will be controlled by the organic law of the foreign corporation.

When submitting a plan of domestication to the members, the board of directors generally must recommend the transaction. The board, however, might exercise the exception under Section 1242(a)(2) where the number of directors having a conflicting interest makes it inadvisable for the board to recommend the domestication or where the board is evenly divided as to the merits of the domestication but is able to agree that the members should be permitted to consider it.

Section 1242(a)(1) permits the board of directors to condition its submission of a plan of domestication to the members or the effectiveness of the plan of domestication. Among the conditions that a board of directors might impose are that the plan will not be deemed approved unless it is approved by a specified vote of the members, or by one or more specified classes or series of memberships, voting as a separate voting group, or by a specified percentage of disinterested members.

Section 1242(a)(4) sets forth quorum and voting requirements applicable to a member vote to approve a plan of domestication. Section 1242(a)(4) also provides that each class or series of members has a right to vote on a plan of domestication as a separate voting group.

Section 1242(a)(6) permits the articles of incorporation or bylaws to expressly limit or eliminate separate voting as a voting group for any class or series of memberships on a plan of domestication unless the articles of incorporation of the foreign domesticated corporation into which the corporation would be domesticated include what would be an amendment requiring separate group voting under Section 904 or 922 if it had been done as an amendment of that domestic corporation’s articles or bylaws.

Section 1242(a)(7) applies only in situations where a member of a domestic nonprofit corporation is becoming subject to “interest holder liability,” as defined in Section 102, with respect to the domesticated corporation. Approval of a domestication that would have such a result generally requires the written consent of each such member who becomes subject to such interest holder liability. The exception is the limited case where the member has interest holder...
liability with respect to the domesticating corporation, and the terms and conditions of the
member’s interest holder liability with respect to the domesticated corporation are substantially
identical to those existing prior to the domestication.

§ 1243. AMENDMENT OR ABANDONMENT OF PLAN OF DOMESTICATION;
ABANDONMENT

(a) A plan of domestication of a domestic nonprofit corporation may be amended,
except as otherwise provided in the plan and before articles of domestication have taken effect.

(b) A domestic nonprofit corporation may approve an amendment of a plan of
domestication:

1. in the same manner as the plan was approved, if the plan does not provide
   for the manner in which it may be amended; or

2. in the manner provided in the plan, except that a member that was entitled
to vote on or consent to approval of the plan is entitled to vote on or consent to any amendment
   of the plan that will change:

   (i) the amount or kind of memberships, securities, obligations, money
       rights to acquire memberships, securities, money, other property, or any combination of the
       foregoing, to be received by any of the members of the domesticating corporation under the plan;

   (ii) the articles of incorporation or bylaws of the domesticated
       corporation that will be in effect immediately after the domestication becomes effective, except
       for changes that do not require approval of the members of the domesticated corporation under
       its organic law or its proposed articles or bylaws as set forth in the plan; or

   (iii) any of the other terms or conditions of the plan, if the change
       would adversely affect the member in any material respect.

(b) After a plan of domestication has been approved and before the articles of
domestication have become effective, the plan may be abandoned as provided in the plan. Unless
prohibited by the plan, a domestic nonprofit corporation may abandon the plan in the same
manner as the plan was approved by the corporation without action by its members in
accordance with any procedures set forth in the plan or, if no such procedures are set forth in the
plan, in the manner determined by the board of directors.

(c) If a domestication is abandoned after articles of domestication have been
delivered to the secretary of state for filing but before the articles are effective, articles of
abandonment, signed by the domesticating nonprofit corporation, must be delivered to the
secretary of state for filing before the articles of domestication are effective. The articles of
abandonment take effect upon filing, and the domestication is abandoned and does not become
effective. The articles of abandonment must contain:
§ 1244. ARTICLES OF DOMESTICATION; EFFECTIVE DATE

(a) Articles of domestication must be signed by the domesticating corporation and delivered to the secretary of state for filing.

(b) The articles of domestication must contain:

1. the name and governing jurisdiction of the domesticating corporation;
2. the name and governing jurisdiction of the domesticated corporation; and
3. if the domesticating corporation is a domestic nonprofit corporation, a statement that the plan of domestication was approved in accordance with this [Subchapter] 12D or, if the domesticating corporation is a foreign nonprofit corporation, a statement that the domestication was approved in accordance with its organic law.
If the domesticated corporation is a domestic nonprofit corporation, its articles of incorporation, as an attachment, except that provisions that would not be required to be included in restated articles of incorporation may be omitted from the articles of the domesticated corporation and the articles do not need to be signed.

In addition to the requirements of Section 1244(b), articles of domestication may contain any other provision not prohibited by law.

If the domesticated corporation is a domestic nonprofit corporation, the domestication becomes effective when the articles of domestication are effective. If the domesticated corporation is a foreign nonprofit corporation, the domestication becomes effective on the later of:

1. the date and time provided by the organic law of the domesticated corporation; or
2. when the articles are effective.


CROSS-REFERENCES

“Domestic nonprofit corporation” defined, § 102.
“Domesticated corporation” defined, §1201.
“Domesticating corporation” defined, §1201.
Effect of domestication, §1245.
Filing requirements, § 160.
“Organic law” defined, §102.
Required approvals, § 1203.

OFFICIAL COMMENT

The filing of articles of domestication makes the domestication a matter of public record. Where the domesticated corporation is a domestic corporation, it also makes its articles of incorporation a matter of public record.

The requirements for filing are set forth in Section 160. Under Section 163, the articles of domestication are effective on the date and at the time of filing unless a later effective date is specified in the articles within the limits provided in Section 163. Under Section 163, a delayed effective date may not be later than the 90th day after the date the document is filed.

When the articles of domestication are effective under Section 1244(e), the domestication transaction occurs if the domesticated entity is a domestic nonprofit corporation. A
domestication in which the domesticated entity is a foreign nonprofit corporation will usually also take effect when the articles of domestication take effect because the best practice will be to coordinate the filings that need to be made in each jurisdiction so that they take effect at the same time. Because of the possibility, however, that the filing in the foreign jurisdiction will take effect at a different time, Section 1244(e) provides that the domestication transaction itself will take effect at the later of (i) when the articles of domestication take effect, and (ii) when the domestication takes effect under the law of the foreign jurisdiction. This rule avoids the possibility that the domestication will take effect in the domestic jurisdiction before it takes effect in the foreign jurisdiction, which would produce the undesirable result that the domesticating domestic nonprofit corporation would cease to appear as an active entity on the records of this state before it appears as its active domesticated self on the records of the foreign jurisdiction.

It is only necessary for the filing office to record the effective date of the articles of domestication and the filing office does not need to be concerned with the effective date of the domestication itself. Persons wishing to determine the effective date of a domestication will be able to do so by consulting the records of the filing offices in each jurisdiction.

§ 1245. EFFECT OF DOMESTICATION

(a) When a domestication becomes effective:

(1) all property owned by, and every contract right possessed by, the domesticating corporation are the property and contract rights of the domesticated corporation without transfer, reversion, or impairment;

(2) all debts, obligations, and other liabilities of the domesticating corporation remain the debts, obligations, and other liabilities of the domesticated corporation;

(3) the name of the domesticated corporation may but need not be substituted for the name of the domesticating corporation in any pending proceeding;

(4) the articles of incorporation and bylaws of the domesticated corporation become effective;

(5) the memberships of the domesticating corporation are reclassified into memberships, obligations, rights to acquire memberships, cash or other property in accordance with the terms of the domestication, and the members of the domesticating corporation are entitled only to the rights provided to them by those terms; and

(6) the domesticated corporation is:

(i) incorporated under and subject to the current organic law of the domesticated corporation;
(ii) the same corporation without interruption as the domesticating corporation; and

(iii) deemed to have been incorporated on the date the domesticating corporation was originally incorporated.

(b) Except as otherwise provided in the organic law or organic rules of a foreign nonprofit corporation that is the domesticating corporation, the interest holder liability of a member in a foreign corporation that is domesticated into this state who had interest holder liability in respect of the domesticating corporation before the domestication becomes effective shall be as follows:

(1) The domestication does not discharge that prior interest holder liability with respect to any interest holder liabilities that arose before the domestication becomes effective.

(2) The provisions of the organic law of the domesticating corporation shall continue to apply to the collection or discharge of any interest holder liabilities preserved by Section 1245(b)(1), as if the domestication had not occurred.

(3) The member shall have such rights of contribution from other persons as are provided by the organic law of the domesticating corporation with respect to any interest holder liabilities preserved by Section 1245(b)(1), as if the domestication had not occurred.

(4) The member shall not, by reason of such prior interest holder liability, have interest holder liability with respect to any interest holder liabilities that are incurred after the domestication becomes effective.

(c) A member who becomes subject to interest holder liability in respect of the domesticated corporation as a result of the domestication shall have such interest holder liability only in respect of interest holder liabilities that arise after the domestication becomes effective.

(d) A domestication does not constitute or cause the dissolution of the domesticating corporation.


CROSS-REFERENCES

“Domesticated corporation” defined, § 1201.
“Domesticating corporation” defined, § 1201.
“Interest holder liability” defined, § 102.
“Organic law” and “organic rules” defined, § 102.
OFFICIAL COMMENT

The domesticated corporation is the same entity as the domesticating corporation, and it continues without interruption. It becomes a nonprofit corporation in the resulting jurisdiction with the same status as if it had been originally incorporated there. The domesticated corporation has all of the powers, privileges, and rights granted to corporations originally incorporated in that jurisdiction and will be subject to all of the duties, liabilities, and limitations imposed on nonprofit corporations in that jurisdiction. Thus, a domestication is not a conveyance, transfer or assignment. It does not give rise to claims of reverter or impairment of title based on a prohibited conveyance, transfer or assignment. Nor does it give rise to a claim that a contract with the corporation is no longer in effect on the ground of nonassignability, unless the contract specifically provides that it does not survive domestication. See, however, Section 1240(c) with respect to special rules regarding protected agreements. All pending proceedings involving the domesticating corporation are continued.

Section 1245(b) preserves the interest holder liability of members of the domesticating foreign corporation only for interest holder liabilities to the extent they arise before the domestication becomes effective. Interest holder liability is not preserved for subsequent changes in an underlying liability, regardless of whether a change is voluntary or involuntary. Section 1245(c) similarly provides that interest holder liability with respect to the domesticated corporation only relates to interest holder liabilities that arise after the domestication.

[Subchapter] E
CONVERSION

§ 1250. Conversion.
§ 1251. Plan of conversion.
§ 1252. Approval of conversion.
§ 1253. Articles of conversion; effectiveness.
§ 1254. Amendment of plan of conversion; abandonment.
§ 1255. Effect of conversion.

§ 1250. CONVERSION
(a) By complying with [Subchapter] 12A (preliminary provisions) and this [Subchapter] 12E, a domestic nonprofit corporation may become:
(1) a domestic eligible entity; or
(2) a foreign eligible entity if the conversion is permitted by the organic law of the foreign eligible entity.
(b) By complying with [Subchapter] 12A, this [Subchapter] 12E and applicable provisions of its organic law, a domestic eligible entity may become a domestic nonprofit corporation if the conversion is authorized by the law of the foreign entity’s governing jurisdiction.
(c) If the organic law or organic rules of a domestic eligible entity do not provide procedures for, but do not prohibit, the approval of a conversion, a plan of conversion may nonetheless be approved in the same manner as a merger of that eligible entity. If the organic law or organic rules of a domestic eligible entity do not provide procedures for the approval of either a conversion or a merger, a plan of conversion may nonetheless be adopted and approved by the unanimous consent of all the interest holders of the eligible entity. In either case, the conversion thereafter may be effected as provided in the other provisions of this [Subchapter] 12A.

(d) By complying with the provisions of [Subchapter] 12A and this [Subchapter] 12E applicable to foreign entities, a foreign eligible entity may become a domestic nonprofit corporation if the organic law of the foreign eligible entity permits it to become a nonprofit corporation in another jurisdiction.

(e) If a protected agreement of a domestic nonprofit corporation, or a domestic eligible entity whose organic law does not provide for conversions, that is the converting entity in effect immediately before the conversion becomes effective contains a provision applying to a merger or change of control of the corporation or entity and the agreement does not refer to a conversion of the corporation or entity, the provision applies to a conversion of the corporation or entity as if the conversion were a merger, until such time as the provision is first amended after the enactment date.

Source Note: Model Business Corporation Act (2016 Revision), § 9.30.

CROSS-REFERENCES

“Converted entity” defined, § 1201.
“Converting entity” defined, § 1201.
“Corporation,” “nonprofit corporation,” “domestic corporation” and “domestic nonprofit corporation” defined, § 102.
“Domestic” and “eligible entity” defined, § 102.
“Enactment date” defined, § 1201.
Excluded transactions, § 1202.
“Foreign” and “eligible entity” defined, § 102.
“Interest holder” defined, § 102.
“Membership” defined, § 102.
“Organic law” and “organic rules” defined, § 102.
“Protected agreement” defined, § 1201.
Required approvals, § 1203.

OFFICIAL COMMENT

Subchapter 12E authorizes a domestic nonprofit corporation to become a domestic eligible entity. It also authorizes a domestic nonprofit corporation to become a foreign eligible entity, but only if the conversion is permitted by the laws under which the foreign eligible entity will be organized. Further, Subchapter 12E authorizes a domestic or foreign eligible entity to
become a domestic nonprofit corporation. Whether and on what terms a foreign eligible entity is authorized to convert is governed by its organic law. If a foreign eligible entity is so authorized, it must comply with the provisions of this Subchapter 12E applicable to foreign entities. For example, it must file articles of conversion under Section 1253(a), and Section 1253(b) requires its articles of incorporation to meet the requirements of Section 202.

If the law under which a domestic eligible entity is organized does not expressly authorize it to convert to a domestic nonprofit corporation, Section 1250(c) provides procedures for such an entity to adopt and effect a plan of conversion.

Section 1250(e) provides special rules about “protected agreements”—certain documents and agreements in effect before the date (defined as the “enactment date”) of Chapter 12 (or any similar predecessor statute).

§ 1251. PLAN OF CONVERSION

(a) A domestic nonprofit corporation may convert to an eligible entity under this Subchapter 12E by approving a plan of conversion. A domestic eligible entity whose organic law does not provide for conversions may convert to a domestic nonprofit corporation under this Subchapter 12E by approving a plan of conversion. In either case, the plan of conversion must include:

1. the name and type of the converting entity;
2. the name, governing jurisdiction, and type of entity of the converted entity;
3. the manner and basis of converting the interests of the converting entity, if any, into eligible interests or other securities, obligations, rights to acquire interests or other securities, cash, other property, or any combination of the foregoing;
4. the other terms and conditions of the conversion;
5. the converted entity’s proposed public organic record, if any; and
6. the full text of the organic rules of the converted entity that are to be in a record, as they will be in effect immediately after the conversion becomes effective.

(b) In addition to the requirements of Section 1251(a), a plan of conversion may contain any other provision not prohibited by law.

(c) The terms of a plan of conversion may be made dependent upon facts objectively ascertainable outside the plan in accordance with Section 105 (extrinsic facts in filed record).

Source Note: Model Business Corporation Act (2016 Revision), § 9.31.
Under Section 1251(a)(5), the plan of conversion must include the organic rules of the converted entity that are to be in a record. Those organic rules should comply with the organic law governing the converted entity. Section 1251(a) lists the mandatory provisions that must be in the plan. Section 1251(b) authorizes the plan to contain any other provision the parties wish to include, unless the provision is prohibited by law.

§ 1252. APPROVAL OF CONVERSION

(a) In the case of a conversion of a domestic nonprofit corporation to an eligible entity, or of a domestic eligible entity whose organic law does not provide for conversions to a domestic nonprofit corporation, the plan of conversion must be adopted in the following manner:

(1) The plan of conversion must first be adopted by the governors. The governors may set conditions for approval of the plan of conversion by the members or the effectiveness of the plan of conversion. If the converting entity does not have any interest holders entitled to vote on the conversion, a plan of conversion shall be deemed adopted by the corporation when it has been adopted by the governors.

(2) Except as provided in Section 1252(a)(1), the plan of conversion must then be approved by the interest holders. In submitting the plan of conversion to the interest holders for approval, the governors must recommend that the interest holders approve the plan; unless the governors make a determination that because of conflicts of interest or other special circumstances they should not make such a recommendation, in which case the governors must inform the interest holders of the basis for so proceeding.

(3) If the plan of conversion is required to be approved by the interest holders, and if the approval is to be given at a meeting, the converting entity must notify each interest holder entitled to vote of the meeting of interest holders at which the plan of conversion is to be submitted for approval. The notice must state that the purpose, or one of the purposes, of the meeting is to consider the plan of conversion and must contain or be accompanied by a copy or summary of the plan. The notice must include or be accompanied by a copy of the organic rules
of the converted entity that are to be in a record as they will be in effect immediately after the conversion.

(4) Unless the organic rules, or the governors acting pursuant to Section 1252(a)(1), require a different vote or quorum, approval of the plan of conversion requires the approval of the interest holders at a meeting at which a quorum exists consisting of a majority of the votes entitled to be cast on the plan and the approval of each separate voting group at a meeting at which a quorum of the voting group is present consisting of a majority of the votes entitled to be cast on the plan by that voting group.

(5) If as a result of the conversion, one or more interest holders of the converting entity would become subject to new interest holder liability, approval of the plan of conversion requires the signing in connection with the conversion, by each such interest holder, of a separate consent in a record to become subject to such new interest holder liability.

(6) In addition to the adoption and approval of the plan of conversion by the governors and interest holders as required by this Section 1252, the plan of conversion must also be approved in a record by any person or group of persons whose approval is required under Section 930 (approval by third persons) to amend the articles of incorporation or bylaws of a converting entity that is a domestic nonprofit corporation.

(b) See Section 1203 (required approvals).

Source Note: Model Business Corporation Act (2016 Revision), § 9.32.

CROSS-REFERENCES

Abandonment of conversion, § 1254.
Application to domestic eligible entities, § 1250.
Contents of plan of conversion, § 1251.
“Eligible entity” defined, § 102.
“Interest holder liability” defined, § 102.
“Organic rules” defined, § 102.
“Voting group” defined, § 102.

OFFICIAL COMMENT

Section 1252 sets forth the rules for adoption and approval of a plan of conversion by a domestic nonprofit corporation. The manner in which the conversion of a foreign eligible entity to a domestic nonprofit corporation must be adopted and approved will be controlled by the organic law of the foreign jurisdiction. The manner in which the conversion of a domestic eligible entity to a domestic nonprofit corporation must be adopted and approved will be controlled by the organic law of the eligible entity, as supplemented by Section 1250(b), if applicable.
When submitting a plan of conversion to shareholders, the board of directors must recommend the transaction, subject to the exception in Section 1252(a)(2). The board might exercise the exception where the number of directors having a conflicting interest makes it inadvisable for the board to recommend the conversion or where the board is evenly divided as to the merits of the conversion but is able to agree that shareholders should be permitted to consider it.

Section 1252(a)(1) permits the board of directors to condition its submission of a plan of conversion to the members or the effectiveness of the plan of conversion. Among the conditions that a board of directors might impose are that the plan will not be deemed approved unless it is approved by a specified vote of the members, or by one or more specified classes or series of members, voting as a separate voting group, or by a specified percentage of disinterested members.

Section 1252(a)(4) sets forth quorum and voting requirements applicable to a member vote to approve a plan of conversion. It requires both the vote of the members entitled to vote on the plan, and the vote of each class or series of members voting as a separate voting group. In lieu of approval at a meeting, member approval may be by consent under the procedures set forth in Section 704.

Section 1252(a)(6) applies only in situations where a member of a domestic nonprofit corporation is becoming subject to “interest holder liability,” as defined in Section 102, with respect to the converted entity. Approval of a conversion that would have such a result requires the consent of each member who becomes subject to interest holder liability.

§ 1253. AMENDMENT OR ABANDONMENT OF PLAN OF CONVERSION

(a) A plan of conversion of a domestic nonprofit corporation, or a domestic eligible entity whose organic law does not provide for conversions, may be amended, except as otherwise provided in the plan, and before articles of conversion have become effective.

(1) in the same manner as the plan was approved, if the plan does not provide for the manner in which it may be amended; or

(2) in the manner provided in the plan, except an interest holder that was entitled to vote on or consent to approval of the plan is entitled to vote on or consent to any amendment of the plan that will change:

(i) the amount or kind of interests, securities, obligations, rights to acquire interests, securities, cash, other property, or any combination of the foregoing, to be received by the interest holders of the converting entity under the plan;

(ii) the organic rules of the converted entity that will be in effect immediately after the conversion becomes effective, except for changes that do not require approval of the interest holders of the converted entity under its organic law or organic rules; or
(iii) any of the other terms or conditions of the plan, if the change would adversely affect the member in any material respect.

(b) After a plan of conversion has been approved and before the articles of conversion are effective, the plan may be abandoned as provided in the plan. Unless prohibited by the plan, a domestic nonprofit corporation or domestic eligible entity whose organic law does not provide for conversions may approve abandonment in the same manner as the plan was approved.

(c) If a plan of conversion is abandoned after articles of conversion have been delivered to the secretary of state for filing and before the articles are effective, articles of abandonment, signed by the converting entity, must be delivered to the secretary of state for filing before the articles of conversion become effective. The articles of abandonment take effect on filing, and the conversion is abandoned and does not become effective. The articles of abandonment must contain:

1. the name and governing jurisdiction of the converting entity;
2. the date on which the articles of conversion were filed by the secretary of state; and
3. a statement that the conversion has been abandoned in accordance with this Section 1253.

Source Note: Model Business Corporation Act (2016 Revision), § 9.34.

CROSS-REFERENCES

“Domestic nonprofit corporation” defined, § 102.
“Interests” defined, § 102.
“Organic law” and “organic rules” defined, § 102.

OFFICIAL COMMENT

Section 1253(a)(2) permits the plan of conversion to be amended in the manner provided in the plan, subject to certain cases requiring a shareholder vote on the amendment. If the plan has no provisions with respect to its amendment, it may be amended under Section 1253(a)(1) in the same manner as it was approved.

Under Section 1253(b), unless otherwise provided in the plan of conversion, a domestic nonprofit corporation may abandon a conversion without member approval, even though the transaction has been previously approved by the members. The power of a foreign or domestic eligible entity to abandon a conversion will be determined by its organic law.
ARTICLES OF CONVERSION; EFFECTIVE DATE

(a) Articles of conversion of a domestic nonprofit corporation, or a domestic eligible entity whose organic law does not provide for conversions, must be signed by the converting entity and delivered to the secretary of state for filing.

(b) The articles of conversion must contain:

(1) the name, governing jurisdiction, and type of entity of the converting entity;

(2) the name, governing jurisdiction, and type of entity of the converted entity;

(3) if the converting entity is:

(i) a domestic nonprofit corporation or a domestic eligible entity whose organic law not provide for conversions, a statement that the plan of conversion was approved in accordance with this [Subchapter] 12E; or

(ii) a foreign nonprofit corporation or any other eligible entity, a statement that the conversion was approved by the corporation or entity in accordance with its organic law.

(4) If the converted entity is:

(i) a domestic filing entity, its public organic record, as an attachment, except that provisions that would not be required to be included in a restated public organic record may be omitted; or

(ii) a domestic limited liability partnership, its statement of qualification, as an attachment;

(iii) a foreign eligible entity that is not a registered foreign entity, a mailing address for the surviving entity to which the secretary of state may send any process served on the secretary of state pursuant to Section 1255(e) (effect of conversion).

(c) In addition to the requirements of Section 1254(b), the articles of conversion may contain any other provision not prohibited by law.

(d) If the converted entity is:

(1) a domestic nonprofit corporation, its articles of incorporation must satisfy the requirements of Section 202 (articles of incorporation), except that the articles do not need to be signed, and provisions that would not be required to be included in restated articles may be omitted; or
(2) domestic eligible entity, its public organic record, if any, must satisfy the requirements of the organic law of this state, except that the public organic record does not need to be signed, and provisions that would not be required to be included in restated public organic record may be omitted.

(e) A plan of conversion that is signed by the converting entity and meets all of the requirements of Section 1254(b) may be delivered to the secretary of state for filing instead of articles of conversion and on filing has the same effect. If a plan of conversion is filed as provided in this Section 1254(e), references in this [Subchapter] 12E to articles of conversion refer to the plan of conversion filed under this Section 1254(e).

(f) The articles of conversion are effective on the date and time of filing or the later date and time specified in the statement of conversion.

(f) If a converted entity is a domestic entity, the conversion becomes effective when the articles of conversion are effective. With respect to a conversion in which the converted entity is a foreign eligible entity, the conversion itself becomes effective at the later of:

(1) the date and time provided by the organic law of that eligible entity; or

(2) when the articles of conversion become effective.

Source Note: Model Business Corporation Act (2016 Revision), § 9.33.

CROSS-REFERENCES

“Domestic nonprofit corporation” defined, § 102.
Effect of conversion, § 1255.
Effective time and date of filing, § 163.
“Eligible entity” defined, § 102.
“Filing entity” defined, § 102.
Filing requirements, § 160.
“Organic law” defined, § 102.
“Public organic record” defined, § 102.
Required approvals, § 1203.

OFFICIAL COMMENT

The filing of articles of conversion makes the conversion a matter of public record. Where the converted entity is organized under the laws of this state, the filing also makes a public record of its articles of incorporation or public organic record.

The requirements for filing are set forth in Section 160. Under Section 163, the articles of conversion are effective on the date and at the time of filing unless a later effective date is specified in the articles within the limits provided in Section 163. Under that section, a delayed
effective date may not be later than the 90th day after the date the document is filed. Section 1254(f) provides when the conversion becomes effective.

It is only necessary for the filing office to record the effective date of the articles of conversion and the filing office does not need to be concerned with the effective date of the conversion itself. Persons wishing to determine the effective date of a conversion involving both a domestic and a foreign entity will be able to do so by consulting the records of the filing offices in each jurisdiction.

§ 1255. EFFECT OF CONVERSION

(a) When a conversion becomes effective:

(1) all property of the converting entity is the property of the converted entity without transfer, reversion or impairment;

(2) all debts, obligations and other liabilities of the converting entity remain the debts, obligations and other liabilities of the converted entity;

(3) except as otherwise provided by law or the plan of conversion, all the rights, privileges, immunities, powers, and purposes of the converting entity remain vested in the converting entity;

(4) the name of the converted entity may be substituted for the name of the converting entity in any pending action or proceeding;

(5) if the converted entity is a filing entity, its public organic record is effective;

(6) the converted entity’s private organic rules are effective;

(7) if the converted entity is a limited liability partnership, its statement of qualification is effective;

(8) the interests in the converting entity are reclassified into interests, securities, obligations, rights to acquire interests, securities, cash, or other property in accordance with the terms of the conversion, and the interest holders of the converting entity are entitled only to the rights provided to them by those terms and to any appraisal rights they may have under section 1204 (appraisal rights) and the converting entity’s organic law; and

(9) the converted entity is:

(i) incorporated or organized under and subject to the current organic law of the converted entity;
(ii) the same entity without interruption as the converting entity; and

(iii) deemed to have been incorporated or otherwise organized on the
date that the converting entity was originally incorporated or organized.

(b) Except as otherwise provided in the organic law or organic rules of a converting
entity, a conversion under this [Subchapter] 12E does not give rise to any rights that an interest
holder, governor, or third party would have upon a dissolution, liquidation, or winding up of the
converting entity.

(c) When a conversion under this [Subchapter] 12E becomes effective, a person that
did not have interest holder liability with respect to the converting entity and becomes subject to
interest holder liability with respect to a domestic converted entity as a result of the conversion
has interest holder liability only to the extent provided by the organic law of that entity and only
for those debts, obligations, and other liabilities that are incurred after the conversion becomes
effective.

(d) When a conversion becomes effective, the interest holder liability of a person that
ceases to hold an interest in a domestic converting entity with respect to which the person had
interest holder liability is subject to the following rules:

(1) The conversion does not discharge any interest holder liability under the
organic law of the converting entity to the extent the interest holder liability was incurred before
the conversion became effective.

(2) The person does not have interest holder liability under the organic law of
the converting entity for any debt, obligation, or other liability that is incurred after the
conversion becomes effective.

(3) The organic law of the converting entity continues to apply to the release,
collection, or discharge of any interest holder liability preserved under Section 1255(d)(1) as if
the conversion had not occurred.

(4) The person has whatever rights of contribution from any other person as
are provided by law other than this [Act] or the organic rules of the converting entity with
respect to any interest holder liability preserved under Section 1255(d)(1) as if the conversion
had not occurred.

Source Note: Model Business Corporation Act (2016
Revision), § 9.35.

CROSS-REFERENCES

“Eligible entity” defined, § 102.
“Filing entity” defined, § 102.
“Interest” defined, § 102.
“Interest holder” defined, § 102.
The converted entity is the same entity as the converting entity, and it continues without interruption. It becomes the new type of entity in the specified governing jurisdiction with the same status as if it had been originally incorporated or organized there. The converted entity will be subject to the organic law for that entity in that jurisdiction and will be subject to all of the duties, liabilities, and limitations imposed on such entities in that jurisdiction. Thus, a conversion is not a conveyance, transfer, or assignment. It does not give rise to claims of reverter or impairment of title based on a prohibited conveyance, transfer, or assignment. Nor does it give rise to a claim that a contract with the converting entity is no longer in effect on the ground of nonassignability, unless the contract specifically provides that it does not survive a conversion. See, however, Section 1250(e) with respect to special rules regarding protected agreements. All pending proceedings involving the converting entity are continued.

Section 1255(c) provides that interest holder liability with respect to a domestic nonprofit corporation or eligible entity that is the converted entity only relates to interest holder liabilities that arise after the conversion. Section 1255(d) similarly preserves the interest holder liability of interest holders in an eligible entity that converts to a domestic corporation only for interest holder liabilities to the extent they arise before the conversion becomes effective. Interest holder liability is not preserved for subsequent changes in an underlying liability, regardless of whether a change is voluntary or involuntary.

[Chapter] 13
FOREIGN CORPORATIONS

§ 1301. Governing law.
§ 1302. Registration to do business in this state.
§ 1303. Foreign registration statement.
§ 1304. Amendment of foreign registration statement.
§ 1305. Activities not constituting doing business.
§ 1306. Noncomplying name of foreign corporation.
§ 1307. Withdrawal of registration of registered foreign corporation.
§ 1308. Deemed withdrawal upon domestication or conversion to certain domestic entities.
§ 1309. Withdrawal upon dissolution or conversion to certain nonfiling entities.
§ 1310. Transfer of registration.
§ 1311. Administrative termination of registration.
§ 1312. Action by [attorney general].

§ 1301. GOVERNING LAW
(a) The law of the governing jurisdiction of a foreign nonprofit corporation governs:

(1) the internal affairs of the foreign corporation; and

(2) the interest holder liability of its members.

(b) A foreign nonprofit corporation is not precluded from registering to do business in this state because of any difference between the law of the corporation’s governing jurisdiction and the law of this state.

(c) Registration of a foreign nonprofit corporation to do business in this state does not permit the foreign corporation to engage in any business or affairs or exercise any power that a domestic nonprofit corporation may not engage in or exercise in this state.

Source Note: Model Business Corporation Act (2016 Revision), § 15.01.

CROSS-REFERENCES

Application of Act to existing foreign corporation, § 1302.
Doing business without registration, § 1302.
“Foreign corporation” defined, § 102.
Foreign registration statement, § 1303.
“Interest holder liability” defined, § 102.
Powers of domestic nonprofit corporation, § 302.

OFFICIAL COMMENT

Section 1301 confirms that a foreign nonprofit corporation is generally governed by the laws of its jurisdiction of formation. A foreign nonprofit corporation registered in this state, however, may only engage in business or exercise powers in this state to the same extent as a domestic nonprofit corporation.

§ 1302. REGISTRATION TO DO BUSINESS IN THIS STATE

(a) A foreign nonprofit corporation may not do business in this state until it registers with the secretary of state under this [Chapter].

(b) A foreign nonprofit corporation doing business in this state may not maintain a proceeding in any court of this state until it is registered to do business in this state.

(c) The failure of a foreign nonprofit corporation to register to do business in this state does not impair the validity of a contract or act of the corporation or preclude it from defending a proceeding in this state.
(d) A limitation on the liability of a member or director of a foreign nonprofit corporation is not waived solely because the corporation does business in this state without registering.

(e) Section 1301(a) (governing law) applies even if a foreign nonprofit corporation fails to register under this [Chapter].

Source Note: Model Business Corporation Act (2016 Revision), § 15.02.

CROSS-REFERENCES

Activities not constituting doing business, § 1305.
Foreign registration statement, § 1303.
“Proceeding” defined, § 102.

OFFICIAL COMMENT

Section 1302(b) closes the courts of this state to suits brought by a foreign nonprofit corporation that should have registered. Section 1302(c) makes clear, however, that the failure to register does not impair the validity of the corporation’s acts, and Section 1302(d) preserves the effectiveness of any liability shields applicable under the corporation’s organic law. If a corporation should have registered and failed to do so, it may still enforce its contracts in the courts of this state by registering.

Although Section 1302(b) prevents a foreign nonprofit corporation that is not registered but should from maintaining a proceeding in this state, section 1302(c) makes clear that the corporation may still defend a proceeding. The distinction between “maintaining” and “defending” an action or proceeding is determined on the basis of whether affirmative relief is sought. Such a nonregistered corporation may interpose any defense or permissive or mandatory counterclaim to defeat a claimed recovery, but may not obtain a judgment based on the counterclaim until it has registered.

§ 1303. FOREIGN REGISTRATION STATEMENT

To register to do business in this state, a foreign nonprofit corporation must deliver a foreign registration statement to the secretary of state for filing. The registration statement must be signed by the corporation and state:

(1) the corporate name of the corporation and, if the name does not comply with Section 210 (corporate name), an alternate name as required by Section 1306 (noncomplying name of foreign corporation);

(2) the corporation’s governing jurisdiction;
(3) the street and mailing addresses of the corporation’s principal office and, if the law of the corporation’s governing jurisdiction requires the corporation to maintain an office in that jurisdiction, the street and mailing addresses of that office;

(4) the street and mailing addresses of the corporation’s registered office in this state and the name of its registered agent at that office;

(5) the names and business addresses of its directors and principal officers; and

(6) a brief description of the nature of its activities to be conducted in this state.

Source Note: Model Business Corporation Act (2016 Revision), § 15.03.

CROSS-REFERENCES

Alternate name, § 1306.
Amendment to foreign registration statement, § 1304.
Annual report, § 421.
Application of Act to existing qualified foreign corporation, § 1302.
Corporate name, § 1306 and Ch. 2.
Filing requirements, § 160.
“Principal office”: defined, § 102.
designated in annual report, § 421.
Registered office and agent, Ch. 2.

OFFICIAL COMMENT

The foreign registration statement assures that certain basic information about the foreign nonprofit corporation will be publicly available and that citizens of the state will have access to that information in their dealings with the corporation. The foreign registration statement also provides information that facilitates service of process on the corporation. A registered corporation also must file an annual report as provided in section 421.

§ 1304. AMENDMENT OF FOREIGN REGISTRATION STATEMENT

A registered foreign nonprofit corporation must sign and deliver to the secretary of state for filing an amendment to its foreign registration statement if there is a change in:

(1) its name or alternate name;
(2) its governing jurisdiction, unless its registration is deemed to have been withdrawn under Section 1308 (deemed withdrawal upon domestication or conversion to certain domestic entities) or transferred under Section 1310 (transfer of registration); or

(3) an address required by Section 1303(c) (foreign registration statement).

Source Note: Model Business Corporation Act (2016 Revision), § 15.04.

CROSS-REFERENCES

- Change of registered office or agent, § 221.
- Corporate name, § 1306 and Ch. 2.
- Filing requirements, § 102.
- Foreign registration statement, § 1303.
- Resignation of registered agent, § 222.

OFFICIAL COMMENT

Section 1304 requires that certain information of record in the office of the secretary of state about a registered foreign nonprofit corporation be kept current. Filings for changes in the corporation’s registered office or agent are required by sections 221 and 222, and need not be duplicated by an amendment to the registration statement.

§ 1305. ACTIVITIES NOT CONSTITUTING DOING BUSINESS

(a) Activities of a foreign nonprofit corporation that do not constitute doing business in this state for purposes of this [Chapter] include:

(1) maintaining, defending, mediating, arbitrating, or settling a proceeding;

(2) carrying on any activity concerning the internal affairs of the foreign corporation, including holding meetings of its members or board of directors;

(3) maintaining accounts in financial institutions;

(4) maintaining offices or agencies for the transfer, exchange, and registration of securities of the corporation or maintaining trustees or depositories with respect to those securities;

(5) selling through independent contractors;

(6) soliciting or obtaining orders by any means if the orders require acceptance outside this state before they become contracts;
creating or acquiring indebtedness, mortgages, or security interests in property;
securing or collecting debts or enforcing mortgages or security interests in property securing the debts, and holding, protecting, or maintaining property so acquired;
conducting an isolated transaction that is not in the course of similar transactions;
(10) owning, protecting, and maintaining property; and
(11) doing business in interstate commerce.

(b) A person does not do business in this state solely by being an interest holder or governor of a domestic or foreign entity or exercising the powers or duties of an interest holder or governor.

(c) This section does not apply in determining the contacts or activities that may subject a foreign nonprofit corporation to service of process, taxation, registration as a charity, regulation of charitable solicitations, or other regulation under the laws of this state other than this [Act].

Source Note: Model Business Corporation Act (2016 Revision), § 15.05. Subsection (b) is patterned in part after Uniform Business Organizations Code (2011) (Last Amended 2013) § 1-505(b).

CROSS-REFERENCES
Corporate powers, § 302.
Corporate purposes, § 301.
Governing law, § 1301.
“Proceeding” defined, § 102.

OFFICIAL COMMENT
Chapter 13 does not attempt to formulate an exclusive definition of what constitutes doing business in a state. Rather, the concept is illustrated in a negative fashion by the non-exclusive list of examples in Section 1305(a) of activities that do not constitute doing business. In general terms, any conduct more regular, systematic, or extensive than that described in Section 1305(a) constitutes doing business and requires the foreign nonprofit corporation to register to do business. Typical conduct requiring registration includes maintaining an office to conduct local intrastate business, selling personal property not in interstate commerce, entering into contracts relating to the local business or sales, and owning or using real estate for general purposes. The passive owning of real estate for investment purposes does not constitute doing business. See Sections 1305(a)(8) and (a)(10).
The description of “doing business” in Section 1305(a) applies only under Chapter 13, and only to the question whether the foreign nonprofit corporation’s activities in this state are such that it must register under Chapter 13. It is not applicable to other questions, such as whether the corporation is subject to service of process under state “long-arm” statutes or liable for state or local taxes. A corporation that has registered (or is required to register) will generally be subject to suit and state taxation, while a corporation that is subject to service of process or state taxation will not necessarily be required to register.

The following provides additional guidance with respect to some of the activities listed in section 1305(a) that will not, in and of themselves, constitute doing business in this state.

1. Engaging in Litigation and Other Proceedings

Under Section 1305(a)(1), a foreign nonprofit corporation is not doing business by maintaining, defending, mediating, arbitrating, or settling a proceeding, which as defined in Section 102 includes civil suits and criminal, administrative, and investigatory actions. Accordingly, a corporation is not doing business solely because it resorts to the courts of this state to, for example, collect indebtedness, enforce an obligation, recover possession of personal property, obtain the appointment of a receiver, intervene in a pending proceeding, bring a petition to compel arbitration, file an appeal bond, or pursue appellate remedies. Similarly, a corporation is not required to register merely because it files a complaint with a governmental agency or participates in an administrative proceeding within this state.

2. Internal Affairs

As provided in Section 1305(a)(2), a foreign nonprofit corporation does not do business in this state merely because it holds meetings of its members or board of directors within this state. Other activities relating to the internal affairs of the corporation that do not constitute doing business under this section include having officers or representatives who reside within or are physically present in this state. While there, the officers or representatives may make executive decisions without imposing on the corporation the requirement that it register, if these activities are not so regular and systematic as to cause the residence to be viewed as a business office.

3. Sales through Independent Contractors

Under Section 1305(a)(5), a foreign nonprofit corporation need not register if it sells goods in this state through independent contractors. These transactions are viewed as transactions by the independent contractors, not by the corporation itself, even if the corporation sets some limits or rules for its contractors. If these limits or rules are sufficiently pervasive, however, the corporation may be deemed to be selling for itself in intrastate commerce, and not through the independent contractors and therefore doing business in this state.

4. Creating, Acquiring, or Collecting Debts

The mere act of making a loan by a foreign nonprofit corporation does not constitute doing business in the state in which the loan is made. On the same theory, a corporation may
obtain security for the repayment of a loan, and foreclose or enforce the lien or security interest
to collect the loan, without being deemed to be doing business. Similarly, a refunding or “roll
over” of a loan or its adjustment or compromise does not involve doing business.

5. Isolated Transactions

The concept of doing business involves regular, repeated, and continuing business
activities in this state. A single agreement or isolated transaction within the state does not
constitute doing business. An isolated transaction does not constitute “doing business” regardless
of how long the transaction takes to complete.

6. Interstate Transactions

A foreign nonprofit corporation is not doing business within the meaning of Chapter 13 if it
is transacting business in interstate commerce (Section 1305 (a)(11)). This limitation reflects
the provisions of the United States Constitution that grant to the United States Congress
exclusive power over interstate commerce, and preclude states from imposing restrictions or
conditions upon this commerce.

7. Other Activities

Among other activities that do not give rise to the requirement that a registration
statement be filed by a foreign nonprofit corporation are the ownership of all the shares of a
corporation that is engaged in activities in the state or as a limited partner in a limited partnership
engaged in activities in the state, or taking ministerial actions such as filing financing statements
or registering trademarks.

§ 1306. NONCOMPLYING NAME OF FOREIGN CORPORATION

(a) A foreign nonprofit corporation whose name does not comply with Section 210 (corporate name) may not register to do business in this state until it adopts, for the purpose of
doing business in this state, an alternate name that complies with Section 210 by filing a foreign
registration statement under Section 1303 (foreign registration statement), or if applicable, a
transfer of registration statement under Section 1310 (transfer of registration), setting forth that
alternate name. A corporation adopting an alternate name as provided in this subsection need not
file under this state’s assumed or fictitious name statute with respect to that alternate name. After
registering to do business in this state with an alternate name, a corporation shall do business in
this state under:

(1) the alternate name;
(2) the corporation’s name, with the addition of its governing jurisdiction; or
(3) a name the corporation is authorized to use under the assumed or fictitious
name statute of this state.
(b) If a registered foreign nonprofit corporation changes its name after registration to a name that does not comply with Section 210, it may not do business in this state until it complies with subsection (a) by amending its registration statement to adopt an alternate name that complies with Section 210.

Source Note: Model Business Corporation Act (2016 Revision), § 15.06.

CROSS-REFERENCES

Amendment of foreign registration statement, § 1304.
Corporate names, Ch. 2.
Effective time and date of filing, § 163.
Filing requirements, § 160.
Foreign registration statement, § 1303.
Registered name, § 212.
Reserved name, § 211.

OFFICIAL COMMENT

A foreign nonprofit corporation must register under its name if that name satisfies the requirements of Section 210. If that name cannot be used because it does not comply with Section 210, the corporation may adopt and use an alternate name as provided in this section. Because the alternate name will be part of the records of the secretary of state by reason of the foreign registration statement, Section 1306(a) provides that an assumed or fictitious name filing with respect to the alternate name is not required. However, the assumed or fictitious name statute will apply to any other name under which the foreign nonprofit corporation does business in this state.

A foreign nonprofit corporation that registers to do business in this state may do business under a fictitious name to the same extent as a domestic nonprofit corporation.

§ 1307. WITHDRAWAL OF REGISTRATION OF REGISTERED FOREIGN CORPORATION

(a) A registered foreign nonprofit corporation may withdraw its registration by delivering a statement of withdrawal to the secretary of state for filing. The statement of withdrawal must be signed by the corporation and state:

(1) the name of the corporation and its governing jurisdiction;

(2) that the corporation is not doing business in this state and that it withdraws its registration to do business in this state; and
(3) that the corporation revokes the authority of its registered agent in this state.

(b) After the withdrawal of the registration of a foreign nonprofit corporation, service may be made as provided in Section 223 (service on domestic and foreign nonprofit corporations).

*Source Note:* Model Business Corporation Act (2016 Revision), § 15.07.

**CROSS-REFERENCES**

Administrative termination of foreign registration, § 1311.
Changing registered office or agent, § 221.
Effective time and date of filing, § 163.
Filing requirements, § 160.
Foreign corporation included in definition of “corporation” for purposes of Ch. 2, § 220.
Registered office and agent, Ch. 2.
Resignation of registered agent, § 222.
Service on foreign corporation, § 223.

**OFFICIAL COMMENT**

The statement of withdrawal must set forth an address where service of process may be sent to the foreign nonprofit corporation by the secretary of state pursuant to section 223(c).

§ 1308. DEEMED WITHDRAWAL UPON DOMESTICATION OR CONVERSION TO CERTAIN DOMESTIC ENTITIES

The registration statement of a registered foreign nonprofit corporation that domesticates to a domestic nonprofit corporation or converts to a domestic business corporation or any type of domestic filing entity or to a domestic limited liability partnership is cancelled automatically on the effectiveness of such event.

*Source Note:* Model Business Corporation Act (2016 Revision), § 15.08.

**CROSS-REFERENCES**

Conversion, Ch. 9E.
Domestication, Ch. 9D.
“Filing entity” defined, § 102.

**OFFICIAL COMMENT**
When a registered foreign nonprofit corporation has domesticated or converted to a
domestic entity of the type set forth in this section, information about that entity in its capacity as
a domestic entity will continue to be of record in the office of the secretary of state. At that point,
there is no further reason for it to be registered and this section automatically treats its prior
registration as withdrawn.

§ 1309. WITHDRAWAL UPON DISSOLUTION OR CONVERSION TO CERTAIN
NONFILING ENTITIES

(a) A registered foreign nonprofit corporation that has dissolved and completed
winding up or has converted to a domestic or foreign nonfiling entity other than a limited
liability partnership must deliver to the secretary of state for filing a statement of withdrawal.
The statement must be signed by the dissolved corporation or the converted nonfiling entity and
state:

(1) in the case of a corporation that has completed winding up:

(i) its name and governing jurisdiction; and

(ii) that the corporation withdraws its registration to do business in this
state and revokes the authority of its registered agent to accept service on its behalf; or

(2) in the case of a corporation that has converted to a domestic or foreign
nonfiling entity other than a limited liability partnership:

(i) the name of the converting corporation and its governing
jurisdiction;

(ii) the type of the nonfiling entity to which it has converted and its
name and governing jurisdiction; and

(iii) that it withdraws its registration to do business in this state and revokes
the authority of its registered agent to accept service on its behalf.

(b) After the withdrawal of the registration of a foreign nonprofit corporation, service
may be made as provided in Section 223 (service on domestic and foreign nonprofit
corporations).

Source Note: Model Business Corporation Act (2016
Revision), § 15.09.

CROSS-REFERENCES

Annual report, § 421.
Change of registered agent, § 221.
Conversion, Ch. 9E.
When a registered foreign nonprofit corporation has dissolved and completed winding up, or has converted to a nonfiling entity other than a limited liability partnership, there is no further reason for information about it to appear in the records of the secretary of state. This section thus requires delivery of a statement of withdrawal for the purpose of removing the entity from the rolls of active entities.

§ 1310. TRANSFER OF REGISTRATION

(a) If a registered foreign nonprofit corporation merges into a nonregistered foreign filing entity or converts to a foreign filing entity, the surviving or converted entity must deliver to the secretary of state for filing a transfer of registration statement. The transfer of registration statement must be signed by the surviving or converted entity and state:

(1) the name of the registered foreign nonprofit corporation and its governing jurisdiction before the merger or conversion;

(2) the name of the surviving or converted entity and its governing jurisdiction after the merger or conversion and, if the name does not comply with Section 210 (corporate name), an alternate name adopted pursuant to Section 1306 (noncomplying name of foreign corporation); and

(3) the following information regarding the surviving or converted entity after the merger or conversion:

   (i) the street and mailing addresses of the principal office of the entity and, if the law of the foreign entity’s governing jurisdiction requires it to maintain an office in that jurisdiction, the street and mailing addresses of that office; and

   (ii) the street and mailing addresses of the foreign entity’s registered office in this state and the name of its registered agent at that office.

(b) On the effective date of a transfer of registration statement as determined in accordance with Section 163 (effective time and date of filing), the registration of the registered foreign corporation to do business in this state is transferred without interruption to the foreign entity into which it has merged or to which it has been converted.
CROSS-REFERENCES

Annual report, § 421.
Corporate name, Ch. 2.
Notices and other communications, § 103.
“Principal office”:
  defined, § 102.
  designated in annual report, § 421.
Service on foreign corporation, § 223.

OFFICIAL COMMENT

The purpose of this section is to clarify the status of the merged or converted registered foreign nonprofit corporation in the public records of this state, and to reflect the status of the surviving or converted entity. A filing under this section has the effect of canceling the registration of the foreign nonprofit corporation to do business in this state while at the same time reregistering it as the new foreign nonprofit corporation. If the reregistered foreign nonprofit corporation subsequently wishes to withdraw its registration to do business in this state, it may do so under Section 1307.

§ 1311. ADMINISTRATIVE TERMINATION OF REGISTRATION

(a) The secretary of state may terminate the registration of a registered foreign nonprofit corporation in the manner provided in subsections (b) and (c) if:

  (1) the corporation does not pay within [60] days after they are due any fees, taxes, interest or penalties imposed by this [Act] or other laws of this state that are collected by the secretary of state;

  (2) the corporation does not deliver its annual report to the secretary of state within [60] days after it is due;

  (3) the corporation is without a registered agent or registered office in this state for [60] days or more; or

  (4) the secretary of state has not been notified within 60 days that the foreign corporation’s registered agent or registered office has been changed, that its registered agent has resigned, or that its registered office has been discontinued.

(b) The secretary of state may terminate the registration of a registered foreign nonprofit corporation by:
(1) filing a statement of termination; and
(2) delivering a copy of the statement of termination to the corporation’s registered agent or, if the corporation does not have a registered agent, to the corporation’s principal office.

(c) The statement of termination must state:

(1) the effective date of the termination, which must be not less than 60 days after the secretary of state delivers the copy of the statement of termination as prescribed in subsection (b)(2); and

(2) the grounds for termination under subsection (a).

(d) The registration of a registered foreign nonprofit corporation to do business in this state ceases on the effective date of the termination as set forth in the statement of termination, unless before that date the corporation cures each ground for termination stated in the statement of termination. If the corporation cures each ground, the secretary of state shall file a statement that the statement of termination is withdrawn.

(e) After the effective date of the termination as set forth in the statement of termination, service may be made as provided in Section 223 (service on domestic and foreign nonprofit corporations).

Source Note: Model Business Corporation Act (2016 Revision), § 15.11.

CROSS-REFERENCES

Activities not constituting doing business, § 1305.
Annual report, § 421.
Change of registered office or agent, § 221.
“Deliver” defined, § 102.
Effective time and date of filing, § 163.
Foreign corporation included in definition of “corporation” for purposes of ch. 2, § 220.
“Principal office” defined, § 102.
Registered office and agent required, § 220.
Resignation of registered agent, § 222.
Service on foreign corporation, § 223.

OFFICIAL COMMENT

This section describes the circumstances under and manner in which the secretary of state may terminate the registration of a foreign corporation.

§ 1312. ACTION BY ATTORNEY GENERAL
The attorney general may maintain an action to enjoin a foreign nonprofit corporation from doing business in this state in violation of this [Act].

Source Note: Model Business Corporation Act (2016 Revision), § 15.12.

CROSS-REFERENCES

Activities not constituting doing business in this state, § 1305.

OFFICIAL COMMENT

Although the act provides no fines or penalties for failure to register to do business when required, Section 1312 confirms that the attorney general can nevertheless bring an action to enforce the laws of the state.

[Chapter] 14

TRANSITION PROVISIONS

§ 1401. Saving provisions.

(a) Except as provided in subsection (b), the repeal of a statute by this [Act] does not affect:

(1) the operation of the statute or any action taken under it before its repeal;

(2) any ratification, right, remedy, privilege, obligation, or liability acquired, accrued, or incurred under the statute before its repeal;

(3) any violation of the statute, or any penalty, forfeiture, or punishment incurred because of the violation, before its repeal;

(4) any proceeding, reorganization, or dissolution commenced under the statute before its repeal, and the proceeding, reorganization, or dissolution may be completed in accordance with the statute as if it had not been repealed.

(b) If a penalty imposed for violation of a statute or rule is reduced by this [Act], the penalty, if not already imposed, shall be imposed in accordance with this [Act].
(c) Members of a nonprofit corporation who were entitled to cumulate their votes for
the election of directors on [the date of enactment of this act] continue to be entitled to cumulate
their votes for the election of directors until otherwise provided in the articles of incorporation or
bylaws of the corporation.

(d) This [Act] modifies, limits, or supersedes the federal Electronic Signatures in
Global and National Commerce Act, 15 U.S.C. § 7001 et seq., but this [Act] does not modify, limit, or supersedes Section 101(c) of that act or authorize electronic delivery of any of the notices
described in Section 103(b) of that act.

OFFICIAL COMMENT

Section 1401(a) and (b) are similar to Section 16 of the Uniform Statute and Rule
Construction Act, which was promulgated by the National Conference of Commissioners on

Section 1401(d) is patterned after Uniform Limited Partnership Act (2001) § 1203, and
Uniform Limited Liability Company Act (2006) § 1102, and is required by section 102(a)(2)(B)
7002(a)(2)(B).

§ 1402. SEVERABILITY

If any provision of this [Act] or its application to any person or circumstance is held
invalid by a court of competent jurisdiction, the invalidity does not affect other provisions or
applications of the [Act] that can be given effect without the invalid provision or application.

§ 1403. CONSISTENCY OF APPLICATION

In applying and construing this [Act], consideration must be given to the need to promote
consistency of the law with respect to its subject matter among states that enact it.

§ 1404. REPEAL
The following laws and parts of laws are repealed: [to be inserted by enacting state].

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 17.06. Cf. Model Business Corporation Act (2016 Revision), § 17.06.

OFFICIAL COMMENT

The act is intended to be a complete substitute for earlier statutes of general applicability to nonprofit corporations and it is contemplated that all these statutes should normally be repealed when the revised act is enacted. A few states in the past have retained portions of earlier statutes while enacting integrated codifications of nonprofit corporation law. This practice is generally undesirable since it tends to cause unnecessary confusion in determining the applicable law as well as creating possible internal statutory conflicts.

§ 1405. EFFECTIVE DATE

This [Act] takes effect.

Source Note: Model Nonprofit Corporation Act, 3rd Ed. (2008), § 17.07.