



## **Organization of the Corporation**

### **Director's First Meeting**

- [Ratify the pre-incorporation actions of the Incorporator and first director](#)
- [Authorize the corporation to reimburse the person who paid the costs of incorporating](#)
- [Ratify the appointment of the Registered Agent](#)
- [Adopt the corporation Bylaws](#)
- [Adopt a form of stock certificate](#)
- [Give authorization for the corporate secretary to make all necessary filings](#)
- [Elect officers, directors and shareholders](#)
- [If you are going to be an S-Corporation, authorize the election of 'S' status](#)
- [Select a bank, and authorize the opening of a corporate bank account. You will also need to designate the person\(s\) who will be authorized to sign on the account](#)
- [Approve the Articles of Incorporation](#)
- [Issuance of the Stock](#)
- [Changes of the Guard](#)

Let's discuss these items briefly, to assure that you are clear on the purpose of each part.

### **Ratification of Pre-Incorporation Actions**

First, the ratification of the pre-incorporation actions. It is of supreme importance in the operation of your corporation that you maintain separation between your actions as an individual, and your actions on behalf of the corporation. Ultimately, this could be the difference between having your corporate veil pierced in a lawsuit, and having the corporation protect you from attack. Consequently, we begin the Corporation's life by beginning this necessary separation.

Incorporating the company is clearly an important corporate act, yet how could it be done pursuant to prior corporate authorization, if the corporation doesn't exist? Clearly, this is impossible. The answer to the dilemma is the ratification of the actions, after the fact, which has the effect of making them corporate actions, and not your personal actions.

### **Reimbursement of Costs of Incorporating**

The second item on our list follows from the first. The cost of incorporating cannot possibly be paid for out of the Corporation's bank account, since the corporation is not yet formed. Authorizing a reimbursement in the first meeting allows you to shift the costs over to the corporation as a reasonable and ordinary business expense.

## **Ratification of Resident Agent**

The third item is the ratification of the Resident Agent appointment. A Resident Agent for service of process is required before incorporation, yet this appointment must be authorized by the corporation, hence we again ratify it after the fact.

## **Adoption of the Bylaws**

Adoption of Bylaws, the fourth item, is one to which you should pay careful attention. You may have purchased a corporation from an incorporating company, in which you received Bylaws with your other materials. Before you just accept the boiler plate Bylaws without thinking, be sure that you review them and understand them. The corporation bylaws are designed to provide the day to day rules and regulations for your corporation's activities and internal workings. They set forth the dates and times of the annual meetings of shareholders and directors, the method of notice for these meetings, the abilities of the differing players to make amendments, and other decisions. All of these items are important for you to consider at this point, and critical for you to follow later. In order for you to operate the corporation after this time, you will need to have Bylaws adopted, so don't put off this step.

## **Adoption of Stock Certificates**

Sixth, is the adoption of stock certificates. This is simply the official designation of a particular form or design which conforms to your state's requirements, and will make it difficult for someone to come along with just any old blank form, and claim it as evidence of ownership. The Seal should be placed on a sample certificate, and included with the minutes of the meeting as an official sample for the corporation's records.

## **Authorization of Required Filings**

Seventh, authorizing the corporate Secretary to make all necessary filings will provide the necessary authorization to continue the organization process in compliance with applicable federal, state and local requirements for such things as Employer Identification Numbers, officers' lists, business licenses, and so on.

## **Election of Officers**

Eighth, the election of officers is certainly important. It may seem hard to imagine, but this step is often overlooked. Any time we are asked to help someone bring their

corporate records up to date, the first thing we do is to make a chart showing the shareholders, directors, and officers that show up on the various filings and documents that have been done, and compare them with the annual meetings which have (or have not) been held. The purpose for doing this is to determine if there were officers and directors for the corporation in any given year. Usually, there are years, or many years when the corporation transacted business, and didn't have any valid officers or directors. You should begin clean, and omit this fatal step now; elect officers.

## **Who Should Serve?**

At this juncture, we need to consider two basic questions, who should serve as director and who should serve as officer? Often, business people will have others serve in these capacities who really have minor roles in the business. As is the case in all phases of corporate organizations, you need to carefully consider what the purpose of the corporation is, and who really has a role to play in that purpose. For example, if you are starting up a new corporation to conduct your primary business, who is going to make the important decisions? You? Your children or other relatives?

Often, people with family businesses will appoint their older children in officers' positions. Sometimes, they even appoint them directors. What a sad day many people have when their disgruntled adult children figure out that they can fire their parents! Is that really what you want? Another example along these lines is the person who welcomes his new son in law to the family by making him a director or an officer. Worse yet, when he gifts his soon to be former son-in-law a large amount of stock. Let's face it, there are enough pitfalls in business without causing your own problems by awarding "honorary" titles by installing someone into a real office. Again, you must carefully consider what could eventually go wrong in the future before you make such appointments.

If it is your intention to maintain tight control over the business, then do not appoint other people to critical positions, unless you know that you can keep them under control. Always consider what could happen, even though you don't think that it will. Then and only then can you be secure in your new undertaking.

## **Adopt a Fiscal Year**

If you are planning to become an S Corporation, you will have to adopt a calendar year. A fiscal year for tax purposes will void your S election. If you are not planning on being an S Corporation, then give some thought to your fiscal year. Most people choose a calendar year because they are used to calendar years. If you have multiple corporations, however, a fiscal year can be an excellent tax planning device.

If you authorize a particular tax year in your first meeting, and then get with your tax advisor, and wish to change your fiscal year, you can do it, as long as you have not filed your first tax return. The corporation's first tax year must end within one year of the time

it first started doing business, and must be filed seventy-five days after that ending. At any time prior to the filing of that first return, you can change your fiscal year, as long as your first fiscal year is not longer than 365 days from the date on which you started doing business. Once the first return is filed by the corporation, the fiscal year can no longer be changed.

## **Types of Consideration In Exchange for Stock**

Stock is issued for cash, property, or services. Cash is fairly obvious as a form of consideration, but property and services will vary in form and substance. Property can take many forms, stock can be issued for tangible assets, such as office equipment, and real estate, or it can include such items as mental property, formulas, copyrights, trademarks, and so on. Services can be such things as actual work for the corporation, longevity, consulting, and service contracts. You may have a special circumstance which will fit into one of these categories which isn't mentioned, and yet could certainly be a valid consideration for the stock.

## **Issuance of the Stock**

The actual issuance of the stock is rather simple. You issue stock by corporate resolution. First you will need a resolution to authorize issuance, and then you will need to draft a resolution issuing a specific number of shares to a specific individual or individuals for a type of consideration, cash, property or services. The resolution need not state how much money is involved, just the particular type of consideration. As an accounting function, you will have an equity account, usual called "paid in capital" on your books which indicates the actual amount of cash, or the cash value of the property or services performed in exchange for the stock.

**All states require that corporations maintain a stock ledger as a record of share ownership.** Stock ledgers usually are in two steps. First is the Register of Original Certificate Issue, which performs much the same duty as a check register. It allows the secretary to keep track of your numbered certificates, so that at any time, he or she can determine where they are. The register will indicate to whom and when each issued certificate was issued, and when combined with the remaining blank or unused certificates in the record book, will indicate if any certificates are missing.

The second ledger that you will need to keep is called the Shareholder Ledger. The shareholder ledger is a separate ledger for each shareholder which indicates each stock transaction the shareholder has been involved in, and shows a running total of the shares each person owns. It also has the address of the shareholder. The shareholder ledger is what is used in determining who is entitled to vote in shareholder meetings, and how many shares each shareholder is entitled to. The address on the ledger is used for providing notices of meetings to each shareholder.

States will vary on whether or not copy of the shareholder ledger must be kept by the Resident Agent. You should contact your state's Secretary of State to find out what is required in this area.

## **Changes of the Guard**

There are several possibilities in this area. First, there is the fundamental matter of appointing officers. Next, there is the possibility that an officer may resign or be fired. Next, directors need to be appointed, they can resign and need to be replaced, and then, of course, they too can be fired. All of these actions are done through documented means. As most of these actions involve actions of the directors or shareholders, there are resolutions involved. Yet even a resignation requires some sort of written procedure, even if the officer quits verbally and stomps off in a huff, refusing to write anything down.

The reasons for this need of documentation are fairly obvious. In a corporation, everything depends on the roles we are playing at any given time, and upon our ability to prove (or disprove) it. With a partnership or sole proprietorship, this is not nearly as important, because those entities are synonymous with the individuals involved. Corporations, however are different, and anyone can claim to be an officer or director for various purposes. What we don't always consider is that people can also deny their truthful position when they want to wiggle out of something. Thus, not only is such documentation important from the simple perspective of formalities, it is critical for some very practical reasons as well.

## **Officers**

Election or appointment of officers is done by the directors. In their annual meeting, they elect the officers for the coming year. Yet, in the event that something goes awry during that time, they may have cause to replace an officer. The procedures are relatively simple. First, let's assume that an officer resigns.

Resignations can, of course come about for a variety of reasons. Let's first of all look at what happens when a resignation is friendly. The Treasurer resigns to pursue his or her dream to travel the world. The Treasurer would then submit a brief letter of resignation (usually given to the president, could be given to the board or secretary). The directors get together and draft a resolution accepting the resignation and appointing a new person to fill the unexpired term. The new Treasurer accepts in writing the appointment ( as all directors and officers should be required to do) and that is all there is to it.

## **Directors**

This area becomes a little more complicated than dealing with the officers, because we must involve the stockholders. Directors are appointed by stockholders in most cases. Yet, where there are no stockholders, the directors may appoint as many additional directors as the Bylaws permit, by consent to action. A consent to action is actually the

name of a resolution of the stockholders, and since there are no shareholders, and the directors are acting in their place, they would use a consent rather than a director's resolution. The consent to action uses the exact same format as a resolution, simply substituting the name.

There is another case in which the directors would elect directors, even while there are shareholders, and that is to fill an unexpired term, where a vacancy would have resulted from a termination, resignation or death. This appointment could also be made by the shareholders. We know you are wondering which is best, having the directors fill a vacancy, or having the shareholders do it. As a practical matter, this depends upon whether you are a director or a shareholder! Since directors serve at the pleasure of the shareholders, it would be a good idea for the directors not to be overly aggressive in this area.

Procedurally, resignations of directors should be handled in the same way as resignations of officers, with a written resignation being submitted and accepted by the shareholders, prior to the appointment of a new director. If your board of directors has not fallen below the minimum number set by the Articles, you aren't required to fill a vacancy.

Termination of a director is another matter. In almost all cases, the directors do not have this authority, so it must be done by the shareholders. Additionally, most state statutes require a super majority of the voting shares of the corporation to remove a director, usually two thirds, sometimes three quarters. While removal of a director can be done either in a meeting or by consent to action, if you have several shareholders, it would be wise to hold a meeting, so that the representation of the necessary percentages of shares can be fully demonstrated. Where there is only one shareholder, this would not be a problem.

## **Salaries**

Officers' salaries and directors' fees are also a matter for resolutions. Because officers are hired by the directors, the specifics of their compensation, including bonuses, benefits and salaries are all determined by the Board. As always, it is naturally understood that if there is no resolution, then the Board has not taken an action. This being the case, a corporation which has officers, benefits for officers and officers' salaries (or no officer salaries for that matter) needs to have documentation. A lack of documentation can make the corporation appear to be an alter ego in some cases, or in others it may appear that the officer(s) in question could be acting improperly. Some corporations also pay fees to directors for attending meetings. These fees are also documented with resolutions.

## **Purchasing**

Resolutions relating to purchasing can be minimal in number, or very numerous, depending on the degree of latitude the directors wish to give to the officers. Normally speaking, since the officers are charged with the responsibility of conducting the day to

day business of the corporation, they can make normal and necessary purchases without prior or specific Board approval. Yet in some cases, the directors may wish to limit the ability of officers to purchase. This limitation would be a matter of drafting and adopting a resolution. Limitations may be placed on types of purchases, dollar amounts, or most anything that the directors would deem necessary.

Out of the ordinary purchases, however, should always be approved by the directors. Such purchases would include new phone systems, re-tooling of a plant, purchases of company cars which are not otherwise provided for, real estate purchases, and so on. The rule of thumb would be set by a policy resolution. Policy which allowed for purchases in the ordinary course of regular business would then require by implication, resolutions for unusual purchases. For most small to medium sized companies where the players are more or less the same people in differing roles, this arrangement is the easiest one to handle.

## **Establishing a Principal Place of Business**

It is fair to say that in all cases, the establishing of a principal place of business is neither ordinary or regular in the course of a corporation's activities. It is something which seldom occurs, and may only occur once in the entire history of a company. Thus, an action of the Board is going to be necessary to authorize the move. In fact, it may even require a series of resolutions. Let's say that the corporation has maintained the same location for a number of years, but with the growth of the company, the current location is no longer big enough to get the job done. The Board may direct the president to look into a possible relocation. That's one resolution. Then the president reports back what he has found out. Then the Board tells the president to enter into negotiations with the landlord. Probably the Board will say that they would agree to a certain price, or certain terms. They may say that if the price and terms are met, than the president can go ahead and sign. All of this would be done by resolution. Remember that the Board's thinking and decisions are the purpose of resolutions.