

REG>Corporations SAMPLE

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Characteristics and Advantages of Corporate Form

1. Limited liability
 - a. Generally a shareholder in a corporation risks only his/her investment
2. Transferability of interest
 - a. Shares in corporations are represented by stocks and can be freely bought, sold, or assigned unless shareholders have agreed to restrictions
3. Continuous life
 - a. Unlike a partnership, a corporation is not terminated by death of a shareholder, or his/her incapacity
 - (1) Regarded as perpetual, and continues to exist until dissolved, merged, or otherwise terminated
4. Separate entity
 - a. A corporation is a legal entity in itself and is treated separately from its stockholders
 - (1) Can take, hold, and convey property
 - (2) Can contract in own name with shareholders or third parties
 - (3) Can sue and be sued
5. Financing
 - a. Often easier to raise large amounts of capital than in other business organizations by issuance of stock or other securities (e.g., bonds)
 - b. More flexible because it can issue different classes of stock and/or bonds to suit its needs and market demands
6. Corporate management manage corporations and are selected by the directors

Disadvantages of Corporate Business Structure

1. Tax treatment

a. Tax burdens may be more than on other business structures because of double taxation which happens when income is taxed at the corporate level and then dividends paid from after-tax income are taxed again at the shareholder level

(1) A corporation may alleviate double taxation by forming as a Subchapter S corporation which is taxed similar to a partnership

2. Costs of incorporating must meet formal creation requirements

3. If the corporation goes public;

a. There are substantial costs of compliance with federal securities laws

b. May be subject to hostile takeover

Types of Corporations

1. Domestic corporation is one that operates and does business within the state in which it was incorporated

2. Foreign corporation is one doing business in any state except the one in which it was incorporated

a. Foreign corporations (that are “doing business” in another state) are not exempt from many requirements and details that domestic corporations must meet

(1) Doing business in state is typically defined as maintaining an office or selling personal property in the state

(a) The following are not considered as doing business in a state

1] Defending against a lawsuit

2] Holding a bank account

3] Using mail to solicit orders

4] Collecting debts

5] Using independent contractors to make sales

(2) Foreign corporations can be required to qualify to do business in a state; accomplished by obtaining a certificate of authority from the state

(a) Must appoint an agent to receive service of process for suits against corporations

(b) Must pay specified fees

(c) Must file information with the Secretary of State

b. If foreign corporation does not qualify to do business in a state

(1) May be denied access to courts to sue

(2) Is liable to the state for any fees, taxes, interest, and penalties as if it had qualified to do business

(3) Is subject to fines

3. Professional corporations are ones under state laws that allow professionals to incorporate (e.g., doctors, accountants, attorneys)

a. All states allow professional corporations

b. Typically, shares may be owned only by licensed professionals

c. Retain personal liability for their professional acts

d. Obtain other corporation benefits (e.g., limited liability for corporate debts, some tax benefits)

4. **De facto** individuals act as if a corporation has been formed but the corporation has not been formed properly under the law and usually defective because of some small error

5. **De jure** corporations have been formed correctly in compliance with the incorporation statutes

Formation of a Corporation

1. Promoters are persons who form corporations and arrange capitalization to begin corporations

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- a. Promoters handle issuing of the prospectus, promoting stock subscriptions, and drawing up charter
- b. Promoters have a fiduciary relationship with corporation, and is not permitted to act against interests of corporation. Does not prevent personal profit if fully disclosed
- c. Promoters are not agents of the corporation, because the corporation is still not in existence

(1) Any agreements (preincorporation contracts) made by promoters are not binding on the future corporation until adopted after the corporation comes into existence

(a) Requires actual resolution of board of directors

(b) Normally promoters are personally liable on contracts. Adoption by corporation does not relieve promoters; **novation is required to relieve promoter**. The other party must agree to substituting the corporation. (Novation is the act of either replacing an obligation to perform with a new obligation, or replacing a party to an agreement with a new party.)

1] Promoters have liability even if promoter's name does not appear on contract

2] However, promoter is not liable if third party clearly states that s/he would look only to corporation for performance

2. Incorporation requirements

a. Articles of Incorporation (charter) are filed with the state and contain;

(1) Proposed name of corporation and initial address

(2) Name and address of registered agent of corporation

(3) Number of authorized shares of stock and types of stock

b. Initial shareholders' meeting

c. At same meeting or subsequent meeting, directors

(1) Elect officers

(2) Adopt or reject preincorporation contracts

(3) Begin business of corporation

(4) Adopt initial bylaws

- (a) These need not be filed with any government agency
 - (b) Provide specific rules for management
3. Articles of Incorporation may be subsequently amended
- a. Approval of any adversely affected shareholders of amendment needed
 - (1) Often majority vote or sometimes two-thirds vote required
 - (a) Dissenting minority shareholders may assert right of appraisal and therefore receive fair value for shares
 - 1] Fair value is value just before vote