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EC78-869 Incorporating your Farm or Ranch Business? Guidelines for Articles of Incorporation and By-Laws

John R. Urich

Philip A. Henderson

J. David Aiken

University of Nebraska-Lincoln, daiken@unl.edu

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meetings

EC 78-869

officers

Incorporating Your Farm or Ranch Business ?

records

GUIDELINES

FOR

stock

ARTICLES OF INCORPORATION

AND

debenture
bonds

BY-LAWS

board of
directors

shareholders

taxes

dividends



limited
liability

Extension work in "Agriculture, Home Economics and subjects relating thereto," The Cooperative Extension Service, Institute of Agriculture and Natural Resources, University of Nebraska-Lincoln, Cooperating with the Counties and the U.S. Department of Agriculture
Leo E. Lucas, Director

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GUIDELINES FOR ARTICLES OF INCORPORATION

John R. Uhrich¹
Philip A. Henderson²
J. David Aiken³

INTRODUCTION

A growing number of farm and ranch owners are incorporating their farm or ranch businesses. In many instances, the farm or ranch operation has been incorporated primarily for estate planning purposes. Others have incorporated for income tax advantages, to limit liability, or for other reasons.

The privilege to operate as a Nebraska based corporation is granted by the Nebraska Business Corporation Act. The Act requires an annual meeting of shareholders, election of directors, separate recordkeeping of corporate transactions, and the filing of annual reports⁴ with the State of Nebraska. Failure to comply with these statutory requirements can result in revocation of a corporation's charter, loss of limited liability, and unfortunate income tax consequences for the shareholders.

The two documents which provide for corporation establishment and management are the articles of incorporation and the by-laws. The articles of incorporation comprise the formal charter of the corporation; they set forth the general purposes and powers of the corporation. Corporate by-laws are enacted by the shareholders or directors to regulate the everyday internal affairs of the corporation.

The basic provisions for the articles of incorporation and by-laws are contained in the Nebraska Business Corporation Act. In certain instances, the Act serves only as a guideline and can be changed by agreement among the shareholders. In other instances, the provisions of the Act are mandatory and cannot be changed. For example, the Nebraska statutes require that there be a board of directors to manage the affairs of the corporation. The board of directors cannot be dispensed with in the articles or by-laws. On the other hand, the statutes require that at least a majority vote is needed to

elect a director to the board. However, the shareholders can provide for a greater-than-majority vote in the articles or by-laws. Within a certain framework, the shareholders are, therefore, able to structure the control, management, and operation of the corporation to fit their individual needs.

These requirements are the same for all corporations regardless of the type of business activity, whether it be farming, ranching, or manufacturing. They apply equally to publicly-held and closely-held corporations.

In a closely held corporation, the shares of stock are owned by a limited number of shareholders. Since the entire stock issue is often held by one family, there is little, if any, public trading of the stock. The typical family farm or ranch corporation is a closely-held corporation. In contrast, a publicly held corporation, such as General Motors, offers its shares of stock to the general public.

The purpose of this publication is to explain the contents of the articles of incorporation and by-laws of a corporation organized under Nebraska jurisdiction. The material is organized in a manner similar to that which would be found in an actual set of articles of incorporation or by-laws with one important exception. It does not contain the actual wording that would be found in these two documents. The advice and service of a lawyer are indispensable to the actual drafting of the articles of incorporation and by-laws. (For additional information on corporations see North Central Regional Extension Publication Number 11, "The Farm Corporation—What it is, How it Works, How it Is Taxed.")

ARTICLES OF INCORPORATION

The articles of incorporation must be filed with the Secretary of State accompanied by a filing fee. The fee is based on the amount of *authorized* capital stock of the corporation. As shown in Table 1, the filing fee on the first \$100,000 of authorized capital stock is \$100. Thereafter, an additional \$1.00 is assessed for each \$1,000 of capital stock

¹ Law student, University of Nebraska.

² Extension Economist, (Farm Management), University of Nebraska.

³ Water Law Specialist, University of Nebraska.

⁴ See appendix.

over \$100,000. For example, the filing fee for a corporation with \$200,000 authorized capital stock would be \$200.

Table 1. Corporation filing fees.

For filing articles of association, incorporation or consolidation; domestic or foreign, the capital stock¹ is

\$10,000 or less	\$ 20.00
\$10,001 to \$25,000	35.00
\$25,001 to \$50,000	50.00
\$50,001 to \$75,000	75.00
\$75,001 to \$100,000	100.00

For capital stock in excess of \$100,000 there is a charge of \$1.00 for each additional \$1,000, plus recording.

¹The capital stock of a corporation organized under the laws of any other state that domesticates in this state, and which stock does not have a par value, shall be deemed to have a par value of an amount per share equal to the amount paid in as capital for each of such shares as are then issued and outstanding, and in no event less than one dollar per share.

By statute, the articles of incorporation must contain certain basic information, described below, about the corporation. In addition, the articles may contain any provision concerning the regulation of the internal affairs of the corporation.

Article I (Name)

Generally, any name may be chosen for the corporation subject to three statutory limitations. First, the corporate name must contain one of the following words: "corporation," "company," "incorporated," "limited," or an abbreviation of one of these words. Second, the name must not contain any word or phrase which indicates that it was organized for a purpose other than purposes stated in the articles of incorporation. Third, the name must not be the same as, or deceptively similar to, the trade-name or name of any other existing corporation chartered under Nebraska law or any other corporation authorized to do business in Nebraska.

The exclusive right to use a particular corporate name can be requested by filing an application

with the Secretary of State in anticipation of the actual formation of the corporation. If the Secretary finds that the name is available for use, it can be reserved for a period of 120 days.

Article II (Duration)

Although a corporation can be established for any length of time, usually it is formed with the idea that it will continue indefinitely. A corporation can continue despite the death of its shareholders. A shareholder's ownership interest in the corporation passes at his death to his heirs or to designated beneficiaries.

A corporation can be dissolved at any time by a two-thirds vote of the shareholders. However, the tax consequences of dissolving a corporation may be severe. Upon dissolution of a corporation, a shareholder is taxed (at capital gain rates) on any property received by him, to the extent the value of that property exceeds the adjusted basis of his stock in the corporation. In most situations, the value of the farm or ranch property will have appreciated substantially over the shareholder's stock basis. Any gain will be taxed regardless of whether the property acquired is sold after it is distributed to the shareholder or is retained by him for future farm or ranch operations. Additionally, documentary tax stamps must be purchased and affixed to deeds when the liquidating corporation distributes real property to its shareholders. Consequently, a corporation should be formed only when the incorporators are certain that a corporation is the form of business organization which will best serve their long term tax, business, and operational needs.

Article III (Purpose and Powers)

A corporation can be formed for any lawful purpose. Usually the purpose clause found in the articles will be quite broad, encompassing a wide range of activities. For example, a typical clause might state, "The purpose of this corporation shall be to engage in agricultural production, processing, purchasing, manufacturing, marketing, and any other lawful business." A corporation cannot engage in activities that are outside the purposes for which the corporation was formed.

By statute, a corporation is given broad power to carry out its purposes. For example, a typical

farm or ranch corporation will usually be given the power to own, lease, operate, manage, and control all the land, buildings, machinery, etc., owned by the corporation. It is also given the power to sell, purchase, or mortgage any of the corporate assets. Any limitations that the incorporators desire to place on the corporation should be stated specifically in the articles.

Article IV (Stocks and Bonds)

A corporation is a legal entity separate from its shareholders. The corporate assets are owned by the corporation, not the shareholders. A shareholder's ownership interest in the corporation is that set of rights and duties which result from owning shares of stock. There are many different types of stock: voting or non-voting; common or preferred; preferred stock that receives a fixed dividend; preferred stock that participates equally with common stock in dividend distributions; etc.

The aggregate number of shares and the par value per share must be stated in the articles. A corporation can issue both common stock and preferred stock. However, if a corporation issues more than one class of stock, it may not elect to be treated as a Subchapter S corporation for income tax purposes.

Double taxation may be involved if a regular corporation is used. First, the corporation itself pays taxes on its annual earnings. Second, the shareholders pay taxes on any profits distributed to them in the form of dividends, except for the \$100 dividend exclusion.

A corporation which elects Subchapter S treatment can avoid the double taxation. The income from the Subchapter S corporation is not taxed at the corporate level but passes through to the shareholders for taxation at their respective rates. To qualify for Subchapter S treatment, a corporation must meet certain requirements. Among other things, it must have 10 or fewer shareholders and only one class of stock. After five years as a Subchapter S corporation, the number of shareholders can increase to 15. (For additional information on the taxation of corporations see North Central Regional Extension Publication Number 11, "The Farm Corporation—What it is, How it Works, How it Is Taxed.")

Common Stock

Common stock is the basic stock of the corporation. Common stock receives dividends only when the directors declare dividends based on past or present earnings. Normally, owners of common stock have voting rights and are entitled to share in the ultimate distribution of assets.

Common stock may be issued in different classes, often called Class A and Class B common. Each class of stock may have different voting rights. For example, Class A common stock may be entitled to elect two directors while Class B common stock may be entitled to elect only one director.

Preferred Stock

Preferred stock, as the name implies, is given a preference or priority over common stock. For example, dividends on preferred stock can be paid without paying dividends on common stock. In the event the corporation is dissolved, preferred shareholders are usually entitled to receive back their initial contribution to the corporation before the common shareholders receive their contribution. Preferred stock may either be voting or non-voting.

Preferred stock may be issued for several different purposes. Non-voting preferred stock may be especially useful in a business whose shareholders consist of two groups: 1) those who will manage the operation and 2) those who will supply the necessary funds needed by the business but who will take no active part in its operation. The issuance of non-voting preferred stock to the investors who supply the necessary capital will allow the preferred shareholders to receive a return on their investment without giving them any appreciable control over the operations. At the same time, the common shareholders can use the capital provided by preferred stockholders without losing control over the operation.

Preferred stock, either voting or non-voting, can also be useful as a means to fix the value of ownership interests in the corporation for estate planning purposes. Particularly in a farm or ranch corporation, the value of a share of common stock will appreciate as the value of the land and other assets held in the corporation increases. In contrast, a corporation can assign a fixed price to a share of preferred stock; if it does, the value of the

preferred stock will not change as the value of corporate assets rise.

Bonds and Debentures

Stock ownership should not be confused with ownership of bonds or debentures in a corporation. Bonds and debentures are debts of the corporation. A bond is a debt secured by some sort of lien (i.e., mortgage) on specific corporate assets. On the other hand, a debenture (also referred to as a debenture bond) is an unsecured debt of the corporation. This means that the debenture holder has no claim against specific corporate assets in case of default, and receives no priority over other unsecured creditors in the event of bankruptcy or liquidation of the corporation.

A bond or debenture holder is not a shareholder of the corporation. The only rights a bondholder has are those agreed upon between the corporation and the holder in a contract (i.e., mortgage, trust deed, or indenture agreement). If substantial rights to participate in management, control, and profits are granted to the bond holder, he will not be considered a creditor but a shareholder of the corporation. (An attorney or accountant should be consulted to determine the proper balance between debt and equity.)

A corporation may issue bonds or debentures that are convertible into stock at the option of the holder. Such bonds are generally convertible into common stock, although in some instances bonds are made convertible into preferred stock or other bonds. A holder of convertible bonds is not a shareholder and is not entitled to any rights of a shareholder until the option is exercised and the stock is issued.

Article V (Place of Business)

The articles must include the address of the corporation and the names of its registered agent which generally is one of the officers, directors, or shareholders of the corporation.

Article VI (Incorporators)

The names and addresses of the incorporators must also be included in the articles. The incorporators are those who initially form the corporation. One or more persons of the age of majority may

act as incorporator(s). Until the directors are elected at the first shareholder meeting, the incorporators will direct the affairs of the corporation and may take such steps as are necessary to obtain stock purchases and organize the corporation.

Article VII (Preemptive Rights)

A corporation may need additional capital to expand or maintain existing operations. One method of securing additional capital is to sell stock in the corporation. Preemptive rights give each existing shareholder a right to purchase a proportionate part of any new shares issued. Preemptive rights prevent any dilution of a shareholder's percentage ownership in a corporation when additional shares are issued. In this way, each shareholder has the opportunity to own the same percentage of the stock both before and after the sale of the additional stock.

To illustrate, suppose a newly formed corporation authorizes 200 share of stock but issues only 100 of those shares to A and B. A and B each own 50 shares, or 50% of the corporation. A few years later, the corporation decides to issue the additional 100 shares of stock. With preemptive rights the corporation must first offer 50 shares of this additional stock to each of the existing shareholders, A and B. If A and B each purchase 50 shares, each will retain his 50% ownership interest in the corporation.

A corporation may dispense with preemptive rights by a provision in the articles of incorporation. If the articles are silent as to preemptive rights, a shareholder is presumed to possess such rights.

Article VIII (Sale and Transfer of Stock)

First Option

A shareholder's right to freely sell his stock can be restricted to some extent either in the articles of incorporation, corporate by-laws, or in an agreement among shareholders. Such a provision can be especially desirable to shareholders in a small, closely-held corporation who wish to keep outsiders from obtaining ownership in the corporation. However, not all restrictions on the sale of stock are valid. A restriction which is unreasonable or which provides an absolute restraint on the sale of stock will not be enforceable.

One of the more frequently used restrictions is a "first option." This provision provides that a shareholder who desires to sell his stock must first offer the shares to the corporation. If the corporation does not purchase them, they can be offered to the other individual shareholders. If neither the corporation nor other individual shareholders purchase the shares, they can be sold to parties outside of the corporation.

Rather than encumber the articles with restrictive provisions, the shareholders may enter into a separate agreement among themselves which includes the basic "first option" provisions. Such an agreement is binding on all the shareholders who sign the agreement even though no such provision appears in the articles of incorporation.

Buy-Sell Agreement

There are several reasons for selling stock in a small closely-held corporation. First, the heirs of a deceased shareholder may not want to continue in the ownership and operation of the business. Second, a shareholder who has retired from any active participation may want additional income for retirement purposes. Finally, a shareholder may want to sell his stock in order to receive a greater return on his investment elsewhere.

A unique problem facing shareholders in a closely-held corporation is that there may be few persons, other than existing shareholders, willing to purchase the stock. This is especially true for minority shareholders. A minority shareholder can neither compel the payment of dividends nor control the operating policies of the corporation. Therefore, few persons outside the corporation may be willing to purchase a minority interest.

A buy-sell agreement is typically used for the benefit of the shareholder who wants "out" of the corporation. This agreement is a contract for the sale of one's stock either to the corporation or to the other shareholders. The agreement typically specifies the conditions under which the other shareholders are obligated to purchase, the method for pricing the stock, and how much each shareholder is obligated to purchase. In addition, the agreement may provide that the purchase price will be paid over a certain number of years. This provision may be especially important in those situations where neither the corporation nor shareholders have enough capital to pay for the entire purchase price in one lump sum.

Article IX (Amendments)

A corporation may amend its articles of incorporation in whole or in part at any time. The procedure for amending the articles is set by statute. The board of directors adopts a resolution setting forth the proposed amendment. The proposed amendment is then submitted to a vote at a regular or special meeting of the shareholders. The amendment will be adopted upon receiving the affirmative vote of at least two-thirds of the shares entitled to vote.

BY-LAWS OF A CORPORATION

Decision-making in a corporation is shared among officers, directors, and shareholders. One person may serve in all three capacities, particularly in a small family farm corporation. Each of these groups has a different set of responsibilities to the corporation. In simple terms, the shareholders, who own the corporation, elect directors who formulate over-all corporate policies and objectives. The directors then appoint officers to execute those objectives.

The by-laws establish the routine operating procedures for the shareholders, directors, and officers. The basic provisions of the by-laws will include: procedures relating to meetings; voting requirements; and the duties and responsibilities of the shareholders, directors, and officers. The initial by-laws must be approved by a majority of the shareholders. Thereafter, by-laws can be adopted, amended, or repealed by the board of directors or by shareholders.

Too frequently, farms which have chosen to incorporate will fail to follow formalities set forth in the by-laws. This is unfortunate in at least two respects. First, a corporation which fails to hold annual meetings, elect directors, keep separate corporate records, etc., may subject its shareholders to the hazard of having a court "pierce the corporate veil," i.e., rule that the corporate form of business was not really intended. If such a ruling were made the shareholders would lose the corporate advantage of limited liability. Second, many of the procedures called for in the by-laws, such as holding an annual meeting, provide an important means for all those owning an interest in the corporation to air their views. Communication among the shareholders, directors, and officers is a key to the successful operation of the corporation.

The following is only a broad overview of the subject matter contained in the by-laws. One way by-laws might be organized would be for: Article I to deal with shareholders; Article II, with directors, and Article III, with officers. The by-laws could be organized quite differently, however, and attorneys may elect to include more or less material than is suggested in the following paragraphs.

Article I (Shareholders)

Authority and Function

The shareholders are the corporation owners. Those who own voting stock elect directors who provide the over-all corporation management. A shareholder who owns more than 50% of the voting stock may elect a majority of members on the board of directors and thereby controls corporate operating policies. On the other hand, a shareholder who owns exactly 50% of the voting stock cannot elect a majority of board members. If the 50% shareholder is unable to agree with some of the other shareholders in selection of directors or operation of the corporation, a deadlock may occur. Such a situation may severely affect the corporation leadership and direction.

Not all shareholders are entitled to vote for directors. Only those shareholders who own voting stock, either common or preferred, can vote for directors. However, all shareholders, regardless of whether they own voting common or preferred, or non-voting preferred, are entitled to exercise their voting power on certain types of extraordinary corporate action. All shareholders are entitled to vote on: 1) the voluntary dissolution of the corporation; 2) mergers, consolidations, or sale of all or substantially all of the corporation's assets; and 3) mortgages, sales, or leases of corporate property not in the regular course of business.

These extraordinary items require the approval of at least two-thirds of the total outstanding stock, voting as well as non-voting. Consequently, shareholders who own two-thirds or more of the total outstanding stock may authorize a sale of substantially all the corporate assets and may also dissolve the corporation. By the same token, a shareholder who owns only slightly more than one-third of the total outstanding stock can prevent the dissolution of the corporation and a sale of substantially all the corporate assets. A share-

holder who owns less than one-third of the total outstanding stock may have little impact on corporation decision making.

These voting rights may be changed, to a certain extent, either in the articles of incorporation, by-laws, or agreement among shareholders. (See next section on How Shareholders Act).

How Shareholders Act

Meetings. Shareholders hold annual meetings to elect directors and to discuss the corporation's past and future operations. Items typically included on the annual meeting agenda include: election of directors, approval and ratification of the action of the officers and directors for the previous year, and adoption of salary and bonus plans for the coming year.

The date of the annual meeting is usually specified in the by-laws. The annual meeting can be held anywhere and anytime. Generally, however, the annual meeting is at or near the close of the corporation's taxable year.

A written or printed notice of each meeting, stating the place, day, and hour of the meeting is sent to each shareholder. By statute, this notice must be sent to each shareholder at his last known address not less than 10 days nor more than 50 days before the proposed meeting date. The shareholder, however, may waive this requirement.

Special meetings may be called by the board of directors, the holders of one-tenth or more of the outstanding voting shares, or by anyone else authorized in the by-laws to call special meetings. A notice must also be sent to each shareholder stating the purpose, time, and place of the special meetings. Here again, the shareholder may waive the requirement.

Voting. *In all matters, other than the election of directors*, a shareholder is entitled to one vote for each share of stock he holds. The shareholder vote is determined simply by counting the number of shares for or against each position. Voting in this manner is known as straight voting.

Voting for directors is more complicated. *Shareholders are required to vote cumulatively for directors.* This means that each share of stock is entitled to as many votes as the number of directors to be elected. For example, if three board

of directors are to be elected, a shareholder who owns one share of stock is entitled to cast three votes. The shareholder may then cumulate his votes. That is, the shareholder may cast his three votes for one director or he may divide his three votes among the directors in any manner he chooses. The following formula can be used to determine how many votes a shareholder must have to elect a director to the board:

$$\frac{\text{Total number of shares voting at election} \times \text{Number of directors shareholder seeks to elect}}{\text{Total number of directors to be elected} + 1} + 1 = \text{Number of shares needed}$$

Suppose that Farmer Jones incorporates his farm operation. A total of 100 shares of common stock are outstanding. Farmer Jones owns 51 shares, his daughter, Sarah, owns 23 shares, and his son, John, who operates the farm, owns 26 shares. A three-man board of directors is to be elected from a field of four candidates. Therefore, a total of 300 votes (100 shares X 3 directors) can be cast: Farmer Jones is entitled to 153 votes (51 shares X 3 directors), his daughter Sarah to 69 votes (23 shares X 3 directors), and his son John to 78 votes (26 shares X 3 directors). Each shareholder can vote his entire block of shares for one director or divide them among the four candidates.

A minimum number of 26 shares (78 votes) is needed to elect one director to the corporation. Since Sarah owns only 23 shares, she is unable to elect a director of her choice. On the other hand, John, who owns exactly 26 shares can elect one of the three directors by casting his entire 78 votes for the director of his choice. Farmer Jones can elect the other two directors by splitting his 153 votes between two candidates; 76 votes for one and 77 votes for the other.

The reason for requiring cumulative voting in the election of directors is to assure the minority shareholders some representation on the board. Suppose in the above example, straight voting, rather than cumulative voting, was used. That is,

each director would be voted on separately. Farmer Jones would be able to cast 51 votes for each director while the son and daughter together could only cast 49 votes for each director. Therefore, Farmer Jones would have been able to elect all three directors. By requiring cumulative voting, John can cast his entire block of votes for one director and thereby gain representation on the board of directors.

Greater-Than-Majority Control. The majority shareholders do not have unbridled control over the corporation. The majority must refrain from using their power to obtain any special advantage for themselves, or to produce corporate action of any kind that is designed to prejudice the minority shareholders. They must exercise their control for the benefit of all shareholders.

For example, the majority cannot prevent the board of directors from paying dividends, when there are ample funds available, for the sole purpose of forcing the minority shareholders to sell their stock at deflated values. Nor can the controlling shareholders amend the articles or by-laws for the sole purpose of interfering with the minority's representation or voting rights.

The by-laws or articles of incorporation may fix voting and quorum requirements, at a greater-than-majority control figure, including unanimity. Such provisions may be used to provide minority shareholders the veto power over business decisions which are adverse to their individual interests. For instance, a requirement of approval by the holders of 80% of the shares obviously empowers a person holding 21% of the shares to prevent shareholder action.

The limitations and disadvantages of high vote requirements should not be overlooked. They give the minority shareholder only a veto power and do not enable minority shareholders to affirmatively determine policy. Since the veto substantially increases the possibility of deadlock and frustration of basic corporate objectives, its use may be detrimental rather than beneficial to the close corporation.

Other Control Devices. A number of devices can be utilized to obtain control over corporation management and selection of its directors. These devices include:

1. *Classification of Stock.* The articles of incorporation can provide for several classes of stock with different voting powers, rights to dividends, rights on liquidation, and other qualities. Some shares may be common while others are preferred. Each share of common stock has the right to vote in all elections for directors. A corporation may provide in its articles that preferred shareholders shall have no right to vote.

2. *Classified Board of Directors.* One way to assure that all or several shareholders in a close corporation will be represented on the board of directors is to create two or more classes of stock and provide that each class shall elect a specified number of directors. For example, class A common stock might be given the power to elect three directors and class B common stock the power to elect two.

If all the shares in a class are issued to one person, he will be able to transfer 49 percent of his shares and still retain the power to elect all the directors in that class. This arrangement can facilitate estate planning since the holder of a class can give shares to his family or others without loss of control as long as he retains more than half the shares in the class.

One disadvantage of issuing common and preferred stock or classifying shares is that the corporation will not be able to elect Subchapter S treatment for income tax purposes. (See earlier discussion in Article IV - Stocks and Bonds).

3. *Shareholder Voting Agreement.* The most frequently used control device in close corporations is a shareholder's voting agreement. A majority, minority, or all of the shareholders may enter into the agreement. The typical shareholder agreement provides how each shareholder will vote his shares in an election of directors. The agreement may also predetermine such matters as employment, compensation, or dividend policy provided it accomplishes a valid corporate purpose and does not adversely affect minority interests.

4. *Voting Trusts.* Any number of shareholders may create a voting trust by entering into an agreement and transferring title to their shares to voting trustees. The trustee will issue certificates of beneficial interest, called "voting trust certificates," to the shareholders. The trustee then votes

the share in accordance with the terms of the trust agreement.

A shareholder's agreement is usually preferable to a voting trust for allocating control in a close corporation. A voting trust has a limited duration of 10 years. Shareholder agreements can be established for any length of time. Furthermore, a voting trust is more complicated to establish than a shareholder agreement. A voting trust involves the selection of voting trustees, transfer of shares to the trustees, and the issuance of voting trust certificates.

5. *Proxies.* A shareholder may vote in person or by proxy. A proxy is a written statement allowing another person, usually another stockholder, to vote his stock.

Article II (Directors)

Authority and Function

The corporation business and affairs are managed by the board of directors. Typical examples of policy matters handled by the board include:

- a. Acquisition of additional farm or ranch land, equipment, etc.
- b. Methods of financing additional capital expansion, (i.e., issuance of stocks, bonds, notes).
- c. Determination of management and marketing policies (i.e., what crops will be produced, when they will be sold, etc.).
- d. Dividend and other financial policies.
- e. Selection, supervision, removal, and compensation of officers, employees, and agents.

Selection and Removal of Directors

Number. There is no minimum number of directors required by statute. For the corporation with a sole shareholder, only one director need be appointed. In a family farm corporation it is common to have as many directors as there are shareholders. In this way, each minority shareholder is given the opportunity to be represented on the board. The number of directors can be changed by an amendment of the by-laws.

Qualifications. There are no statutory qualifications concerning those who may serve as corporate

directors. Directors need not be state residents or corporation shareholders. However, the by-laws can establish any set of qualifications for a director. Any change in qualifications made in the by-laws or articles of incorporation cannot affect incumbent directors during the term for which they were elected.

Vacancies. The board of directors has the exclusive right to fill vacancies on the board by a majority vote of remaining board members. A director elected to fill a vacancy serves for the unexpired term of his predecessor. On the other hand, shareholders are entitled to fill new directorships created by an amendment to the by-laws or articles of incorporation.

Removal. Any director may be removed, with or without cause, by a vote of a majority of the shares entitled to vote. However, a director cannot ordinarily be removed if the votes cast against removal would have been sufficient to have elected him or her to office if they had been cast cumulatively. For example, suppose three directors are elected annually to the Jones corporation. At a special shareholder's meeting, 51 shares of stock vote to remove Director A while 49 shares of stock vote against his removal. Even though a majority voted for removal, Director A would not be removed since the votes cast against removal would have been enough to elect him to office if they had been cast cumulatively.

How the Board Acts

Board Meetings. Directors must act collectively at a duly convened meeting. Generally, directors should act as a group and not as individuals when performing their management duties. However, it is not always possible to wait and act at a meeting. Illness, vacations, or the urgency of matter may require individual board members to act without a meeting. When action is taken without a board meeting, all directors should later sign a written consent approving such action. Any informal action approved by all the board members cannot later be repudiated by the corporation, shareholders, or directors.

Notice of Regular Meetings. The by-laws may prescribe whether regular meetings can be held with or without notice to board members. Board meetings are generally held immediately after and

at the same place as the annual meeting of the shareholders.

Notice of Special Meetings. Special meetings are convened to deal with extraordinary items that must be taken care of before the next annual meeting. The authority to call special meetings can be vested in the president or in individual directors. Notice of special meetings must be given to every director in advance of the meeting.

Waiver of Notice. The purpose of a notice is to inform the directors of a meeting. A director who attends a meeting where proper notice was not given cannot later object to the proceedings which took place at the meeting. A director who attends such a meeting will have waived his notice of the meeting, unless he attended the meeting solely to object to the legality of the meeting due to improper notice.

Quorum and Voting Requirements. A majority of the directors will generally constitute a quorum. However, the by-laws or articles of incorporation can provide that a greater number than a simple majority is required to constitute a quorum. If a quorum is present, the directors in attendance can act by a simple majority vote. Again, a higher voting requirement can be provided in the by-laws or articles of incorporation. Each director is entitled to one vote regardless of the number of shares he or she may own.

Minutes of the Meetings. Every corporation is required by statute to keep minutes of the board of directors and shareholders meetings. The minutes should contain, at a minimum the following information:

1. Names of persons present at meeting.
2. Whether or not a quorum was present.
3. Nature of the meeting—regular or special.
4. Whether minutes of last meeting were read and approved or that reading was dispensed with.
5. Reference to reports given by officers.
6. Action taken upon reports of officers or other committees of the board.
7. Other matters taken up at the meeting.
8. Adjournment.

Article III (Officers)

Authority and Function

The officers are the duly authorized agents of the corporation. They have the power to perform the regular corporation business duties, to spend money on behalf of the corporation, and to maintain adequate records of their transactions.

Corporate Officers

Officers of a corporation consist of a president, one or more vice-presidents, a secretary, and a treasurer. The board of directors may also serve as the corporation officers. Separate officers may, however, be elected or appointed to their positions by the board of directors. If desired, the by-laws may provide some other method of selecting officers.

One person may hold all four offices. Thus, it is entirely possible for a one person farm corporation to exist in Nebraska. One person can serve as sole shareholder, director and hold all four offices in the corporation.

a. President. The president is the corporation's chief executive officer. His duties include the general supervision and control of the business, presiding at meetings of shareholders and directors, and executing contracts authorized by the board.

b. Vice-President. In the absence or disability of the president, the vice-president assumes the duties of the president.

c. Secretary. The secretary is responsible for keeping minutes of shareholders' and directors' meetings, giving corporate notices, and keeping a register of the names and addresses of the shareholders. The secretary may also affix the corporate seal to any conveyance of real estate. However, the use of a seal is no longer required to validly convey land by a corporation in Nebraska.

d. Treasurer. The treasurer is responsible for keeping a complete record of all financial transactions, and for receiving and disbursing corporation funds. The treasurer may want to make use of a professional accountant to help maintain an adequate record of the farm corporation's transactions. A good accountant not only assists in the preparation of financial statements and tax returns but can offer advice for minimizing the corporation's and shareholders' future taxes.

Removal. Any officer may be removed by the board of directors whenever the best interests of the corporation will thereby be served. However, removal will not affect any contract rights existing between the corporation and the officer.

CONCLUSION

Incorporating a business which has traditionally been managed by a single individual or small group of individuals represents a substantial change in business philosophy. A business that was at one time operated on an informal basis will be subject to the complexities of corporate procedures and the specific requirements of the Internal Revenue Code for corporations. Election of a board of directors, annual meetings, separate record keeping of corporate transactions, and filing annual reports with the state are common corporate formalities. The farm or ranch family should carefully consider whether the benefits of incorporating the business outweigh the costs and disadvantages. For more information relative to the pros and cons of incorporation, see North Central Regional Extension Publication No. 11, *The Farm Corporation*.

GLOSSARY OF TERMS

Articles of Incorporation—Formal charter provisions of the corporation. The articles must be filed with the Secretary of State in order to conduct business as a corporation.

Basis (Shareholder)—Cost of property with adjustments for such items as depreciation and improvements. The basis for inherited property, however, is different. The basis for inherited marketable stock and bonds is their market value as quoted in newspapers as of December 31, 1976. For other inherited property, such as stock in a closely held farm or ranch corporation, its basis will be determined according to a statutory formula which estimates the market value of the property as of December 31, 1976.

Board of Directors—Persons elected by the shareholders to manage the property and business affairs of the corporation.

Bonds—Debt secured by a lien (i.e., mortgage) on specific corporate assets.

Buy-Sell Agreement—Contract for the sale of a shareholder's stock, either to the corporation or to other shareholders.

By-laws—Document which establishes the routine operating procedures for the shareholders, directors, and officers. The basic provisions in the by-laws include: procedures relating to meetings, voting requirements, and the duties and responsibilities of the shareholders, directors, and officers.

Closely-held Corporation—Corporation owned by a limited number of shareholders. Also referred to as a "close" or "closed" corporation.

Common Stock—The ordinary stock of the corporation which entitles the owner to share pro rata in dividend distributions and in asset distribution on dissolution without priority or preference over any other stock.

Corporation—A legal entity created by state law which is composed either of a single person or a collection of individuals. The corporation is a separate and distinct legal entity from its shareholders. The principal characteristics of a corporation include: 1) the power to make contracts, to sue or be sued, and to own or convey property; 2) the shareholders liability is limited to the amount of their investment; 3) the management and control of corporate affairs is centralized in a board of directors and officers acting under the board's authority; and 4) the corporation continues notwithstanding the death of its shareholders.

Cumulative Voting—System of voting which allows each share of stock as many votes as the number of directors to be elected. The total votes each share is entitled to may be cast for one director or divided among several directors.

Debenture—Unsecured corporate debt.

Dissolution—The voluntary or involuntary termination of the corporation's status as a legal entity. A corporation can voluntarily be dissolved by the affirmative vote of two-thirds of all the outstanding shares. Among other things, a corporation can involuntarily be dissolved when: 1) the directors are deadlocked in the management of the corporation; 2) the shareholders are deadlocked in voting power; 3) the directors or those in control of the corporation are acting fraudulently, or oppressively; 4) the corporation is insolvent; 5) failure to pay the corporate occupational tax.

Dividends—Any pro-rata distribution of cash, property, or other shares (stock dividend) paid to shareholders out of the corporation's earnings and profits.

First Option—A provision in the articles of incorporation or a separate shareholder agreement which provides that whenever a shareholder desires to sell his stock he must first offer the shares to the corporation or other shareholders before offering them for sale to non-shareholders.

Liquidation—The process of winding up the corporation's affairs by paying the corporate debts and distributing the remaining assets to the shareholders.

Officers—The duly authorized agents of the corporation who are selected by the board of directors to conduct the regular business of the corporation. The officers consist of a president, one or more vice-presidents, secretary, and treasurer.

Par value—Amount stated on stock certificate at the time of issuance.

Preemptive Rights—Right of each existing shareholder to purchase a proportionate part of any new stock issuance.

Preferred Stock—Class of stock which is given a preference over other classes of stock in regard to dividends and rights on liquidation of the corporation. Preferred stock may be either voting or non-voting.

President—Chief executive officer of the corporation whose duties include the general supervision of the business, presiding at meetings of shareholders and directors, and executing contracts authorized by the board of directors.

Proxy—A written statement authorizing another person, usually another shareholder, to vote one's stock.

Publicly Held Corporation—Corporation whose shares of stock are owned by the general public and are publicly traded.

Secretary—Corporate officer who is responsible for keeping the minutes of shareholder's and director's meetings, giving corporate notices, and keeping a register of the names and addresses of the shareholders.

Share of Stock—Ownership interest in a corporation which entitles the holder to certain rights in the management, profits, and assets of the corporation. Also referred to as stock.

Shareholder or Stockholder—A person who owns shares of stock in a corporation.

Shareholder Voting Agreement—An agreement among the shareholders which provides how each shareholder will vote his shares of stock.

Subchapter S Corporation—A closely-held corporation which elects to have corporate earnings and profits taxed directly to the shareholders. To qualify as a Subchapter S, the corporation must have 10 or fewer shareholders and only one class of stock. After five years, the number of shareholders in a Subchapter S corporation can be increased to 15.

Treasurer—Corporate officer who is responsible for keeping a complete record of all financial transactions and receiving and disbursing corporate funds.

Vice-President—Corporate officer who assumes the duties of the president in his absence.

APPENDIX

STATE OF NEBRASKA 1978 DOMESTIC CORPORATION OCCUPATION TAX REPORT (for calendar year commencing 1/1/78)

(For use of Secretary of State's office)

Report No. _____

Receipt No. _____

☐ Check ☐ Cash ☐ M O

Excerpt of Sec. 21-302 RRS Nebr. 1974: This report shall show (1) exact corporate name, (2) location of registered office, (3) names of president, secretary, treasurer, and members of the board of directors, with street address of each.

ALL ITEMS MUST BE COMPLETED:

1. Exact Corporate Name
(as stated in Articles of Incorporation or most recent Amendment)

2. President
Name Street Address City, State Zip Code

Secretary
Name Street Address City, State Zip Code

Treasurer
Name Street Address City, State Zip Code
(If Secretary and Treasurer are one and the same, please state.)

Director
Name Street Address City, State Zip Code

Director
Name Street Address City, State Zip Code

Director
Name Street Address City, State Zip Code
(All directors must be named. Additional blanks are provided on reverse of this form. Please avoid attachments.)

3. Nature of Business

4. The Registered Office is located at Nebraska
Street Address, City Zip Code

and the name of the Registered Agent at such address is
(*Address in Item 4 shall be complete, using full street address. A box number is acceptable only in those cases where street addresses are not available.)

Sec. 21-313 RRS Nebr. 1974: The report and remittance must be submitted on or before August 1st, or the corporation shall be automatically dissolved as of August 2, 1978, as required by law.

Complete both items:

Amount of Paid-up Capital Stock \$

Occupation Tax Fee (schedule on reverse) \$

I HEREBY SWEAR THAT THIS REPORT HAS BEEN EXAMINED BY ME AND, TO THE BEST OF MY KNOWLEDGE AND BELIEF, SAID REPORT IS TRUE AND COMPLETE.

Signature and title of president, or vice president, or secretary, or treasurer required:

Dated By

Title

Receipts are computer printed for the occupation tax of each individual corporation. Therefore, a separate monetary instrument, such as check, money order, etc., must be tendered for each corporation.

Please make checks payable to: ALLEN J. BEERMANN, Secretary of State
Mailing Address: Room 2304, State Capitol Building, Lincoln, Nebraska 68509

Additional Directors:

Director	Name	Street Address	City, State	Zip Code
Director	Name	Street Address	City, State	Zip Code
Director	Name	Street Address	City, State	Zip Code
Director	Name	Street Address	City, State	Zip Code
Director	Name	Street Address	City, State	Zip Code

OCCUPATION TAX FEE SCHEDULE

Amount of Paid-Up Capital Stock		Tax Fee
\$ 0.00 —	\$ 10,000.00	\$ 10.00
10,000.01 —	20,000.00	15.00
20,000.01 —	30,000.00	22.50
30,000.01 —	40,000.00	30.00
40,000.01 —	50,000.00	37.50
50,000.01 —	60,000.00	45.00
60,000.01 —	70,000.00	52.50
70,000.01 —	80,000.00	60.00
80,000.01 —	90,000.00	67.50
90,000.01 —	100,000.00	75.00
100,000.01 —	125,000.00	90.00
125,000.01 —	150,000.00	105.00
150,000.01 —	175,000.00	120.00
175,000.01 —	200,000.00	135.00
200,000.01 —	225,000.00	150.00
225,000.01 —	250,000.00	165.00
250,000.01 —	275,000.00	180.00
275,000.01 —	300,000.00	195.00
300,000.01 —	325,000.00	210.00
325,000.01 —	350,000.00	225.00
350,000.01 —	400,000.00	250.00
400,000.01 —	450,000.00	275.00
450,000.01 —	500,000.00	300.00
500,000.01 —	600,000.00	340.00
600,000.01 —	700,000.00	380.00
700,000.01 —	800,000.00	420.00
800,000.01 —	900,000.00	460.00
900,000.01 —	1,000,000.00	500.00
1,000,000.01 —	2,000,000.00	800.00
2,000,000.01 —	3,000,000.00	1,100.00
3,000,000.01 —	4,000,000.00	1,400.00
4,000,000.01 —	5,000,000.00	1,700.00
5,000,000.01 —	6,000,000.00	2,000.00
6,000,000.01 —	7,000,000.00	2,300.00
7,000,000.01 —	8,000,000.00	2,600.00
8,000,000.01 —	9,000,000.00	2,900.00
9,000,000.01 —	10,000,000.00	3,200.00
10,000,000.01 —	15,000,000.00	4,500.00
15,000,000.01 —	20,000,000.00	5,500.00
20,000,000.01 —	25,000,000.00	6,500.00
25,000,000.01 —	50,000,000.00	7,750.00
50,000,000.01 —	100,000,000.00	8,000.00

When paid-up capital stock exceeds \$100,000,000 8,250.00

FARM CORPORATION REPORT

The Nebraska Legislature in the 1975 Session passed Legislative Bill 203 (Farm Corporation Reporting Act) which was subsequently signed by the Governor and became law on August 24, 1975. The various sections of the bill have now been assigned Section Numbers and can be found in the 1975 Supplement to the Statutes as Section Numbers 76-1501 thru 76-1506.

Nebraska Statute 76-1501, which was Section (1) of LB 203, states succinctly the purpose of the Farm Corporation Reporting Act. I wish to call to your attention the fact, that this law and this reporting form does not in any way replace nor is it a substitute for the Annual Domestic or Foreign Occupation Tax Report or the Biennial Non-profit Report. Corporations falling within the provisions of LB 203 (Farm Corporation Reporting Act) will be required to file either the Annual Occupation Tax Report or Non-profit Biennial Report and The Farm Corporation Reporting Act Form.

Please note that all of the instructions for completing this form are found either in the Statutes, the adopted Rules and Regulations which are reproduced or on the Reporting Form itself. There is no filing fee required for filing the Annual Farm Corporation Reporting Act Form.

I do call to your specific attention, additionally, the penalty provisions that appear in Nebraska Statute 76-1506 and Nebraska Statutes 76-402 thru 76-415, Reissue Revised Statutes of Nebraska, 1943, relating to real property and Aliens. These are very important sections of the law and should be discussed with your legal counsel if Aliens or Alien ownership is involved in your particular corporation.

Finally, if you have any questions relating to the manner of submitting forms under this new law or if you desire additional information, please contact: Secretary of State, Suite 2300, State Capitol, Lincoln, Nebraska 68509. Telephone number is 402/471-2554.

Respectfully submitted,

Allen J. Beermann

ALLEN J. BEERMANN
Secretary of State

**RULES AND REGULATIONS
DEPARTMENT OF STATE
Administrative Rules Governing
FARM CORPORATION REPORTING ACT
L. B. 203 1975 Legislature
Source Reference: 76-1505, 1975 Supp.**

76-1505 Within ninety days after the effective date of this act, the Secretary of State shall provide all forms necessary to carry out the provisions of this act and shall make rules and regulations relating to the manner of submitting reports.

1. The Farm Corporation Act reporting forms shall be on white paper with black ink for the year 1975. The Secretary of State shall have the authority from year to year to change the color of the forms for the purpose of color coding by year.
2. The format other than year and color of the forms are hereby made a part of these rules and regulations and are attached as an addendum for public record purposes.
3. The Secretary of State shall distribute blank forms by mail, by phone request, personal request and they shall be made available to the general public through the offices of the various county clerks in the State of Nebraska. The forms for each reporting year shall be made available beginning November 1 each year for the ensuing year. There shall be no charge for the Farm Corporation Act reporting forms.
4. The forms shall be so designed that they will appear in duplicate with the original being submitted to the office of the Secretary of State and the duplicate being retained by the reporting corporation or their designate.
5. Farm Corporation Act reporting forms shall be submitted no later than January 1, 1976 and each year thereafter. Inasmuch as January 1 is a Federal and State Holiday (New Year's Day) said reports will not be considered delinquent if they are postmarked or received by January 2 each year.
6. The Secretary of State in designing the reporting forms shall have the authority to request the business phone number or numbers of the reporting corporation, its officers or agent, including the area codes. The Farm Corporation Act forms when they are completed shall be signed in black or blue ink by any officer of the corporation or its registered agent.
7. The Farm Corporation Reporting Act forms may be prepared by any individual or individuals on behalf of the corporation such as CPA's, attorneys and the corporate administrative officers. When the Farm Corporation Reporting Act form is prepared by said individuals the preparer of the report shall sign and give his or her address. The corporate officer or registered agent is still required to sign the report even though it is prepared by other individuals.
8. The officer or registered agent signing the report must do so in the presence of a notary or other officer who has the authority to attach and affix a seal. Further, the Secretary of State shall prepare the report forms in the format of an affidavit to accomplish this purpose.
9. The Secretary of State shall have full authority to designate, design or determine the best method for indexing the Farm Corporation Act forms. He shall have administrative authority to file alphabetically, numerically, use log books, microfilm and/or place on a computer program.
10. The Secretary of State shall when each report is filed send a "letter of receipt" to each corporation filing reports under the provisions of 76-1501 through 76-1506.
11. The Secretary of State shall have the authority to from time to time make administrative changes in the format of the Farm Corporation Reporting Act forms.

1977 REPORT
Due January 1, 1978

FARM CORPORATION REPORT

File No. _____

PLEASE TYPE OR
PRINT LEGIBLY

Send Form to
Allen J. Beermann
Secretary of State
Corporation Division
State Capitol
Lincoln, Nebraska 68509

STATE OF _____)
COUNTY OF _____) SS

Type of Corporation in Nebraska

☐ Foreign ☐ Domestic ☐ Non-Profit

NAME OF CORPORATION _____

CORPORATION ADDRESS			REGISTERED AGENT		
Other Trade Name Used (if any)			Name		
Street			Street		
City	State	Zip	City	State	Zip
()			()		
Phone			Phone		

Land used for growing of crops or the keeping or feeding of poultry or livestock.

LOCATION	TOTAL ACREAGE	COUNTY	LOCATION	TOTAL ACREAGE	COUNTY

☐ Check block if an alien Names and address of officers, directors, and shareholders owning ten percent (10%) or more of the stock.

Percentage of Board of Directors that are aliens. _____ %

<input type="checkbox"/>	Name	Title	Address	City	State	Zip
<input type="checkbox"/>	Name	Title	Address	City	State	Zip
<input type="checkbox"/>	Name	Title	Address	City	State	Zip
<input type="checkbox"/>	Name	Title	Address	City	State	Zip
<input type="checkbox"/>	Name	Title	Address	City	State	Zip

RECEIPT OF FILING

Please Print or Type

1977 Report

Farm Corporation Report

Name of corporation

Name of registered agent

Address

City

State

Zip

File Stamp for Office Use Only

Name and address of aliens owning ten percent (10%) or more of voting stock.

Name	Address	City	State	Zip
Name	Address	City	State	Zip
Name	Address	City	State	Zip
Name	Address	City	State	Zip

Give the name and address of each person residing on the farm or actively engaged in farming and owning ten percent (10%) or more of the voting stock.

Name	Address	City	State	Zip
Name	Address	City	State	Zip
Name	Address	City	State	Zip

Signature of Any Officer or Registered Agent (Title)

Subscribed and sworn to before me this _____ day of _____ 197_____.

Notary Public

SEAL

Commission Expires _____

Name and address and signature of preparer of this report (other than officer or registered agent).

Name			
Title			
Address			
City	State	Zip	

If additional space is required, please use an additional sheet of paper and add as an addendum.