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Bill Analysis

Version: As Introduced

Primary Sponsor: Rep. Swearingen

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SUMMARY

- Requires nonprofit corporation directors to be adult natural persons (i.e., individuals rather than business entities).
- Authorizes a committee consisting of one or more directors of a nonprofit corporation to create a subcommittee, unless otherwise provided in the articles, the regulations, or the resolution of the original committee.
- Specifies the fiduciary duty required of an officer of a nonprofit corporation.
- Provides that neither a director nor an officer is a trustee with respect to the corporation or any property held or administered by it.
- Expands the circumstances in which provisional directors may be appointed.
- Revises the standards for determining liability of directors when nonprofit corporations make loans and the interest rate relating to that liability.
- Establishes that a loan made in violation of the law governing nonprofit corporation does not affect the borrower's liability on the loan.
- Authorizes a majority of the incorporators of a nonprofit corporation to amend the articles of incorporation if (1) the articles do not name initial directors, (2) a meeting of voting members has not yet occurred, and (3) the incorporators have not yet elected directors.
- Establishes to what extent a certificate issued by the Secretary of State confirming that a nonprofit corporation is in good standing is conclusive evidence.
- Limits the liability of those who provides goods to, or performs services for, nonprofit corporations or their members to only the person or entity to whom the goods or services were provided.

- Provides an exception to religious organizations excluded from the definition of an unincorporated nonprofit association in the Unincorporated Nonprofit Association Law.

DETAILED ANALYSIS

The bill makes numerous changes to the Nonprofit Corporation Law, including changes related to director qualifications and appointment, director and officer liability, and certificates of good standing from the Secretary of State. It also makes one minor change to the Unincorporated Nonprofit Association Law.

Director qualifications

The bill requires nonprofit corporation directors to be natural persons and adults (i.e., individuals over 18 and not business entities). Current law simply requires directors to have the qualifications, if any, stated in the nonprofit corporation's articles of incorporation or regulations.[1]

Director duties

Evaluating duties

The bill modifies the application of a list of items directors may consider when performing their duties as directors. Specifically, it limits application of the list to directors' consideration of what is in the corporation's best interest. Under current law, the list applies to consideration of what is in the corporation's best interest or not opposed to it. The bill limits application only to consideration of what is in the corporation's best interest.

Continuing law, unchanged by the bill, requires nonprofit corporation directors to perform their duties as directors in good faith, in a manner they reasonably believe to be in or not opposed to the corporation's interests.[2]

Directors are not trustees

The bill adds a provision to the law detailing nonprofit corporation directors' duties explaining that directors are not trustees with respect to the corporation or any property held by it, regardless of whether the property is subject to donor restrictions. The provision only applies to directors acting in their capacity as director, not in any other role.[3]

Committees and subcommittees

The bill authorizes any committee consisting of one or more nonprofit corporation directors to create subcommittees and delegate any or all of the committee's power to the

[1] R.C. 1702.27(A)(3).

[2] R.C. 1702.30(B) and (F).

[3] R.C. 1703.30(G) and (H).

subcommittee. This authority, however, may be withheld by the corporation's regulations or the resolution that created the original committee.

The bill does not affect existing law's provisions for the creation of committees by nonprofit corporation boards of directors. It only creates the new authority for those committees to create subcommittees.[4]

Provisional directors

The bill expands provisions of existing law that allow appointment of provisional directors for nonprofit corporations. Currently, a provisional director can be appointed by a court upon the complaint of at least one fourth of the directors. In order to make an appointment, the plaintiffs must establish that the continued operation of the corporation is substantially impeded or impossible because of irreconcilable differences among the existing directors.

The bill expands eligible complainants to include at least one fourth of a nonprofit corporation's voting members. It also expands the circumstances allowing appointment to include situations where there are no directors and the voting members are unable to elect directors, making the continued operation of the corporation substantially impeded or impossible.[5]

Corporate officers

Fiduciary duties

The bill establishes a default fiduciary duty that applies to a nonprofit corporation's officers (e.g., president, treasurer, etc.) unless the corporation's articles or regulations, or a written agreement with an officer, establishes *additional* fiduciary duties.[6]

These new provisions largely mirror existing provisions regarding fiduciary duties for directors. Under them, officers must perform their duties in good faith, in a manner reasonably believed to be in or not opposed to the corporation's best interests, and with the care an ordinarily prudent person in a like situation would use. When performing their duties, officers may rely on information, including financial statements and other data, prepared or presented by either:

- The corporation's directors, officers, or employees who the officer in question reasonably believes to be reliable and competent;
- Counsel, accountants, and other professionals working in their scope of practice.[7]

[4] R.C. 1702.33(G).

[5] R.C. 1702.521.

[6] R.C. 1702.341(A).

[7] R.C. 1702.341(B).

Liability for failure to fulfill fiduciary duties

In order for a court to find that a corporate officer failed to act in good faith, in a manner reasonably believed to be in or not opposed to the corporation's best interests (i.e., to have violated the relevant fiduciary duty), the failure must be proved by clear and convincing evidence. Clear and convincing evidence is evidence indicating something is highly likely or reasonably certain. That is a higher standard than the normal evidentiary standard in civil cases, which is a preponderance of the evidence (the evidence for a proposition outweighs the evidence against, even if only slightly). The bill further provides, however, that an officer will not be considered to be acting in good faith if the officer knows something about the matter in question that would make reliance on information provided by other corporate personnel or professional advisors unwarranted (see "**Corporate officers – Fiduciary duties**," above).[8]

The bill has additional provisions for actions seeking to make a nonprofit corporation's officer liable for money damages (as opposed to found to have violated the relevant fiduciary duties for other purposes, which is what the preceding paragraph addresses). In those cases, it must be shown by clear and convincing evidence that the officer's action or inaction was undertaken with deliberate intent to cause the corporation injury or with reckless disregard for its best interests. The bill does provide that this requirement can be nullified by the corporation's articles or regulations or a written agreement with the officer in question.[9]

Officers are not trustees

To coincide with its new fiduciary duty standards, the bill provides that nonprofit corporate officers are not trustees with respect to any property held or administered by the corporation, including property that is subject to donor restrictions.[10]

Limitation of fiduciary duty provisions

The bill limits its new fiduciary duty provisions for corporate officers to those instances where they are acting as corporate officers. They do not apply when corporate officers are acting in any other capacity aside from that of corporate officer.[11]

Director and officer liability

Under continuing law, directors and officers of nonprofit corporations are not personally liable for the corporation's obligations. They may, however, be liable to the corporation itself under certain circumstances. Those are where there is a distribution of corporate assets to members contrary to law or the corporation's articles, where there is a distribution of assets

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[8] R.C. 1702.341(C), *Black's Law Dictionary* (11th ed. 2019), and *Ohio Trial Practice (Baldwin's Ohio Handbook Series)* § 9:3 (2021 ed.).

[9] R.C. 1702.341(D).

[10] R.C. 1702.341(E).

[11] R.C. 1702.341(F).

without making sure creditors are paid when winding up the corporation's affairs, and when the corporation makes certain loans. The bill modifies the provisions regarding loans.

Under current law, directors and officers may be liable to the corporation when, other than in the usual conduct of the corporation's affairs or in accordance with the corporation's articles, the corporation makes a loan to a corporate officer, director, or member. The bill removes the liability application for loans to members. It also removes the liability provision altogether if, at the time of the loan, the majority of disinterested directors voted for the loan after taking into account its terms and provisions and determining that it could reasonably be expected to benefit the corporation.

The bill also adjusts the interest rate applicable to a director's liability on improper loans from 6% annually to the federal short-term rate as determined by the Tax Commissioner under continuing law. Finally, it adds a new provision establishing that even if a loan is made in violation of the nonprofit corporation law, that violation does not affect the borrower's liability on the loan.[12]

Amendment of articles

Nonprofit corporations are formed when articles of incorporation are filed with the Secretary of State. They may be filed by one or more persons, called incorporators, and may name the corporation's initial directors. Once incorporated, articles may be amended by a majority vote of the corporation's voting members. The bill adds a new provision allowing articles of incorporation that do not name the initial directors to be amended, if certain circumstances are met. Specifically, under the bill, the incorporators may adopt an amendment to the articles at any time prior to both:

- A meeting of the corporation's voting members;
- Election of directors by the incorporators.[13]

Certificate of good standing

The bill adds a new provision of law establishing that a certificate of good standing issued for a nonprofit corporation by the Secretary of State is conclusive evidence of certain facts for seven days after it is issued. The facts the certificate demonstrates are:

- The Ohio nonprofit corporation's authority has not been limited by provisions of continuing law dealing with its termination or dissolution and the winding up of its affairs, provided that the person relying on the certificate has no knowledge that the corporation's articles have been canceled and the certificate is not presented as evidence against the state;

[12] R.C. 1702.55(A), (B), and (H), and R.C. 1343.03 and 5703.47, not in the bill.

[13] R.C. 1702.38(C)(1), and R.C. 1702.01, 1702.04, and 1702.20, not in the bill.

- That an out-of-state nonprofit corporation's license to do business in Ohio has not expired, been canceled, or been surrendered.[14]

Providers of goods and services

The bill adds a new provision to the nonprofit corporation law providing that, absent express agreement, those who provide goods or services to a nonprofit corporation do not incur legal liability or owe any duties to the corporation's members or creditors, or the members' creditors, by reason of providing the goods or services. Similarly, the bill provides those who provide goods or service to a nonprofit's corporations members do not incur legal liability or owe any duties to the corporation or its creditors by virtue of providing goods or services to the members.[15]

Unincorporated nonprofit associations

In addition to the law governing nonprofit corporations, Ohio law governs **unincorporated nonprofit associations**. Those are unincorporated organizations, consisting of two or more members pursuant to an agreement for one or more common nonprofit purposes. Continuing law exempts several entities from the definition, including religious organizations. The bill permits religious organizations to opt in to the unincorporated association law by having the religious organization's governing principles specially state that the exemption does not apply.[16]

Edits made for clarity

The bill makes numerous edits to statutory language that makes that language clearer but does not substantively change the law.[17]

HISTORY

Action	Date
Introduced	02-01-22

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[14] R.C. 1702.53(D).

[15] R.C. 1702.531.

[16] R.C. 1745.05(M)(5).

[17] R.C. 1702.30(C) through (E).