THE NEW ARIZONA BUSINESS CORPORATION ACT

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Corporate law practitioners in Arizona have traditionally been burdened by the incompleteness and inadequacy of state law governing corporate affairs. Arizona's General Corporation Law[1] is silent in a number of important areas and treats others only superficially. Additionally, the paucity of Arizona appellate decisions on many corporate questions, the difficulty of determining the applicable common law,[2] and the lack of guidance offered by decisions of other jurisdictions with varying statutory corporate laws have magnified the problem. These deficiencies in Arizona corporate law have not only presented a potential deterrence to full industrial development in the state, but also have posed an obstacle to efficient operation of existing Arizona businesses.

With these considerations in mind, Arizona's General Corporation Law was completely restructured.[3] The new Arizona Business Corpo-

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1. ARIZ. REV. STAT. ANN. §§ 10-101 to -485 (1956), *as amended*, (Supp. Pamphlet 1975) (partially repealed by ARIZ. REV. STAT. ANN. §§ 10-001 to -149 (Supp. Pamphlet 1975) (effective July 1, 1976)).

Individual sections of the Arizona General Corporation Law will be cited in this article as ARIZ. REV. STAT. ANN. § 10-___ (1956). Where provisions of the general corporation law have been amended and appear in the 1975 supplementary pamphlet of *Arizona Revised Statutes Annotated*, they will be designated "former ARIZ. REV. STAT. ANN. § 10-___ (Supp. Pamphlet 1975)." The citation form throughout this Article for the new Arizona Business Corporation Act will be ARIZ. REV. STAT. ANN. § 10-___ (Supp. Pamphlet 1975).

2. ARIZ. REV. STAT. ANN. § 1-201 (1974) adopts the common law "only so far as it is consistent with and adapted to the natural and physical conditions of this state and the necessities of the people thereof, and not repugnant to or inconsistent with the constitution of the United States or the constitution or laws of this state, or established customs of the people of this state . . . ."

3. In response to the growing dissatisfaction with Arizona's corporation laws, a

ration Act,[4] which becomes effective on July 1, 1976,[5] represents the first general revision of Arizona's business corporation laws since territorial days.[6] The principal thrust of the new law is its expanded statutory coverage of corporate transactions.[7] Based on the Model Business Corporation Act [Model Act],[8] the new Act alters some provisions of

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Committee of the Section of Corporation Law of the State Bar of Arizona [the Bar Committee] was formed in the late 1960's to consider the preparation of a modern comprehensive business corporation law for presentation to the Arizona legislature. The most fundamental decision of the Bar Committee was that a complete restructuring of the present Arizona General Corporation Law, rather than further piecemeal revision, was required. The proposed legislation produced by the Bar Committee was introduced in the Thirty-first Arizona Legislature but failed to pass. S. 1097, 31st Ariz. Legis., 1st Reg. Sess. (1973). A modified form of the bill drafted by the Bar Committee, containing the results of compromises, was passed by the Thirty-second Legislature. Ch. 69, [1975] Ariz. Sess. Laws, 1st Reg. Sess. 240. The provisions on requirements for incorporation illustrate the nature of the procedural compromises. The Bar Committee's bill provided that corporate existence would begin upon the filing by the incorporators of the articles of incorporation in the office of the Arizona Corporation Commission without the exercise of any discretion by the commission and without subsequent publication. S. 1097, *supra* § 2. The final version adopted by the legislature, however, provides that the commission must determine that the articles conform to all legal requirements before filing them. ARIZ. REV. STAT. ANN. § 10-055(A)(3) (Supp. Pamphlet 1975). Section 10-055(C) further requires publication of the articles three times within 60 days after the date of filing by the commission. See text & notes 58-67 *infra*. On February 10, 1976, a bill providing a number of corrective changes to the Act, none of which are viewed by the Bar Committee as substantive in nature, was introduced in the Arizona legislature. H. 2364, 32d Ariz. Legis., 2d Reg. Sess. (1976). These proposed amendments do not include any alteration in the publication requirements of the Act and continue to grant the commission discretion in filing proposed articles of incorporation.

4. ARIZ. REV. STAT. ANN. §§ 10-002 to -149 (Supp. Pamphlet 1975).

5. Ch. 69, § 13, [1975] Ariz. Sess. Laws 1st Reg. Sess. 320. The Act repeals most of the existing Arizona General Corporation Law, ARIZ. REV. STAT. ANN. §§ 10-101 to -383, -481 to -485 (1956), *as amended*, (Supp. Pamphlet 1975), except for the provisions relating to unclaimed shares and dividends, corporations sole, and nonprofit corporations. ARIZ. REV. STAT. ANN. §§ 10-401 to -458 (1956), *as amended*, (Supp. Pamphlet 1975).

6. Chapter LI, section 18 of *The Compiled Laws of the Territory of Arizona* (1871), provided the first general law under which business corporations could be organized in the Arizona Territory. Between the creation of the Territory in 1863 and November 6, 1866, the date of approval of chapter LI, business corporations were chartered by special act of the territorial legislature. *See, e.g.*, An Act to Incorporate the Arizona Central Road Co., [1864] Acts, Res. & Mems. of the Ariz. Terr. 1st Legis. Assembly 21; An Act to Incorporate the Hualapai Mining, Smelting, and Assaying Co., *id.* at 37; An Act to Incorporate the LaPaz & Prescott Railway Co., [1865] Acts, Res. & Mems. of the Ariz. Terr. 2d Legis. Assembly 45. The former Arizona General Corporation Law, ARIZ. REV. STAT. ANN. § 10-101 to -383, -481 to -485 (1956), *as amended*, (Supp. Pamphlet 1975), contains many provisions similar to those found in its statutory forerunners. *See, e.g.*, Ariz. Rev. Stat. ¶¶ 229-250 (1887); Ariz. Rev. Stat., Civil ¶¶ 761-783 (1901); Ariz. Rev. Stat., Civil ¶¶ 2093-2118 (1913); Ariz. Rev. Code §§ 576-594 (1928); Ariz. Code §§ 53-201 to -308 (1939). Many of these provisions have been retained in modified form in the new Arizona Business Corporation Act. *Compare, e.g.*, Ariz. Rev. Stat. ¶ 232 (1887), Ariz. Rev. Stat., Civil ¶ 764 (1901), Ariz. Rev. Stat., Civil ¶ 2096 (1913), Ariz. Rev. Code § 576 (1928), *and* Ariz. Code § 53-203 (1939) *with* ARIZ. REV. STAT. ANN. § 10-053 (Supp. Pamphlet 1975) (who may incorporate); Ariz. Rev. Stat. ¶ 239 (1887), Ariz. Rev. Stat., Civil ¶ 772 (1901), Ariz. Rev. Stat., Civil ¶ 2105 (1913), Ariz. Rev. Code § 592 (1928), *and* Ariz. Code § 53-306 (1939) *with* ARIZ. REV. STAT. ANN. § 10-083 (Supp. Pamphlet 1975) (voluntary dissolution).

7. *See, e.g.*, text & notes 246-55 *infra*.

8. MODEL BUS. CORP. ACT ANN. (2d ed. 1971) [hereinafter cited as MODEL ACT]. The Model Business Corporation Act [Model Act], prepared by the Committee on Corporate Laws of the Section of Corporation, Banking, and Business Law of the American Bar Association [ABA Committee on Corporate Laws], was chosen as a

former Arizona law and codifies many rules which existed only under common law.

This Article will note the most important new statutory changes and their effect on Arizona corporations. First, the new Act's applicability to existing Arizona corporations will be discussed. Comparative features between the new law and the old then will be analyzed, with emphasis on the new Act's different treatment of some matters previously covered under the old law. Subjects of corporate law which have for the first time been treated statutorily in the new Act also will be examined. The Article next will point out various matters of immediate concern to all existing corporations in Arizona. Finally, annotated model articles of incorporation, which reflect the new statutory provisions and may provide guidance in the formation of new corporations or the amendment of existing corporations' articles and bylaws, are provided in the Appendix.

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starting point, and later as a pattern, by the Arizona Bar Committee. While only a few of the 152 sections of the Model Act were enacted unchanged in the Arizona Act, many of the Arizona changes were minor. For the most part the section numbers of the Model Act have been carried over into the Arizona Act, except where changes were necessary to conform to the uniform statutory format of the Arizona Revised Statutes.

The Model Act, first published in 1950, originally was patterned after the Illinois Business Corporation Act of 1933. The Bar Committee used the 1969 version of the Model Act in drafting the new Arizona Act, and thus the changes made in 1973 by the ABA Committee on Corporate Laws in section 2(f) (definition of shareholder), section 43 (place and notice of directors and committee meetings), and section 106(g) (admission of foreign corporations) are not reflected in the Arizona Act. *Compare* MODEL ACT §§ 2(f), 43, *and* 106(g) *with* ARIZ. REV. STAT. ANN. § 10-002(16), -043, *and* -106(B)(7) (Supp. Pamphlet 1975). *See* Report of the Committee on Corporate Laws, *Changes in the Model Business Corporation Act*, 29 BUS. LAW. 947, 947-48 (1974). In 1974 changes were approved to sections 35 and 48 as well, providing a standard of care for directors and broadening directors' rights to rely on others and on materials prepared by others. *Compare* MODEL ACT §§ 35 *and* 48 *with* ARIZ. REV. STAT. ANN. §§ 10-035 *and* -048 (Supp. Pamphlet 1975). *See Report of the Committee on Corporate Laws: Changes in the Model Business Corporation Act*, 30 BUS. LAW. 501, 501-09 (1975) [hereinafter cited as *1975 Report*]. In September 1974, the ABA Committee on Corporate Laws also proposed changes to section 42 of the Model Act, concerning executive and other committees, as well as to sections 63, 65, 73, 74, 76, 77, and 80, and the addition of new section 72-A, all designed to establish a procedure whereby direct exchanges of shares in corporate combinations may be effected utilizing the same safeguards, notice requirements, and shareholder voting rights required for comparable mergers and similar transactions, and resulting in the same binding effect upon shareholders. *See Report of the Committee on Corporate Laws, Changes in the Model Business Corporation Law*, 30 BUS. LAW. 991 (1975). *See generally* Eisenberg, *Model Business Corporation Act and the Model Business Corporation Law Annotated*, 29 BUS. LAW. 1407 (1974). On November 26, 1975, the Bar Committee appointed a subcommittee to consider substantive changes in the Act for recommendation to the Bar Committee. The subcommittee presently anticipates considering the above revisions by the ABA Committee on Corporate Laws as well as other matters and intends to recommend appropriate amendments to the Act to the full Bar Committee in the future.

Several other states have adopted or are considering adoption of the Model Act. *See, e.g.*, Hodge & Perry, *Model Business Corporation Act: Does the Mississippi Version Lime the Bushes?*, 46 MISS. L.J. 371 (1975); Schaefer, *Status of the Adoption of the Model Business Corporation Act in Montana—A Commentary*, 36 MONT. L. REV. 29 (1975).

TABLE OF CONTENTS

I. APPLICATION OF THE ACT TO EXISTING ARIZONA CORPORATIONS

Complete revision by a legislature of a broad area of general law such as that controlling the activities of corporations raises the issue of whether the new legislation applies to entities created and operating under former law. The ability of a state to permit or require changes in corporate affairs is subject to two basic constitutional limitations. First, a corporate charter granted by a state to a corporation has been deemed

a binding contract between the former and the latter.[9] Under this theory unilateral alteration of that contract by the state's revision of its corporation laws would unconstitutionally impair its contractual obligation.[10] Secondly, a corporate charter also constitutes a contract between the corporation and its owners, whereby the corporate shareholders acquire vested rights through the articles of incorporation and the state's corporation laws.[11] The alteration of such rights would, in addition to impairing an existing contract, constitute an uncompensated taking of property unless the requirements of due process are satisfied.[12]

These traditional constitutional limitations on a state's power to revise statutes affecting corporations have been eroded, however. Reserved power provisions in state corporation laws[13] automatically become part of every corporate charter,[14] thereby permitting the state legitimately to change or repeal corporate laws without violating the Constitution's contract clause.[15] Arizona's constitution, for example,

9. Trustees of Dartmouth College v. Woodward, 17 U.S. (4 Wheat.) 518, 662 (1819).

10. *Id.*; *see* U.S. CONST. art. I, § 10.

11. Western Foundry Co. v. Wicker, 403 Ill. 260, 267, 85 N.E.2d 722, 726 (1949), *cited in* H. HENN, HANDBOOK OF THE LAW OF CORPORATIONS AND OTHER BUSINESS ENTERPRISES § 340, at 696 n.12 (2d ed. 1970).

12. *See* U.S. CONST. amend. XIV, § 1; Shields v. Ohio, 95 U.S. 319, 324-25 (1877); In the Matter of Mount Sinai Hosp., 250 N.Y. 103, 110-11, 164 N.E. 871, 874 (1928); *cf.* Coombes v. Getz, 285 U.S. 434, 441-42 (1932). Since no one has a vested interest in any rule of the common law, Munn v. Illinois, 94 U.S. 113, 134 (1877), the vested rights doctrine properly is applied only to statutory or constitutional provisions.

13. *E.g.*, ARIZ. CONST. art. 14, § 2: "Laws relating to corporations may be altered, amended, or repealed at any time, and all corporations doing business in this state may, as to such business, be regulated, limited, and restrained by law."

14. Lurie v. Arizona Fertilizer & Chemical Co., 101 Ariz. 482, 485, 421 P.2d 330, 333 (1966); Trico Elec. Cooperative, Inc. v. Ralston, 67 Ariz. 358, 366, 196 P.2d 470, 475 (1948). The charter of an Arizona corporation formed under general legislation consists of the provisions of the state constitution, the particular statutes under which the corporation is organized, all other general laws which are made applicable to corporations formed under such statute, and the corporation's articles of incorporation. Lurie v. Arizona Fertilizer & Chemical Co., *supra*; Trico Elec. Cooperative, Inc. v. Ralston, *supra*.

15. U.S. CONST. art. 1, §10. In Veix v. Sixth Ward Bldg. & Loan Ass'n, 310 U.S. 32, 38-39 (1940), the Supreme Court held that a state's police power exercised in protection of the public health, safety, and general welfare permits change or repeal of a corporate charter, even in the absence of an express reserved power clause in the contract between the corporation and the state. The Court likened the state's power to enact legislation affecting contract rights without violating the Constitution's contract clause to the power often reserved to amend charters. *Id.* at 40. The Court appeared to impute some form of acquiescence to a shareholder purchasing with knowledge, actual or constructive, of the nature of regulations on the corporation: "It was while statutory requirements were in effect that petitioner purchased his shares. When he purchased into an enterprise already regulated in the particular to which he now objects, he purchased subject to further legislation upon the same topic." *Id.* at 38. Under this approach, some courts have deemed shareholders to have consented to changes made by the state, thereby avoiding the sanction against the impairment of contractual obligations. See authority cited in H. HENN, *supra* note 11, § 340, at 696 n.16.

The power to impair preexisting contract rights through amendment of the corporation code, however, is not unlimited. In a pre-*Veix* case the Court had upheld a corporate creditor's right to enforce a suretyship obligation against the corporation's directors, even though the statute placing such obligation upon the directors had been repealed after action was commenced on the debt. Coombes v. Getz, 285 U.S. 434

expressly reserves the power to alter, amend, or repeal corporate laws.[16] The vested rights doctrine similarly has been undermined[17] and its application to most Arizona corporations effectively nullified by legislative enactments. Under Arizona's General Corporation Law, business corporations have been required to renew their charters at 25-year intervals if continued existence was desired.[18] A corporation's exercise of its renewal right has been, in effect, a renegotiation with the state of its charter, and the renewal thereby obtained was a new grant of the privilege of fictitious existence. As a result, the corporation and its shareholders thereafter were subject to the laws in existence at the time of the new grant, shareholder rights being defined by such law.[19] The new Act, while not retaining the renewal provision,[20] does grant to corporations the general and specific authority to amend articles of incorporation,[21] thus effectively abrogating the notion of shareholders' vested rights.[22]

The constitutional objections to applying the new Act to preexisting corporations, therefore, are substantially weakened; nevertheless, the Arizona legislature departed from the Model Act to provide for only limited application to existing corporations. While the Model Act recommends immediate application to both preexisting and subsequently created corporations,[23] Arizona has chosen to defer application of the new Act either temporarily or permanently to those corporations operating under prior law.[24] The provisions of the Arizona Act apply on its effective date to all existing corporations[25] organized under any general

(1932). This decision was interpreted by the *Veix* Court as resting on the fact that plaintiff, a third party to any contract among the corporation, the shareholders, and the state, could not be bound by any reserved amendment authority which might be implied into such a contract. 310 U.S. at 40.

16. ARIZ. CONST. art. 14, § 2. See note 13 *supra.*

17. The application of the vested rights doctrine clearly is on the decline, with at least one commentator concluding some time ago that it had disappeared entirely. Gibson, *How Fixed are Class Shareholder Rights?*, 23 LAW & CONTEMP. PROB. 283, 291 (1958).

18. ARIZ. REV. STAT. ANN. § 10-151(A) (1956).

19. Hanks v. Borelli, 2 Ariz. App. 589, 592, 411 P.2d 27, 30 (1966).

20. The new Act specificaliy provides that a corporation has perpetual succession unless a limited duration is stated in the articles of incorporation. ARIZ. REV. STAT. ANN. § 10-004(A)(1) (Supp. Pamphlet 1975).

21. *Id.* § 10-058.

22. The comment to section 58 of the Model Act, upon which section 10-058 of the new Arizona Act was based, states: "One of the major purposes . . . was to sweep aside the complexities of judicial decisions on vested rights . . . ." MODEL ACT § 58, Comment ¶ 2, at 225. See text & notes 11-12 *supra.*

23. MODEL ACT § 147, Comment ¶ 2, at 911-12. The ABA Committee on Corporate Laws felt that uniformity of application outweighed any momentary inconvenience to existing corporations. *Id.*

24. *See* ARIZ. REV. STAT. ANN. § 10-147 (Supp. Pamphlet 1975).

25. *Id.* These existing corporations can be classified as: (1) those corporations organized under the Arizona General Corporation Law, ARIZ. REV. STAT. ANN. § 10-121 to -128 (1956), or its predecessors; (2) those corporations organized under some other general act of the State of Arizona; (3) those corporations organized under the general corporate laws of the Territory of Arizona; and (4) those corporations organized under

act of the State of Arizona for any lawful purpose not specifically prohibited to corporations under Arizona law.[26] However, all previously valid provisions of their current articles of incorporation remain in full force and effect until the end of the corporation's term of existence, until the articles of incorporation are amended or restated, or until the corporation merges, consolidates, or reorganizes.[27] At such time all of the provisions of the resultant articles of incorporation must comply with the Act.[28] Consequently Arizona corporations organized under the

special acts of the territorial legislature. See discussion note 6 *supra*. While section 10-147 of the new Act does not distinguish between the first two classifications above, a distinction is made between corporations organized under state and territorial laws.

26. The term "corporation" is defined in ARIZ. REV. STAT. ANN. § 10-002(8) (Supp. Pamphlet 1975) as "a corporation for profit subject to the provisions of this chapter, except a foreign corporation." The term "general act" includes the acts under which all existing Arizona business corporations were organized since 1866. *See* ARIZ. CONST. art. 14, § 2. The phrase "purpose or purposes for which a corporation might be organized under this chapter" includes "any lawful purpose or purposes not specifically prohibited to corporations under laws of this state." ARIZ. REV. STAT. ANN. § 10-003 (Supp. Pamphlet 1975). Thus the Act is applicable to all domestic private corporations for profit organized under Arizona law since 1866.

The Act also applies in significant respects to other types of organizations. *See* ARIZ. REV. STAT. ANN. § 6-463(A) (Supp. 1975-76) (savings and loan associations); ARIZ. REV. STAT. ANN. § 6-503 (1956) (credit unions); ARIZ. REV. STAT. ANN. §§ 9-1153, -1187 (Supp. Pamphlet 1975) (industrial development authorities); *id.* §§ 9-1223, -1228 (pollution control corporations); *id.* §§ 10-002(22), -023, -028(D) (water users' associations); *id.* § 10-123 (foreign corporations organized for profit); ARIZ. REV. STAT. ANN. §§ 10-452(A), -453(6) (1956) (nonprofit corporations); ARIZ. REV. STAT. ANN. § 10-509 (Supp. Pamphlet 1975) (business trusts); ARIZ. REV. STAT. ANN. § 10-702 (1956) (cooperative marketing associations); *id.* § 10-904 (professional corporations); *id.* § 10-953 (business development corporations); *id.* § 20-704 (insurance companies). The Act does not apply to foreign nonprofit corporations, *see* ARIZ. REV. STAT. ANN. § 10-002(11) (Supp. Pamphlet 1975), or to those corporations defined as "public corporations" in ARIZ. REV. STAT. ANN. § 10-102(A) (1956). *See* ARIZ. REV. STAT. ANN. § 10-002(8) (Supp. Pamphlet 1975).

Separate close corporation legislation has been introduced into the Arizona legislature. See S. 1299, 32d Ariz. Legis., 2d Sess. (1976). It presently is contemplated by the Bar Committee that nonprofit corporation legislation also will be introduced in the near future. The Act, however, does have some features not contained in the present statutes which permit additional flexibility for close corporations. These features may be found in ARIZ. REV. STAT. ANN. §§ 10-004(A)(12), -027 (Supp. Pamphlet 1975) (bylaws); *id.* § 10-015 (authorized shares); *id.* § 10-016 (shares in series); *id.* § 10-032 (quorum of shareholders); *id.* § 10-034 (shareholders' agreements); *id.* § 10-035 (allocation of authority among directors and shareholders); *id.* § 10-036 (number and election of directors); *id.* § 10-037 (classification of directors); *id.* § 10-040 (quorum of directors); *id.* § 10-050 (officers); *id.* § 10-053 (incorporators); *id.* § 10-054 (articles of incorporation); *id.* §§ 10-060, -073, -079 (class voting on amendments, mergers and consolidations, and sales of assets); *id.* § 10-143 (greater shareholder voting requirements); *id.* §§ 10-044, -144, -145 (actions without meetings and waiver of notice requirements). The special comment on close corporations to section 35 of the Model Act contains a brief summary of the application of these provisions to close corporations. MODEL ACT § 35, Comment ¶ 2, at 756.

27. ARIZ. REV. STAT. ANN. § 10-147(A) (Supp. Pamphlet 1975). Under the Act, corporations desiring to amend and restate their articles of incorporation first must amend and then restate, since ARIZ. REV. STAT. ANN. §§ 10-059, -064 (Supp. Pamphlet 1975) do not provide for "amended and restated articles of incorporation" in one document as presently may occur in Arizona. *See* ARIZ. REV. STAT. ANN. § 10-104(A)(4) (1956).

28. ARIZ. REV. STAT. ANN. § 10-147(A)(2) (Supp. Pamphlet 1975). Although the Act does not contain an analogue to ARIZ. REV. STAT. ANN. § 10-151(A) (1956) (providing for renewal by appropriate resolution of the corporation's shareholders prior to the expiration of its term of existence), section 10-147(B) provides that such existing corporations may be renewed by amendment of their articles of incorporation as

Arizona General Corporation Law or one of its predecessors may continue to exist only partially affected by the new Act for a period of as long as 25 years less 1 day after the effective date of the Act.[29]

Corporations originally organized under territorial law after March 8, 1887, may continue in their present form until their terms of existence expire,[30] until they amend or restate their articles, or, presumably, until they merge, consolidate, or reorganize.[31] Even after amending their articles, they may retain any previously valid provisions, even those in conflict with the Act.[32] Any territorial corporations still in existence which were organized under the 1866 act with perpetual duration[33] or under earlier special acts[34] apparently may continue to exist indefinitely without the burdens or benefits of the Act. The Act could not be forced upon such corporations without raising constitutional questions since the reservation of power to amend corporate charters found in the Arizona constitution has no retroactive application to corporations formed prior to statehood.[35]

Due to this continuing uncertainty as to the law applicable to existing Arizona corporations, all persons dealing with such corporations, territorial or otherwise, and all shareholders, subscribers, affiliates,

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provided in sections 10-058 through -063. Section 10-147(B) also contains a reference permitting renewal within 5 years of the expiration of its present period of existence "as provided under § 10-106." The reference presumably was intended to be to section 10-105, which provides for amendment of the articles of incorporation of a corporation dissolved by the expiration of its period of duration within 5 years after the expiration of its terms of existence.

29. The Act is made applicable expressly to "all existing corporations organized under any general law of this state" except to the extent that existing valid articles provide for other effects in some circumstances. ARIZ. REV. STAT. ANN. § 10-147(A) (Supp. Pamphlet 1975). All such existing Arizona corporations will become subject on July 1, 1976, to all of the Act's provisions except articles 2 and 9.

30. ARIZ. REV. STAT. ANN. § 10-147(A)(1) (Supp. Pamphlet 1975). Such territorial corporations originally were subject to the terms of the statutes under which they were organized, which granted only limited existence. *See* Ariz. Rev. Stat. ¶ 238 (1887); Ariz. Rev. Stat., Civil ¶ 711 (1901). Consequently, territorial corporations formed under either the 1887 or 1901 Act, as well as those formed for a limited duration under the 1866 Act, *see* Ariz. Comp. Laws ch. LI, §§ 4, 17 (1871), either no longer exist due to the expiration of their limited terms of existence or have renewed their existence under present or former Arizona corporate statutes. In the latter case, such renewals constitute new grants of corporate existence, subjecting the renewed corporation to the corporate laws in existence at the time of renewal. See text accompanying notes 18-19 *supra*. As a result, these corporations presently are subject to the 25-year renewal provisions of ARIZ. REV. STAT. ANN. § 10-151 (1956).

31. *Compare* ARIZ. REV. STAT. ANN. § 10-147(C) (Supp. Pamphlet 1975) *with id.* § 10-147(A).

32. *Id.* § 10-147(C).

33. *See* Ariz. Comp. Laws ch. LI, §§ 4, 17 (1871).

34. *See, e.g.*, An Act to Incorporate the Mowry Silver Mine Road Co., [1865] Acts, Res. & Mems. of the Ariz. Terr. 2d Legis. Assembly 42; An Act to Incorporate the La-Paz and Prescott Railway Co., *id.* at 45.

35. *See* ARIZ. CONST. art. 14, § 2; Citrus Growers' Dev. Ass'n v. Salt River Valley Water Users' Ass'n, 34 Ariz. 105, 114, 268 P. 773, 776 (1928). The Supreme Court's lenient attitude toward statutory changes affecting corporate activities would seem to lessen the possibility of constitutional problems. See discussion note 15 *supra*.

directors, officers, employees, agents, and creditors of existing Arizona corporations would do well to inform themselves of any provisions in such corporations' articles of incorporation in conflict with the Act.[36] Arizona practitioners will best serve their corporate clients by examining their corporate structure and needs and counseling on the advisability of retaining the status quo where possible or of adopting the Act's provisions.

II. COMPARATIVE FEATURES

Most of the matters covered by the present Arizona General Corporation Law also are encompassed by the Act.[37] However, a number of provisions have been altered considerably by the Act, and the practicing attorney should be in a position to advise both new and existing corporations which may wish to take advantage of these changes.

A. *Corporate Indebtedness*

Under the Act Arizona business corporations no longer will be subject to statutory limitations on their indebtedness.[38] The Act authorizes corporations to "borrow money at such rates of interest as the corporation may determine . . . ."[39] The Act does indirectly inhibit certain corporate borrowing, however. While the former statute authorized an interest rate of up to 18 percent per annum on certain corporate indebtedness and prohibited the claim or defense of usury by a corporation borrowing under such terms,[40] this provision has no counterpart in the Act. Therefore, the new provision on indebtedness presumably must be read in conjunction with Arizona's general usury statutes.[41]

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36. *See* ARIZ. REV. STAT. ANN. §§ 10-147(A), (C) (Supp. Pamphlet 1975).

37. Several matters covered by the old law have been deleted in the new Act. These subjects, however, were of significance only to certain special interest groups. *See* ARIZ. REV. STAT. ANN. § 10-125 (1956) (exemption of veterans' associations from publication requirements and fees); *id.* § 10-174 (construction or operation of railroads or canals by mining or manufacturing corporations); *id.* § 10-197 (defense of status as foreign corporation barred in actions based on certain acts prohibited to officers, directors, and agents).

38. The former law limited corporate indebtedness to two-thirds of authorized capital stock unless approval was obtained by a three-fourths vote of the shareholders. ARIZ. REV. STAT. ANN. § 10-173(A) (1956).

39. ARIZ. REV. STAT. ANN. § 10-004(A)(8) (Supp. Pamphlet 1975).

40. Former ARIZ. REV. STAT. ANN. § 10-177 (Supp. Pamphlet 1975). This section has been repealed by the new Act.

41. If the courts interpret section 10-004(A)(8) as independent of the usury laws or as intended by the legislature to replace former section 10-177, there will be no maximum rate of interest applicable to corporate indebtedness. If, however, the courts determine that section 10-004(A)(8) must be read in conjunction with the usury statute, ARIZ. REV. STAT. ANN. § 44-1201 (Supp. 1975-76), the maximum allowable interest rate will be 12 percent per annum on any indebtedness pursuant to a written agreement with an original principal balance of $25,000; 10 percent per annum under a written agreement if the original principal balance is $25,000 or less; and 6 percent if no written

B. *Procedures and Forms*

The Act establishes new procedures, and in some cases new forms, for incorporation;[42] amendment to and restatement of articles of incorporation;[43] merger and consolidation;[44] voluntary dissolution and liquidation;[45] involuntary dissolution;[46] admission, regulation, and withdrawal of foreign corporations;[47] annual reports;[48] financial reports to shareholders;[49] and interrogatories by the Arizona Corporation Commission.[50] Generally, the new procedures simplify the filing process and eliminate the requirement of recordation with county recorders.[51] The Arizona Corporation Commission is granted discretionary authority in the Act to accept or reject the filings.[52] The statutory guideline with

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agreement exists. Since only the largest, most established corporations generally can qualify for low interest rates, newer and smaller businesses in Arizona might be unable to borrow for expansion or for working capital purposes at rates permitted by the general usury limitations. In the absence of a corporate exemption from the general limitations, lendable funds otherwise available in Arizona might gravitate to the substantial majority of states which allow corporate borrowers to pay interest rates in excess of 12 percent. A bill reenacting former section 10-177 as section 10-150 of the new Act has passed the Arizona house unanimously at the time this article is being written. H. 2184, 32d Ariz. Legis., 2d Reg. Sess. (1976). The bill as passed by the House contains an emergency clause.

42. ARIZ. REV. STAT. ANN. §§ 10-053 to -057 (Supp. Pamphlet 1975); *see id.* §§ 10-128 to -129 (relating to certificates of disclosure and filing fees); *id.* § 10-142 (relating to forms).

43. *Id.* §§ 10-058 to -065.

44. *Id.* §§ 10-071 to -081.

45. *Id.* §§ 10-082 to -093.

46. *Id.* §§ 10-094 to -105.

47. *Id.* §§ 10-106 to -124; *see* statutory sections cited note 42 *supra.*

48. ARIZ. REV. STAT. ANN. § 10-125 (Supp. Pamphlet 1975); *see* statutory sections cited note 42 *supra.* The provision of former ARIZ. REV. STAT. ANN. § 10-104(B)(1) (Supp. Pamphlet 1975) limiting the penalty for failure to pay the registration fee in conjunction with the filing of annual reports to an amount equal to the delinquent fee is eliminated in the Act and the penalty will continue to accrue at a rate of 20 percent of the delinquent fee per month, or fraction thereof, until payment is made or the corporation's charter is revoked. ARIZ. REV. STAT. ANN. §§ 10-125(E), -094(1) (Supp. Pamphlet 1975).

49. ARIZ. REV. STAT. ANN. § 10-127 (Supp. Pamphlet 1975).

50. *Id.* §§ 10-137 to -138.

51. *Compare* ARIZ. REV. STAT. ANN. § 10-123 (1956) *with* ARIZ. REV. STAT. ANN. § 10-055 (Supp. Pamphlet 1975) (articles of incorporation); ARIZ. REV. STAT. ANN. § 10-322 (1956) *with* ARIZ. REV. STAT. ANN. § 10-062 (Supp. Pamphlet 1975) (articles of amendment). *See also* ARIZ. REV. STAT. ANN. § 10-064 (Supp. Pamphlet 1975) (restated articles of incorporation); *id.* §§ 10-067 to -068 (statement of cancellation of redeemed and other reacquired shares); *id.* § 10-069 (statement of reduction of stated capital); *id.* § 10-074 (articles of merger or consolidation); *id.* § 10-082 (articles of dissolution); *id.* § 10-085 (statement of intent to dissolve); *id.* § 10-090 (statement of revocation of voluntary dissolution proceedings); *id.* § 10-093 (articles of dissolution); *id.* § 10-111 (application of foreign corporation for authority to transact business); *id.* § 10-120 (application for withdrawal).

The filing fee section, *id.* § 10-129, does not appear to contemplate the issuance of certificates of good standing nor to provide for certifying copies of documents on file with the Arizona Corporation Commission as did the former statutes. ARIZ. REV. STAT. ANN. §§ 10-104(A)(14), (16) (1956). The effect of this omission is uncertain. Pending House Bill 2364 would provide for the issuance of certificates of good standing but does not provide for certifying copies of documents on file with the commission. H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 61 (1976).

52. The Arizona Corporation Commission is granted only 5 working days from the date of delivery to it of the proposed articles of incorporation to determine that they

regard to the commission's exercise of this discretion is limited to a determination of whether the documents filed conform to the requirements of the Act and to any other applicable law.[53] The Act also contains an express grant to the commission of the power and authority "reasonably necessary" in the administration of the Act.[54]

Under the Act, de jure incorporation is complete upon the filing of articles of incorporation, except as against certain state challenges to the corporate existence.[55] Any steps short of filing apparently will not constitute compliance.[56] This strict rule effectively abolishes the de facto corporation doctrine under present Arizona law.[57]

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appear to conform in all respects to the requirements of the Act and other applicable law. ARIZ. REV. STAT. ANN. § 10-055(B) (Supp. Pamphlet 1975). On the other hand, no express time for such determination is set forth in the Act with regard to amended or restated articles, *id.* §§ 10-062(B), -064(C), -065(C)(2), -067(C), -068(C), -069(C), articles of merger or consolidation, *id.* §§ 10-074(B), -075(D), articles of dissolution, *id.* § 10-093(A), or applications by foreign corporations for authority to transact business. *Id.* § 10-111(A).

Pending House Bill 2364 would delete the 5-day limitation upon the commission's determination that the articles are proper. H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 20 (1976). Additionally, the commission's discretion is stated in the proposed amendment to be limited to a determination that compliance has been made with the requirements of section 10-008 (corporate name), section 10-054 (contents of articles), section 10-128 (certificate of disclosure), and that the articles appear in all other respects to conform to the requirements of the Act. *Id.* The amorphous additional discretion to determine apparent conformance to the "requirements of law" is eliminated both with regard to articles of incorporation (section 10-055(A)(3)), *id.*, and to applications of foreign corporations for authority to transact business in the state (section 10-111(A)). *Id.* § 48. Interestingly, the commission's discretion remains unchanged with respect to series designations (section 10-016(G)), articles of amendment (section 10-062(A)(2)), restated articles of incorporation (section 10-064(C)), amendments of articles of incorporation in reorganization proceedings (section 10-065(C)(2)), statements of cancellation (sections 10-067(C) and 10-068(C)), statements of reduction in capital (section 10-069(C)), articles of merger or consolidation (section 10-074(B)), articles of merger of subsidiary corporations (section 10-075(D)), and articles of dissolution (section 10-093(A)).

53. ARIZ. REV. STAT. ANN. § 10-055 (Supp. Pamphlet 1975).

54. *Id.* § 10-139. An additional requirement of the Act is that all mandatory reports be made on the originals, not duplicates, of forms prescribed and furnished by the commission. *Id.* § 10-142(A).

55. *Id.* § 10-056. In contrast, section 56 of the Model Act deems de jure incorporation complete upon issuance of the certificate of incorporation, as does Arizona's former law. *See* ARIZ. REV. STAT. ANN. § 10-126(A) (1956) (providing for commencement of business upon issuance of a certificate of incorporation). The contrast is a result of the decision to reject the Model Act's certificate approach; the issuance of certificates of incorporation for domestic corporations and certificates of authority for foreign corporations was viewed as serving no useful corporate purpose, yet imposing a significant administrative burden on the commission.

56. *See* MODEL ACT § 56, Comment ¶ 2, at 205.

57. In the past Arizona has recognized the existence of a de facto corporation when there has been a bona fide but defective attempt to organize. *See* Rice v. Sanger Bros., 27 Ariz. 15, 20, 229 P. 397, 399 (1924); Sawyer v. Pabst Brewing Co., 22 Ariz. 384, 390-91, 198 P. 118, 121-22 (1921); ARIZ. REV. STAT. ANN. § 10-172 (1956). However, in accordance with the Model Act's express nonrecognition of de facto corporations, MODEL ACT § 56, Comment ¶ 2, at 205, the new Arizona Act's express provision defining the commencement of corporate existence, ARIZ. REV. STAT. ANN. § 10-056 (Supp. Pamphlet 1975), and its provision for joint and several liability of "[a]ll persons who assume to act as a corporation without authority so to do . . . ," *id.* § 10-146, probably eradicate the de facto doctrine in Arizona. *See* H. HENN, *supra* note 11, § 142, at 245.

The publication requirements under the new Act, which decrease the number of required publications from six to three,[58] are sometimes inconsistent, confusing, and of uncertain value. Initially, the Act requires publication of the articles of incorporation following filing.[59] Since the Act defines articles of incorporation to mean not only the original articles, but also restated articles, articles of merger or consolidation, and amendments thereto,[60] the above requirement could be interpreted as applying to all of these documents. Indeed, the Act goes on to state the same publication requirement specifically in regard to articles of amendment[61] and articles of merger or consolidation.[62] No publication requirement is set forth in regard to restated articles, however.[63] Nor is the publication mandated for various corporate changes which are statutorily denoted as amendments[64] or for articles of amendment pursuant to reorganization.[65] It is difficult for the practitioner to know whether the omission of any specific publication requirement as to these transactions means that publication is not in fact required, or whether the omission merely leaves these documents to be encompassed within the broad mandate as to articles of incorporation and amendments thereto.[66] Since the penalty for failure to make a required

58. *Compare* ARIZ. REV. STAT. ANN. §§ 10-124, -126(B), *and* -322 (1956) *with* ARIZ. REV. STAT. ANN. §§ 10-055(C) *and* -062(C) (Supp. Pamphlet 1975); ARIZ. REV. STAT. ANN. § 10-343 (1956) *with* ARIZ. REV. STAT. ANN. § 10-074(C) (Supp. Pamphlet 1975). In general, where publication is required the corporation must, within 60 days, publish a copy of the relevant document in three consecutive issues of a newspaper of general circulation in the county of the corporation's known place of business. *See id.* § 10-055(C) (articles of incorporation); *id.* § 10-062(C) (articles of amendment); *id.* § 10-074(C) (articles of merger or consolidation); *id.* § 10-111(B) (foreign corporation's application for authority to transact business). With regard to certain types of documents, however, publication must be accomplished within 30 days. *See id.* § 10-087(A)(2) (statement of intent to dissolve); *id.* § 10-116(C) (restatement of foreign corporation's application for authority to transact business).

59. ARIZ. REV. STAT. ANN. § 10-055(C) (Supp. Pamphlet 1975).

60. *Id.* § 10-002(3). Nevertheless, in subsequent sections referring back to section 10-055, it is regarded as applying only to the original articles. *See, e.g., id.* §§ 10-062(B), -064(C), -065(C)(2).

61. *Id.* § 10-062(C).

62. *Id.* § 10-074(C). Publication is not required, however, where the merger involves parent and subsidiary. *Id.* § 10-075(D).

63. *See id.* § 10-064(C).

64. *See id.* §§ 10-067(C), -068(C), -069(C) (cancellation of shares or other reduction in stated capital); *id.* § 10-016(G) (resolution designating series and fixing relative rights and preferences).

65. *See id.* § 10-065(D).

66. The language of the filing requirements as to each of the documents affected by the ambiguity includes generally the following: "The commission shall, after determining that [e.g., the restated articles] appear in all respects to conform to the requirements of this chapter and to law, file [e.g., the restated articles] in the manner provided for filing original articles in § 10-055." *E.g.*, ARIZ. REV. STAT. ANN. §§ 10-016(G), -064(C), -065(C)(2) (Supp. Pamphlet 1975). Since section 10-055(C) requires publication of the articles of incorporation, this language conceivably could be interpreted as encompassing that requirement. This line of reasoning, however, is weakened by the fact that the sections on filing of amendments and articles of merger or consolidation contain the same language, but go on specifically to require publication. *See id.* §§ 10-062(B)-(C), -074(B)-(C).

Insofar as the purpose of publication is to establish thereby, together with central filing, a public record of the formation or dissolution of the corporation, its basic charter

publication is revocation of the filing of the articles of incorporation,[67] doubts probably should be resolved in favor of publication until legislative or judicial clarification is forthcoming.

The Model Act does not command publication, requiring only delivery to the secretary of state of duplicate originals of the document.[68] In fact, only five states in addition to Arizona retain the requirement,[69] and it is of doubtful usefulness since a complete public record of basic corporate documents currently is maintained by the commission.

C. *Purposes and Powers*

Under the Act, corporations may be organized for any lawful purpose not specifically prohibited to corporations under Arizona law.[70] Although the purpose or purposes for which a corporation is organized must be set forth in its articles of incorporation,[71] it "may be stated to be, or to include, the transaction of any or all lawful business for which corporations may be incorporated"[72] under the Act. Despite the Act's

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and alterations thereof, *see* MODEL ACT § 55, Comment ¶ 2, at 198, seemingly all important changes in the corporate structure, operational procedures, or financial base should be published. The Arizona statute, if interpreted to exempt from publication those transactions explicitly requiring filing but not publication, renders meaningless the rationale for the requirement, as the media record of the corporation's basic documents will be potentially incomplete and unreliable. The paradoxical effect of the new Act's publication requirements is illustrated by the provisions governing voluntary dissolution. The statement of voluntarily intent to dissolve a corporation must be published. ARIZ. REV. STAT. ANN. § 10-087(A)(2) (Supp. Pamphlet 1975). After such publication a decision may be made to revoke the dissolution, or the dissolution may be followed through to completion. *See id.* §§ 10-088 to -089, -092. In either case a filing must be made with the commission, *id.* §§ 10-090, -093; in neither case, however, must a subsequent publication be made. *See id.*

67. *See* ARIZ. REV. STAT. ANN. §§ 10-056, -095(A) (Supp. Pamphlet 1975). Although reinstatement is possible within 6 months of revocation once the required publication is made, *id.* § 10-095(D), the period of revocation would result in irreparable injury to most operative corporations. Interestingly, the state's revocation remedy is not available until 1 year after the affidavit of publication is due, *id.* § 10-095(A), thus seemingly rendering the specific statutory deadlines meaningless except as a point from which to measure for purposes of invoking the state's remedy. Although it might seem that a court could view any document not published as being inoperative, such a remedy would appear to be foreclosed by the statutes making such documents effective upon filing, apparently on the theory that the filing constitutes adequate constructive notice. *See, e.g., id.* §§ 10-056, -063(A), -064(D). As a result, the revocation remedy may be the only penalty for failure to publish. For additional discussion of the state's revocation authority, see text & notes 134-36 *infra.*

Pending House Bill 2364 would eliminate the 1-year limitation on the state's revocation remedy and make such remedy available if the required publication is not made and the affidavit of publication filed "within the time prescribed by this chapter." H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 43 (1976).

68. MODEL ACT § 55, Comment ¶ 2, at 198.

69. GA. CODE ANN. § 22-803 (1970); IOWA CODE ANN. §§ 496A.50, .52-.53 (1962); MINN. STAT. ANN. §§ 301.06-.07 (1969); MISS. CODE ANN. § 5309-123 (Supp. 1972); PA. STAT. ANN. tit. 15, §§ 1205-1206 (1967). Only two states besides Arizona require publication of amendments. GA. CODE ANN. § 22-905 (1970); PA. STAT. ANN. tit. 15, § 1807 (1967); *see* MODEL ACT § 62, Comment ¶ 3.03, at 282.

70. ARIZ. REV. STAT. ANN. § 10-003 (Supp. Pamphlet 1975).

71. *Id.* § 10-054(A)(3).

72. *Id.* Several limitations should be kept in mind in deciding whether an all inclusive statement of purposes should be used. First, the corporate name may not

acceptance of a very broad purpose clause, the articles of incorporation somewhat anomalously also must contain a brief statement of the character of business which the corporation initially intends to conduct in Arizona.[73]

Corporate purposes are effectuated by the corporation's exercise of its lawful powers. The Arizona constitution permits corporations to have only those powers expressly granted by law or expressly or impliedly granted in their articles of incorporation.[74] This constitutional provision has been strictly interpreted[75] because "unlike a natural person, [the corporation] may not do all things not expressly or impliedly prohibited, but must draw from its charter the power to act in any given respect, and can do only that which is expressly or impliedly authorized therein."[76] The statutory grant of corporate powers in Arizona's General Corporation Law is somewhat limited,[77] and consequently corporations were severely restricted under the former law in their authorized activities unless their articles were drafted as broadly as possible.

The new Act expands the category of express corporate powers, thereby obviating the necessity of a lengthy enumeration of desired powers in the articles of incorporation.[78] In addition to those specific powers granted by the new law, the statute permits a corporation to

include any word or phrase indicating or implying that "it is organized for any purpose other than any *specific* purpose contained in its articles of incorporation." *Id.* § 10-008(A)(2) (emphasis added). See Annot. 1 *infra*. Second, greater specificity may be desirable in the creation of subsidiaries and affiliates, to avoid conflicts of interest or the undesired application of the corporate opportunity doctrine. A limitation may also be desirable in situations in which a corporation in a regulated industry, such as a bank holding company, is prevented by other laws or regulations from entering into certain kinds of businesses or in situations in which the incorporators have agreed that the corporation will limit its activities. Finally, an all inclusive statement of powers may not be viewed favorably by financial institutions and could create problems in qualifying the corporation to transact business in other jurisdictions. See Annot. 4 *infra*.

73. ARIZ. REV. STAT. ANN. § 10-054(A)(4) (Supp. Pamphlet 1975). This brief statement, not required by the Model Act, *see* MODEL ACT § 54, does not limit the character of the business which ultimately may be conducted by the corporation. ARIZ. REV. STAT. ANN. § 10-054(A)(4) (Supp. Pamphlet 1975). This requirement's purpose presumably is only to identify the type of corporation being formed in those instances where a corporation has a general, nonspecific corporate name and has articles granting only general powers. The provision remedies the inability to determine the corporation's business from public record, and seems intended solely to provide knowledge to the public and not to affect the specified or inherent powers of the corporation. See Model Article 3 & Annot. 3 *infra*.

74. Article 14, section 4 of the Arizona constitution provides that "no corporation shall engage in any business other than that expressly authorized in its charter or by the law under which it may have been or may hereafter be organized." *See* Head & Amory v. Providence Ins. Co., 6 U.S. (2 Cranch) 459, 464 (1804); Lurie v. Arizona Fertilizer & Chemical Co., 101 Ariz. 482, 485, 421 P.2d 330, 333 (1966); Trico Elec. Cooperative, Inc. v. Ralston, 67 Ariz. 358, 366-67, 196 P.2d 470, 475 (1948).

75. Trico Elec. Cooperative, Inc. v. Ralston, 67 Ariz. 358, 366-67, 196 P.2d 470, 475 (1948).

76. *Id.* at 366, 196 P.2d at 475.

77. ARIZ. REV. STAT. ANN. § 10-152 (1956).

78. ARIZ. REV. STAT. ANN. §§ 10-004, -054(B) (Supp. Pamphlet 1975). A corporation wishing to do so, however, may deny, limit, or reduce the statutory powers contained in the Act by appropriate provision in its articles of incorporation. *Id.* § 10-004(B).

"[h]ave and exercise all powers necessary or convenient to effect its purposes."[79] While some of the powers delineated in the new Act are also found in the former Arizona General Corporation Law,[80] others have not been codified previously.[81]

Several specific statutory grants of power are especially important. The power of the corporation to enjoy perpetual duration[82] is a significant change from the former law which, while granting the right to perpetual succession,[83] limited the charter grants to 25 years.[84] The power to provide for the transferability of shareholders' interests and the power to exempt the private property of shareholders from liability for corporate debts, which are granted in the "general powers" provision of Arizona General Corporation Law,[85] have been retained in separate provisions of the new Act.[86] The provision granting shareholders the limited liability[87] which is normally the primary objective of incorporation[88] permits the articles of incorporation to provide otherwise.[89] This is the obverse of former law, which required that the articles of incorporation state whether private property of the shareholders was to be exempt from corporate debts.[90] Unless the articles so stated, the shareholders were liable for the debts of the corporation in the proportion their stock bore to the whole capital stock.[91]

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79. ARIZ. REV. STAT. ANN. § 10-004(A)(16) (Supp. Pamphlet 1975). See also Annot. 2 *infra.*

80. *Compare* ARIZ. REV. STAT. ANN. § 10-004(A)(2) (Supp. Pamphlet 1975) (sue and be sued by the corporate name); *id.* § 10-004(A)(3) (common seal); *id.* § 10-004(A)(4) (deal in property), *and id.* § 10-004(A)(12) (establish bylaws and make rules) *with* ARIZ. REV. STAT. ANN. §§ 10-152(2), -152(3), -152(6), *and* -152(7) (1956).

81. ARIZ. REV. STAT. ANN. § 10-004(A)(5) (Supp. Pamphlet 1975) (sell, convey, mortgage, pledge, lease, exchange, transfer, option, or otherwise dispose of its property and assets); *id.* § 10-004(A)(6) (lend money and use its credit to assist its employees); *id.* § 10-004(A)(7) (use and deal in securities); *id.* § 10-004(A)(9) (lend its money and hold real property as security); *id.* § 10-004(A)(10) (exercise its powers within or without the state); *id.* § 10-004(A)(11) (elect or appoint officers and agents, define their duties, and fix their compensation); *id.* § 10-004(A)(13) (make charitable, public scientific, or educational donations); *id.* § 10-004(A)(14) (establish incentive plans); *id.* § 10-004(A)(15) (promote or participate in other business associations). For a criticism of the power to lend money and use corporate credit to assist employees, and of the power to make donations for public, charitable, scientific, or educational purposes, see Note, *Corporations—A Survey of the Pending West Virginia Corporation Act,* 77 W. VA. L. REV. 50, 53 (1974).

82. ARIZ. REV. STAT. ANN. § 10-004(A)(1) (Supp. Pamphlet 1975). See Annot. 37 *infra.*

83. ARIZ. REV. STAT. ANN. § 10-152(1) (1956).

84. *Id.* § 10-151(A).

85. *Id.* §§ 10-152(4)-(5).

86. ARIZ. REV. STAT. ANN. §§ 10-015, -025 (Supp. Pamphlet 1975).

87. *Id.* § 10-025.

88. *See* H. HENN, *supra* note 11, § 202, at 403.

89. ARIZ. REV. STAT. ANN. § 10-025(A) (Supp. Pamphlet 1975). In this respect, Arizona's Act differs from the Model Act, where "[t]he limitation of liability to the subscription price of the shares is absolute . . . ." MODEL ACT § 25, Comment ¶ 2, at 509.

90. Former ARIZ. REV. STAT. ANN. § 10-122(9) (Supp. Pamphlet 1975).

91. *Id.*

Thus, the Act's provisions regarding corporate purposes and powers afford greater flexibility to Arizona corporations in their initial planning and organizational stages as well as in their subsequent operations.[92] The "all purpose" provision, the provision for perpetual duration, and the expanded enumeration of general powers which need not be incorporated by reference in the articles of incorporation are features of the Act which probably will have this effect. In addition to these changes, several other perhaps less striking but nonetheless consequential subjects covered by existing statute receive new treatment under the Act.

D. *New Treatment of Existing Statutory Subjects*

(1) *Corporate Name.* Under both the former Arizona General Corporation Law and the Act, domestic groups seeking to incorporate and foreign corporations seeking authority to transact business in Arizona may not choose a name already reserved or which is the same as, or deceptively similar to, the name of an existing domestic corporation or foreign corporation authorized to transact business in Arizona unless written consent to the use of the name is obtained and filed with the Arizona Corporation Commission.[93] Additionally, under the Act, the name chosen[94] cannot be the same as, or deceptively similar to, any trade name registered with the secretary of state,[95] unless written con-

92. These provisions of the Act also are designed to correct the widespread confusion concerning the function of the purposes and powers clauses in articles of incorporation. *See* Trico Elec. Cooperative, Inc. v. Ralston, 67 Ariz. 358, 366, 196 P.2d 470, 475 (1948). Since corporations at common law could not act outside of the narrow purposes and powers customarily stated in their articles of incorporation together with the powers necessarily incidental thereto, MODEL ACT § 7, Comment ¶ 2, at 278, anyone who dealt with a corporation acted at his peril in that regard. Under former law, ultra vires acts were deemed void in Arizona and could not be validated by ratification or otherwise. Trico Elec. Cooperative, Inc. v. Ralston, *supra* at 367, 196 P.2d at 475. Although ARIZ. REV. STAT. ANN. § 10-007 (Supp. Pamphlet 1975) alters that approach, it does not address the validity of intra vires acts which are not authorized by the proper corporate authority. MODEL ACT § 7, Comment ¶ 2, at 279.

93. *Compare* ARIZ. REV. STAT. ANN. §§ 10-122(1) *and* -481(B) (1956) *with* ARIZ. REV. STAT. ANN. §§ 10-008(A)(3) *and* -108(3) (Supp. Pamphlet 1975).

94. Under the Act, the name must contain the word "association," "bank," "corporation," "company," "incorporated," or "limited," or an abbreviation thereof. ARIZ. REV. STAT. ANN. § 10-008(A)(1) (Supp. Pamphlet 1975). For other limitations on corporate names, see sections 10-008(A)(2),(4).

95. *Id.* §§ 10-008(A)(3), -108(3). Filing of trade names is not current, however; See Annot. 2 *infra.*

Formerly corporate names were protected under the common law of unfair competition, which prevented a person from adopting or using a name, trade designation, or style which was identical to or deceptively similar to that of someone already operating in the trade area. MODEL ACT § 8, Comment ¶ 2, at 293. If use by the second user would have caused actual confusion with the first, the use by the second user was an infringement and was usually enjoined. *See* Boice v. Stevenson, 66 Ariz. 308, 319, 187 P.2d 648, 655 (1948); Lininger v. Desert Lodge, 63 Ariz. 239, 246, 160 P.2d 761, 764 (1945). The law of trade infringement as stated by the Arizona supreme court applied to any use of a trade name or style, whether it was the corporate name of the user, a

sent to the use of the name or a court decree establishing the prior right of the applicant to the use of the name in Arizona is filed with the Arizona Corporation Commission.[96] Further, because of the filing duties imposed on the commission, it will have to verify with the secretary of state the availability of the name chosen by all applicants for incorporation or for authority to transact business in Arizona,[97] thereby placing additional administrative burdens upon both offices.[98]

(2) *Indemnification.* One of the more significant provisions of the Act is that permitting indemnification of members of corporate management for expenses incurred by them in defending against personal liability suits based on an alleged breach of corporate duty.[99] Corporate management's need for protection has grown sharply in recent years,[100] and the Act continues and enlarges the indemnity power permitted under prior law.[101] The parties subject to indemnification include present and former directors, officers, employees, or agents either of the corporation or of other business entities serving at the

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trade name adopted by a corporate user, or a name adopted by an unincorporated business. The new Act seemingly does not prevent the incorporation of a business with a name which would potentially infringe a prior use, but which is not actually embodied in the corporate name of such prior user, and which will not be used in the proposed corporation's business. ARIZ. REV. STAT. ANN. § 10-008(A)(2) (Supp. Pamphlet 1975). It is not certain, however, that the name provisions of the new Act will be interpreted as abrogating the common law of trade name protection; several states have inserted in their corporation codes specific provisions negating this result, MODEL ACT § 8, Comment ¶ 3.03(6), at 303, but Arizona did not follow this course.

Of potentially greater concern is the absence in Arizona's trade name statutes, ARIZ. REV. STAT. ANN. §§ 44-1460 to -1460.05 (1967), of any method by which a registered trade name not in use may be challenged or cancelled prior to the expiration of the registration period. Under section 44-1460.02 a trade name may be registered for a term of 5 years with right of renewal for successive like terms upon application prior to the expiration of the then existing term. No legal impediment would appear to exist to the wholesale registration of trade names and the subsequent sale of consent to use such names. *See* ARIZ. REV. STAT. ANN. § 10-008(A)(3)(a) (Supp. Pamphlet 1975). This potential problem would be avoided by the adoption of pending House Bill 2364, which eliminates the requirement that the corporate name not be the same as, or deceptively similar to, any trade name registered with the secretary of state. H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 3 (1976).

96. ARIZ. REV. STAT. ANN. § 10-008(A)(3) (Supp. Pamphlet 1975). See discussion note 95 *supra.*

97. *See* ARIZ. REV. STAT. ANN. §§ 10-055(A)(2), -111(A) (Supp. Pamphlet 1975). See discussion note 95 *supra.*

98. *Compare* S. 1097, 31st Ariz. Legis., 1st Sess. § 10-055 (1973), *with* ARIZ. REV. STAT. ANN. § 10-055 (Supp. Pamphlet 1975). See discussion note 95 *supra.*

99. ARIZ. REV. STAT. ANN. § 10-005 (Supp. Pamphlet 1975). See Model Articles 10A-B & Annot. 30 *infra.*

100. The growth of derivative suits, criminal and civil antitrust actions, and especially personal liability suits under various federal statutes such as the securities laws have necessitated some form of indemnification in order for corporations to maintain competent management staffs. MODEL ACT § 5, Comment ¶ 2, at 216-17. *See generally* Bishop, *Sitting Ducks and Decoy Ducks: New Trends in Indemnification of Corporate Directors and Officers,* 77 YALE L.J. 1078 (1968); Hershman, *Officers' and Directors' Responsibilities and Liabilities—Opening Remarks,* 27 BUS. LAW. *Symposium,* at 1 (1972); Comment, *Indemnification of the Corporate Insider: Directors' and Officers' Liability Insurance,* 54 MINN. L. REV. 667 (1970).

101. *Compare* ARIZ. REV. STAT. ANN. § 10-005 (Supp. Pamphlet 1975) *with* former ARIZ. REV. STAT. ANN. § 10-198 (Supp. Pamphlet 1975).

request of the corporation.[102] Indemnification is not available, however, unless a disinterested majority of the board of directors, independent legal counsel, a court, or the shareholders find as a matter of fact that the officer, director, employee, or agent acted or failed to act "in good faith and in a manner he reasonably believed to be in or not opposed to the best interests of the corporation, and, with respect to any criminal action or proceeding, "had no reasonable cause to believe his conduct was unlawful."[103]

The permitted indemnification under the Act is more extensive than that provided by former Arizona law,[104] which did not specifically permit indemnification for amounts paid in settlement or compromise of a dispute. Although this provision was never interpreted by Arizona courts, the general hostility of courts to indemnification in the absence of express statutory authorization might have prevented corporations from indemnifying their officers and directors for amounts paid to settle cases, regardless of apparent authority granted by their articles of incorporation.[105] The Act makes it clear that corporations henceforth will have that power in third party actions against corporate defendants.[106]

Statutory indemnification under the Act is permissive, except in the event of a successful defense, when a right of action exists for reimbursement of the reasonable expenses and attorneys' fees actually incurred by the person concerned.[107] Permissive indemnification in connection with other third party actions extends to expenses, judgments, fines, and amounts paid in settlement "actually and reasonably incurred."[108] In other derivative actions indemnification is permitted only to a person not "adjudged to be liable for negligence or misconduct

102. ARIZ. REV. STAT. ANN. § 10-005(B) (Supp. Pamphlet 1975).

103. *Id.* §§ 10-005(A), (D). It has been suggested that the "not opposed to the best interests of the corporation" language is designed to and does cover situations where a corporate official is sued for his own securities transactions because of his status with the corporation. Klink, Chalif, Bishop & Arsht, *Liabilities Which Can Be Covered Under State Statutes and Corporate By-Laws*, 27 BUS. LAW., *Symposium* at 109, 117 (1972).

104. Former ARIZ. REV. STAT. ANN. § 10-198 (Supp. Pamphlet 1975).

105. *See* H. HENN, *supra* note 11, § 379, at 800-04. Absent specific statutes, some courts have greatly restricted the power of indemnification on public policy grounds. The leading case so holding is New York Dock Co. v. McCollom, 173 Misc. 106, 16 N.Y.S.2d 844 (Sup. Ct. 1939). *But see* Solimine v. Hollander, 129 N.J. Eq. 264, 19 A.2d 344 (Ch. 1941). The *McCollom* decision led to enactment of indemnification statutes in most states. Since an extension of the indemnification power may be viewed with disfavor by the courts, inclusion of the permissive provisions in articles rather than bylaws is advisable in order to strengthen the position of the corporation in granting indemnity. See Annot. 30 *infra*. *See* Comment, *Indemnification of Directors and Officers: Public Policy v. Corporate Responsibility*, 48 J. URBAN L. 957 (1971).

106. ARIZ. REV. STAT. ANN. § 10-005(A) (Supp. Pamphlet 1975).

107. *Id.* § 10-005(C). This limited mandatory indemnification, however, does not extend to a person serving at the request of the corporation as a director, officer, employee, or agent of another business enterprise. *Compare id., with id.* § 10-005(A). Mandatory indemnification may also be provided by inclusion of a provision in the articles of incorporation. See Annot. 30 *infra*.

108. ARIZ. REV. STAT. ANN. § 10-005(A) (Supp. Pamphlet 1975).

in the performance of his duty to the corporation" and then only for expenses, including attorneys' fees but not judgments and fines.[109] The Act provides exceptions to this rule, however, where the court orders that no indemnification be granted or, on the other hand, that the person be indemnified, in addition to expenses, for some or all of amounts paid in settlement.[110]

The scope of conduct which may give rise to indemnification also has been broadened under the Act to include acts performed without the scope of employment but arising by reason of status as an officer, director, employee, or agent.[111] The Act provides a procedure for case-by-case determination of whether permissive indemnification is authorized where there is no court order regarding indemnification.[112] To ease the impact of the delay occasioned by such proceedings, the Act also authorizes advances of expenses to be made against a guarantee of repayment by the person concerned if he is ultimately adjudged not entitled to indemnification.[113]

The statutory indemnification is not exclusive of any other rights of indemnification granted by the appropriate corporate authority.[114] The corporation may provide insurance for any person presently or formerly occupying a position subject to permissive indemnification, even if the corporation would lack power to indemnify such person against such liability under the conditions for permissive indemnification.[115] Finally, the Arizona Act extends the statutory power of indemnification to any existing or future corporation without the addition of an implementing provision in the corporation's articles of incorporation or bylaws.[116]

109. *Id.* § 10-005(B).

110. *Id.* It is to be anticipated that various courts will reach different conclusions on the public policy to be followed in awarding expenses such as attorneys' fees and settlement costs in derivative actions.

111. *Compare* former ARIZ. REV. STAT. ANN. § 10-198(B) (Supp. Pamphlet 1975) *with* ARIZ. REV. STAT. ANN. §§ 10-005(A)-(B) (Supp. Pamphlet 1975).

112. ARIZ. REV. STAT. ANN. § 10-005(D) (Supp. Pamphlet 1975).

113. *Id.* § 10-005(E).

114. *Id.* § 10-005(F).

115. *Id.* § 10-005(G). This provision conclusively resolves the question of corporate authority to pay the premiums on liability insurance for corporate directors, officers, employees, and agents. It does not set forth, however, any specific standards as to what liabilities such insurance may cover, thereby giving rise to public policy considerations requiring resolution by the courts. *See generally* Northwestern Nat'l Cas. Co. v. McNulty, 307 F.2d 432 (5th Cir. 1962). On its face the authorization to maintain insurance would seem to permit management to be saved from the financial consequences of its own negligence or misconduct in every case. It seems unlikely, however, that courts will hold that the provision overrules the common law policy against insurance which purports to protect against the consequences of deliberate or, possibly, reckless wrongdoing. For a general discussion of indemnity insurance, see Knepper, *Corporate Indemnification and Liability Insurance for Corporation Officers and Directors*, 25 SW. L.J. 240 (1971); Potter, *Directors' and Officers' Liability Insurance*, 9 ALBERTA L. REV. 331 (1971).

116. ARIZ. REV. STAT. ANN. § 10-005(H) (Supp. Pamphlet 1975). This provision is not found in the Model Act.

(3) *Certificates of Conformance and Disclosure.* In a provision not found in the Model Act, and considerably more comprehensive than former regulatory provisions, the Act requires the filing of "certificates of conformance" and provides penalties for failure to comply.[117] Under the new provision, the persons subject to the disclosure requirements, the categories of violations which must be disclosed, the nature of information which must be supplied, the penalties for noncompliance, and the applicability of penalties to persons other than officers and directors of the corporation on whose behalf the disclosure is made all differ from former law.[118] The Act has substantially increased the categories of persons required to disclose, and now includes "all officers, directors, trustees, incorporators and persons controlling or holding over ten per cent of the issued and outstanding common shares or ten per cent of any other proprietary, beneficial or membership interest in the corporation . . . ."[119] Generally, disclosure must be made of any involvement in various civil and criminal violations by such individuals.[120] Like the prior statutes, the disclosures required are limited to those items expressly set forth in the statute,[121] and the imposition of criminal sanctions requires knowing misrepresentations or concealments.[122]

The initial document to be filed with the Arizona Corporation Commission under the Act, denominated a "certificate of disclosure,"[123] may in certain cases result in the issuance by the commission of detailed interrogatories.[124] These must be answered to the commission's satisfaction under penalty of its denial to accept for filing articles of incorporation or an application for authority to transact business, or, if the corporation already is in existence or admitted to transact business in Arizona, revocation of the filing of the articles of incorporation or authority to transact business.[125] The commission also is granted entirely new regulatory authority to issue interrogatories regarded as necessary to enable it to ascertain whether compliance has been made with the Act.[126]

117. *Compare* former ARIZ. REV. STAT. ANN. § 10-199 (Supp. Pamphlet 1975) *with* ARIZ. REV. STAT. ANN. § 10-128 (Supp. Pamphlet 1975). *See also id.* § 10-135.
118. *Compare, e.g.*, former ARIZ. REV. STAT. ANN. §§ 10-199(A), (F) (Supp. Pamphlet 1975) *with* ARIZ. REV. STAT. ANN. §§ 10-128(A), (G) (Supp. Pamphlet 1975). *See also id* § 10-135.
119. ARIZ. REV. STAT. ANN. § 10-128(A) (Supp. Pamphlet 1975).
120. *See id.*
121. *See id.*
122. *Id.* § 10-128(G).
123. *Id.* § 10-128.
124. *Id.* § 10-128(E).
125. *Id.* The application of section 10-128 to business trusts is subject to some doubt. Section 10-509 provides that business trusts are subject to the Arizona corporate law relating to the filing of required statements and reports. While section 10-128(A) of the Act appears to except business trusts by limiting its application to domestic and foreign corporations, section 10-128(B) seemingly includes business trusts.
126. *Id.* § 10-137.

(4) *Annual Reports.* The information required to be disclosed in annual reports by domestic and foreign corporations authorized to do business in Arizona has been increased significantly.[127] An important change in the new Act requires disclosure of the names of shareholders of record holding more than 20 percent of any class of shares issued by the reporting corporation, including persons beneficially holding such shares through nominees.[128] The reporting domestic or foreign corporation also must file a balance sheet prepared in accordance with generally accepted accounting principles as of the close of the corporation's fiscal year.[129] Additionally, the Act requires a brief statement of the character of the business, if any, in which the corporation actually is engaged in Arizona.[130] The dates on which each corporate officer and director took office, as well as their names and addresses, also must be disclosed.[131] The signatures of the appropriate corporate officials executing the annual report must be acknowledged,[132] and the report accompanied by a certificate of disclosure.[133]

(5) *Penalties.* Another subject of former law appearing in the Act in altered form is the prohibition of, and penalties for, certain acts. Many of the penalties are imposed directly on the corporation itself. In addition to the statutory grounds for involuntary dissolution of a corporation by the Arizona attorney general,[134] the Arizona Corporation Commission may revoke the filing of a corporation's articles of incorporation for failure in the time provided to pay an annual fee or penalty, to file an annual report, to cause a required publication to be made, to file an affidavit of publication, to file a certificate of disclosure, or to answer interrogatories propounded by the commission.[135] This same result may be worked if certain deficiencies appear in a corporation's initial certificate of disclosure or in its answers to written interrogatories propounded by the commission.[136] The authority of a foreign corporation to transact business within Arizona also may be revoked by the commission for failure to comply with a number of procedural requirements

127. *Compare* ARIZ. REV. STAT. ANN. § 10-211 (1956) *with* ARIZ. REV. STAT. ANN. § 10-125 (Supp. Pamphlet 1975).
128. ARIZ. REV. STAT. ANN. § 10-125(A)(7) (Supp. Pamphlet 1975).
129. *Id.* § 10-125(A)(8). Pending House Bill 2364 eliminates this requirement and substitutes in lieu thereof a mandatory statement in the annual report that "all corporate income tax returns required by Title 43 have been filed with the Arizona Tax Commission." H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 58 (1976).
130. *Id.* § 10-125(A)(3). *See also* text & note 73 *supra.*
131. ARIZ. REV. STAT. ANN. § 10-125(A)(4) (Supp. Pamphlet 1975).
132. *Id.* § 10-125(B).
133. *Id.* § 10-125(A)(9). See text & notes 117-26 *supra.*
134. ARIZ. REV. STAT. ANN. § 10-094 (Supp. Pamphlet 1975).
135. *Id.* § 10-095. As to the penalty for failure to make a required publication, see text & note 67 *supra.*
136. ARIZ. REV. STAT. ANN. §§ 10-128(D)-(E) (Supp. Pamphlet 1975).

such as filing.[137] In addition to its revocation authority, the commission has power to levy penalties against domestic and admitted foreign corporations for failure to file annual reports or pay annual fees,[138] against foreign corporations for transacting business within the state without authority,[139] and against admitted foreign corporations for failure to file with the commission in a timely manner any amendment to their articles of incorporation or articles of merger.[140]

Under certain circumstances the Superior Court of Arizona is given the power to liquidate the assets and business of a corporation.[141] Finally, it appears that the attorney general may bring judicial action to enjoin a corporation from the transaction of unauthorized business.[142]

Individuals also are subject to potential civil and criminal liability for actions taken in connection with a corporation. For instance, any person acting as a corporation without authority to do so or procuring incorporation through fraudulent means will be jointly and severally liable for all debts and liabilities incurred or arising from such acts.[143] Any person knowingly executing or contributing information to an untrue or misleading certificate of disclosure will be guilty of a misdemeanor.[144] Corporate officers also may be subject to civil liability arising from or connected with ultra vires acts,[145] false statements or knowing and wrongful alteration of corporate books or records,[146] or improper preparation or production of the record of shareholders.[147] Criminal sanctions as well may be imposed upon corporate officers for knowing failure or refusal to answer truthfully interrogatories propounded by the Arizona Corporation Commission,[148] for knowing execution of any document filed with the commission which is false in any material respect[149] or for knowing falsification or wrongful alteration of

137. *Id.* § 10-121.
138. *Id.* § 10-125(E).
139. *Id.* § 10-124(C).
140. *Id.* § 10-129(11).
141. *Id.* § 10-097. Subsection (A)(1) provides for liquidation when directors are deadlocked, irreparable injury to the corporation is threatened, and the shareholders are unable to break the deadlock. Subsection (A)(2) permits liquidation in an action by a creditor when a judgment claim is returned unsatisfied and the corporation is insolvent or when the insolvent corporation has admitted in writing that the claim is due and owing.
142. *See id.* § 10-007(3).
143. *Id.* § 10-146.
144. *Id.* § 10-128(G).
145. *Id.* § 10-007. Although the defense of ultra vires is generally rendered invalid under the Act, it is allowable in actions by a corporation or by shareholders in a derivative suit against incumbent or former officers of the corporation. *Id.* § 10-007(2).
146. *Id.* § 10-135. Comparable provisions in ARIZ. REV. STAT. ANN. §§ 10-192 to -194 (1956) carried criminal penalties, and the new Act also imposes criminal penalties for this conduct. *See* text & notes 148-50 *infra.*
147. ARIZ. REV. STAT. ANN. § 10-031(C) (Supp. Pamphlet 1975). No comparable provision is contained in the former Arizona General Corporation Law.
148. *Id.* § 10-136(A).
149. *Id.* A more limited criminal provision is contained in former ARIZ. REV. STAT. ANN. § 10-194 (1956).

corporate books, records, or accounts.[150]

The penalties applicable to all individuals and those applicable to officers relating to ultra vires acts,[151] and to interrogatory answers and documents filed with the Arizona Corporation Commission[152] apply to directors as well. In addition, corporate directors voting for or assenting to improper declarations of dividends or other distributions of the assets of a corporation, to improper purchase of the corporation's shares, or to distribution of the corporate assets upon liquidation without adequate provision for the payment and discharge of the corporation's liabilities and obligations will be jointly and severally liable to the corporation in the amount of the excess over the amount that could have been distributed legally.[153] Directors held liable upon such claims have a statutory right to contribution from other directors who also voted for or assented to the improper action and from shareholders receiving the proceeds of such dividends or distributions knowing them to be improper.[154] The dividend distribution liability provisions of the new Act represent a desirable change from the uncertainties inherent in the much maligned, frequently ignored, and seldom enforced former law.[155]

The Act eliminates criminal penalties[156] in favor of personal civil liability of a director to the corporation for distributions to himself or others which, although approved, contravene either the Act's provisions or the corporation's articles of incorporation.[157] The statute does provide directors with two defenses to such actions, however. Written dissent may be made either during the meeting at which the action was

150. ARIZ. REV. STAT. ANN. § 10-136(B) (Supp. Pamphlet 1975). A more limited criminal provision requiring an intent to defraud is contained in former ARIZ. REV. STAT. ANN. § 10-193 (1956).

151. ARIZ. REV. STAT. ANN. § 10-007 (Supp. Pamphlet 1975).

152. *Id.* § 10-136(A).

153. *Id.* § 10-048(A). The ABA Committee on Corporate Laws in 1974 approved a revision of Model Act § 48 expanding the situations in which directors will be entitled by statute to rely on others and the types of materials on which directors will have the right to rely in making decisions about these matters. *See 1975 Report, supra* note 8, at 501-12. The Arizona Bar Committee currently is studying this revision for possible recommendation to the legislature.

154. ARIZ. REV. STAT. ANN. §§ 10-048(D)-(E) (Supp. Pamphlet 1975).

155. *Compare* former ARIZ. REV. STAT. ANN. § 10-196 (Supp. Pamphlet 1975) *with* ARIZ. REV. STAT. ANN. § 10-048 (Supp. Pamphlet 1975). Probably no other section of the former Arizona General Corporation Law has given rise to so much unresolved uncertainty as has former section 10-196. For example, questions which are problematical under the vague contours of the former law include whether section 10-196(A)(2) prohibits a corporation from repurchasing its own stock, *see* Bank v. Wickersham, 99 Cal. 655, 34 P. 444 (1893); whether section 10-196(A)(5) prohibits the sale by a corporation of its stock to another corporation in return for the latter's stock or note; and what effect on the statutory prohibitions, if any, was wrought by the decision in Copper Belle Mining Co. v. Costello, 11 Ariz. 334, 95 P. 94 (1908) (solvent corporation's purchase of its own stock in good faith and for legitimate purpose upheld by the court, which failed to consider the predecessor of section 10-196).

156. *Compare* former ARIZ. REV. STAT. ANN. § 10-196(B) (Supp. Pamphlet 1975) *with* ARIZ. REV. STAT. ANN. § 10-048(A) (Supp. Pamphlet 1975).

157. ARIZ. REV. STAT. ANN. § 10-048(A)(1) (Supp. Pamphlet 1975).

taken or the next business day.[158] The director may also show that the action was taken in good faith by reliance on approved financial statements.[159] Although no longer subject to criminal liability therefor, directors have the continuing duty to determine when and under what circumstances corporate assets may be distributed,[160] when funds are available for the declaration and payment of dividends, and from which funds dividends may be paid.[161] Directors also continue to be subject to liability for mismanagement[162] and failure to manage[163] under common law principles.

(6) *Disposition of Assets.* Another of the Act's major changes which could become of immediate concern to existing corporations involves the inclusion for the first time of statutory provisions governing the disposition, mortgage, or pledge of all or substantially all of the assets of a corporation.[164] Under common law, unanimous consent of all of the shareholders was required for the sale of all or substantially all of a corporation's assets.[165] Although this rule was relaxed in Arizona to permit disposal of assets in connection with a voluntary corporate dissolution, authorization merely by the board of directors was not sufficient.[166] While it also appeared settled that, absent a provision to the contrary in the articles of incorporation, the directors of an Arizona corporation could mortgage some corporate assets without shareholder consent,[167] it was by no means clear whether directors could mortgage all or substantially all of the assets without consent, nor what vote was required for any consent.[168]

158. *Id.* § 10-048(B).
159. *Id.* § 10-048(C). The element of reliance required under the Act may constrict the defense permitted under prior case law, whereby officers and directors were not held personally liable for errors of judgment made in good faith within the scope of the corporation's ordinary business. *See* Tovrea Land & Cattle Co. v. Linsenmeyer, 100 Ariz. 107, 121, 412 P.2d 47, 56-57 (1966); Kadish v. Phoenix-Scotts Sports Co., 11 Ariz. App. 575, 578, 466 P.2d 794, 797 (1970).
160. *See* ARIZ. REV. STAT. ANN. § 10-046 (Supp. Pamphlet 1975).
161. *See id.* § 10-045.
162. For a convenient checklist of directors' duties and potential liabilities, see W. KNEPPER, LIABILITY OF CORPORATE OFFICER AND DIRECTORS § 15.02 (2d ed. 1973). *See also* articles & comments cited note 100 *supra.*
163. *See* DePinto v. Provident Security Life Ins. Co., 374 F.2d 37, 43-44 (9th Cir. 1967).
164. *See* ARIZ. REV. STAT. ANN. §§ 10-078 to -081 (Supp. Pamphlet 1975).
165. Geddes v. Anaconda Copper Mining Co., 254 U.S. 590 (1921); Thayer v. Valley Bank, 35 Ariz. 238, 242, 276 P. 526, 527 (1929); Little Butte Consol. Mines Co. v. Girand, 14 Ariz. 9, 14, 123 P. 309, 311 (1912).
166. ARIZ. REV. STAT. ANN. §§ 10-362(C) (1956) (vote of two-thirds of valued stock required); *see* Thayer v. Valley Bank, 35 Ariz. 238, 276 P. 526 (1929). The *Thayer* court also recognized two exceptions to the general rule of shareholder consent to sales of all of a corporation's assets. In situations where a failing corporation disposes of its assets for the purpose of closing out the business, or where the conversion of all assets into cash furthers the business for which the corporation was organized, authorization by the board of directors may suffice. *Id.* at 239, 276 P. at 527.
167. Copper Belle Mining Co. v. Costello, 11 Ariz. 334, 344, 95 P. 94, 97 (1908).
168. Application of prior Arizona authority in analogous situations could produce

The new Act distinguishes between sales, leases, exchanges, or other dispositions of assets on the one hand, and mortgages and pledges of assets on the other.[169] The Act further distinguishes between dispositions in the ordinary course of business and those not usual and regular.[170] The board of directors, without authorization or consent of the shareholders, has the authority to sell, lease, exchange, or make any other disposition of all, or substantially all, the property and assets of a corporation in the usual course of its business.[171] A separate procedure is established for a disposition of such assets which is not in the ordinary course of corporate business, including the requirement of authorization by a majority of the shares entitled to vote on the question.[172] However, the board may, in its discretion, abandon the disposition without further action by the shareholders, subject only to the contractual rights of third parties.[173] Finally, the Act provides that the board of directors may authorize the mortgage or pledge of any or all property and assets of a corporation without the authorization or consent of the shareholders, whether or not in the usual and regular course of business.[174]

This increased flexibility is counterbalanced by other provisions, however. The Act grants shareholders dissenters' and appraisal rights[175] in any sale or exchange of all or substantially all of the property

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conflicting answers to this question. Since common law required all of the shareholders to consent to the sale of all or substantially all of the corporate assets, *see* text & notes 165-66 *supra*, and since the consequences of a mortgage closely approximate those of a sale in the event of default, it could be argued that a mortgage of such assets also required unanimous shareholder consent. On the other hand, since the directors may borrow funds and issue bonds, Citrus Growers' Dev. Ass'n, Inc. v. Salt River Valley Water Users' Ass'n, 34 Ariz. 105, 123-24, 268 P. 773, 780-81 (1928), at least within the limitations on indebtedness imposed by former ARIZ. REV. STAT. ANN. §§ 10-173, -177 (1956) and any conditions imposed by the articles of incorporation, it may be argued—somewhat less persuasively perhaps—that the directors acting on their own authority also could mortgage all or substantially all of the corporation's assets.

169. *See* ARIZ. REV. STAT. ANN. § 10-078 (Supp. Pamphlet 1975). Adopting the Model Act's position, the Arizona Act recognizes the substantive distinction between sales and mortgages. *See* MODEL ACT §§ 78-79, Comment 2, at 417.

170. ARIZ. REV. STAT. ANN. §§ 10-078 to -079 (Supp. Pamphlet 1975).

171. *Id.* § 10-078. *See also id.* § 10-004(A)(5). While the term "usual and regular course of business" is not defined in the Act, the term "regular course of business" "must find its meaning in the inherent nature of the business in question and in the methods systematically employed for the conduct of the business as a business." Palmer v. Hoffman, 318 U.S. 109, 115 (1943). For examples of sales in the regular course of business, see Phillips Petroleum Co. v. Rock Creek Mining Co., 449 F.2d 664 (9th Cir. 1971); Santa Fe Hills Golf & Country Club v. Safehi Realty Co., 349 S.W.2d 27 (Mo. 1961); *In re* Rosenshein, 16 App. Div. 2d 537, 229 N.Y.S.2d 14 (1962). For discussion of sales outside the regular course of business, see Alhambra-Shumway Mines, Inc. v. Alhambra Gold Mine Corp., 200 Cal. App. 2d 322, 19 Cal. Rptr. 208 (Dist. Ct. App. 1962); Marks v. Wolfson, 41 Del. Ch. 115, 188 A.2d 680 (Ch. 1963); Michigan Wolverine Student Co-op v. William Goodyear & Co., 314 Mich. 590, 22 N.W.2d 884 (1946).

172. ARIZ. REV. STAT. ANN. § 10-079 (Supp. Pamphlet 1975). *See* Eisenberg, *The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking*, 57 CALIF. L. REV. 1 (1969).

173. ARIZ. REV. STAT. ANN. § 10-079(4) (Supp. Pamphlet 1975).

174. *Id.* § 10-078.

175. *Id.* §§ 10-081 to -082. Shareholders objecting to certain extraordinary changes

and assets of a corporation not made in the usual and regular course of its business, excepting a judicial sale or cash sale in which all or substantially all of the sale proceeds are distributed to the shareholders within one year from the date of sale.[176] In the absence of contrary provision in the articles of incorporation, however, no dissenters' rights are available to holders of securities registered on a national securities exchange or to holders of shares which are held of record by more than 2,000 persons.[177] Although the denial of dissenters' and appraisal rights to shareholders of securities registered on a national securities exchange is included in the Model Act,[178] only two others of the many states adopting the Model Act have enacted this portion,[179] and its utility is questionable. Although shares sold on a national exchange theoretically would have the necessary marketability to make appraisal and purchase by the corporation unnecessary,[180] this assumption may or may not be warranted depending on the nature of the corporate action giving rise to the dissent and the volume of shares actually available on the open market. Denial of dissenters' and appraisal rights in this context may work an unfair result if the market declines swiftly and does not fairly represent the value of the stock.

(7) *"Short Form" Mergers.* The Act recognizes two types of so-called "short form" mergers which may be carried out without the shareholder approval required for "long form" or regular mergers.[181] Unless otherwise required by the articles of incorporation of the surviving corporation, no shareholder authorization is required for merger where: (1) the articles of incorporation of the surviving corporation are not amended; (2) the shares of the surviving corporation outstand-

in corporate structure frequently are granted a statutory right to require the corporation to purchase their shares at an "appraised" value. This right is particularly important for small private corporations without a ready market in which a dissenter can sell his shares. *See* H. HENN, *supra* note 11, § 349; Kaplan, *Problems in the Acquisition of Shares of Dissenting Minorities*, 34 B.U.L. REV. 291 (1954); Comment, *The Dissenting Shareholders' Appraisal Statute: Influence of Cost and Interest Provisions Upon the Efficacy of the Remedy*, 50 B.U.L. REV. 57 (1970).

176. ARIZ. REV. STAT. ANN. § 10-080(A)(2) (Supp. Pamphlet 1975). The division of the subsections of section 10-081, dealing with the rights of dissenting shareholders, could be improved since subsections (A) through (D) inclusive deal with dissents from mergers and consolidations only, while subsections (E) through (G) inclusive deal with dissents from sales or exchanges of assets. The remaining subsections are applicable to both subjects. The requirement for shareholder approval in regular or "long form" mergers is set forth in section 10-073.

177. *Id.* § 10-080(C). But see Model Article 13.4 & Annot. 36 *infra.*

178. MODEL ACT § 80.

179. KY. REV. STAT. ANN. § 271A.400 (Supp. 1974); N.J. STAT. ANN. § 14A:11-1 (Supp. 1975-76).

180. See discussion note 175 *supra.*

181. ARIZ. REV. STAT. ANN. § 10-073(C), -075 (Supp. Pamphlet 1975). Under former law, all mergers were subject to shareholder approval. ARIZ. REV. STAT. ANN. §§ 10-343 to -344 (1956). For general discussion of mergers in Arizona, see Note, *AICPA Efforts to Curb Abuses in Accounting for Corporate Acquisitions: Their Inadequacies and a Proposed Solution*, 12 ARIZ. L. REV. 543 (1970); "Corporate Merger and the Survival of Loss Carryovers for State Tax Purposes," 16 ARIZ. L. REV. 489, 625 (1974).

ing immediately prior to the merger remain outstanding immediately after the merger without alteration; and (3) no more than 20 percent of the shares, securities, and convertible obligations of the surviving corporation are to be issued in connection with the merger.[182] In addition, the board of directors of any corporation owning at least 90 percent of the outstanding shares of each class and series of its subsidiary corporation may carry out an "upstream" merger without the approval of the shareholders of either corporation.[183] In both cases, shareholders are denied the statutory right of dissent applicable to other mergers.[184]

(8) *Foreign Corporations.* The provisions of the former Arizona General Corporation Law relating to foreign corporations[185] also have been altered materially.[186] The first major change in the new Act's approach to regulation of foreign corporations is the nonexclusive enumeration of those activities of a foreign corporation which do not constitute "transacting business."[187] Whether a foreign corporation is "doing" or "carrying on" business within the state is an important determination, since failure to qualify[188] before conducting business may result in denial of access to the court system for the purpose of

182. ARIZ. REV. STAT. ANN. § 10-073(C) (Supp. Pamphlet 1975).
183. *Id.* § 10-075.
184. *Id.* § 10-080(C).
185. The term "foreign corporation" was defined in former ARIZ. REV. STAT. ANN. § 10-102(B) (1956) as encompassing every corporation other than a corporation organized under the laws of Arizona.
186. *Compare* ARIZ. REV. STAT. ANN. §§ 10-481 to -485 (1956), *as amended*, (Supp. Pamphlet 1975), *with* ARIZ. REV. STAT. ANN. §§ 10-106 to -124 (Supp. Pamphlet 1975). The new Act only purports to regulate foreign corporations organized for profit. ARIZ. REV. STAT. ANN. § 10-002(11) (Supp. Pamphlet 1975). *But see id.* §§ 10-129(4), (6). Consequently, the status of foreign nonprofit corporations under the Act is uncertain. It has been stated, however, that any exclusion of foreign corporations must be expressed affirmatively to be effective, MODEL ACT § 106, Comment ¶ 2, at 609, and the Act contains no express exclusion of foreign nonprofit corporations.
187. ARIZ. REV. STAT. ANN. § 10-106(B) (Supp. Pamphlet 1975). The presently recognized "interstate commerce" exemption is expressly stated in *id.* § 10-106(B)(9); guidelines for application of the "isolated transaction" exemption are set forth in *id.* § 10-106(B)(10) ("isolated transaction" must be completed within a 30-day period and must not be one of a number of similar repeated transactions); and the "occurred in Arizona" exemption presumably remains in force. *See* Wolf Corp. v. Rollin, 17 Ariz. App. 250, 251, 497 P.2d 70, 71 (1972) (execution of note and mortgage outside of Arizona enabled foreign corporation to sue in Arizona courts, despite noncompliance with foreign corporation qualification statute). The long debated and unanswered questions of whether ARIZ. REV. STAT. ANN. § 10-485 (1956) established a "limited qualification" procedure or an exemption from the definition of "transacting business" in former section 10-481 and whether former section 10-485 was constitutional have been rendered moot by the Act, since the matters previously covered by section 10-485 now are contained in the enumeration of activities not constituting the transaction of business. *See* ARIZ. REV. STAT. ANN. §§ 10-106(B)(7)-(8) (Supp. Pamphlet 1975).
It should be noted that activities which constitute "doing business" for jurisdictional or taxation purposes are not necessarily equivalent to those comprising "doing business" for purposes of qualification. *See* McGee v. International Life Ins. Co., 355 U.S. 220 (1957); Phillips v. Anchor Hocking Glass Co., 100 Ariz. 251, 253, 413 P.2d 732, 733 (1966); Comment, *Foreign Corporation—What Constitutes "Doing Business" for Service of Process as Contrasted with Domestication Requirement*, 45 MICH. L. REV. 218 (1946).
188. *See* ARIZ. REV. STAT. ANN. §§ 10-110 to -111 (Supp. Pamphlet 1975).

maintaining actions unless qualification is accomplished.[189] Because the new statutory enumerations are nonexclusive,[190] common law developed prior to the Act presumably will continue to be useful in determining whether the corporation is "engaged in an enterprise of some permanence and durability and . . . [is transacting] within the state some substantial part of its ordinary business . . . ."[191]

The second major change wrought by the Act is the provision of a statutory penalty for failure of a foreign corporation doing business to qualify.[192] The Act eliminates the provision of the former statute voiding every act done prior to complying with all requirements for doing business in the state.[193] Prior to the Act, Arizona used a two-prong balancing test to determine whether or not the contract of a foreign corporation would be recognized by a state court. In order to hold a nonqualifying foreign corporation's contract void, the evidence had to show "(1) that the plaintiff was 'transacting business in Arizona' within the meaning of the qualification statute at the time the contract was entered into, and (2) that the particular act sought to be declared null and void occurred in Arizona."[194] The Act, in contrast, expressly states that failure of a foreign corporation to obtain authority to transact business in the state will neither impair the validity of any contract or act nor prevent the corporation from defending itself on a contract action in the state courts.[195] Moreover, any contract may be enforced by a nonqualifying foreign corporation after qualification.[196]

E. *New Statutory Subjects*

The major changes in existing Arizona corporate practice probably will result from the many aspects of that practice subject to express

189. *See id.* § 10-124(A). Under the Act, while a foreign corporation not doing business in the state may maintain and defend suits and actions, *id.* § 10-106(B)(1), a nonqualifying corporation doing business in Arizona does not have access to the state courts except to defend an action. *Id.* §§ 10-124(A)-(B).

190. ARIZ. REV. STAT. ANN. § 10-106(B) (Supp. Pamphlet 1975).

191. L.M. White Contracting Co. v. St. Joseph Structural Steel Co., 15 Ariz. App. 260, 263, 488 P.2d 196, 199 (1971) (interpreting former ARIZ. REV. STAT. ANN. § 10-482 (1956)); *accord*, National Union Indem. Co. v. Bruce Bros., 44 Ariz. 454, 462, 38 P.2d 648, 656 (1934); Monaghan & Murphy Bank v. Davis, 27 Ariz. 532, 536, 234 P. 818, 820 (1925); Rochester Capital Leasing Corp. v. Sprague, 13 Ariz. App. 77, 79, 474 P.2d 201, 203 (1970). *See generally* Gavin, *Doing Business As Applied to Foreign Corporations*, 11 TEMP. L.Q. 46 (1936); Kinnally, *What Constitutes Doing Business By a Foreign Corporation?*, 15 IND. L.J. 520 (1940); *What Constitutes Doing Business, Evaluation of Court Decisions*: 1. *Qualification-Decisions of the Supreme Court of the United States*, 21 CORP. J. 3 (1954); *What Constitutes Doing Business, Evaluation of Court Decisions: 2. Qualification-Decisions of State Courts*, 21 CORP. J. 123 (1955).

192. *See* ARIZ. REV. STAT. ANN. § 10-124(C) (Supp. Pamphlet 1975).

193. ARIZ. REV. STAT. ANN. § 10-482 (1956).

194. Wolf Corp. v. Rollen, 17 Ariz. App. 250, 251, 497 P.2d 70, 71 (1972); *see* Neiderhiser v. Henry's Drive-In, Inc., 96 Ariz. 305, 307-08, 394 P.2d 420, 422 (1964); Rochester Capital Leasing Corp. v. Sprague, 13 Ariz. App. 77, 80, 474 P.2d 201, 204 (1970).

195. ARIZ. REV. STAT. ANN. § 10-124(B) (Supp. Pamphlet 1975).

196. *Id.* § 10-124(A).

statutory regulation for the first time under the Act. The subject matter of the new statutory provisions ranges from the abolition in large part of the doctrine of ultra vires[197] to the acceptance of certified copies of documents filed with the Arizona Corporation Commission as prima facie evidence of the existence or nonexistence of the facts stated therein.[198] The rights and duties of directors and shareholders and the procedural aspects of the issuance of stock also have been codified. The Act creates an environment in which creative Arizona practitioners may be of substantial service to corporate clients in setting up management structures tailored to specific needs.

(1) *Directors.* For the first time in Arizona many of the essential aspects of law relating to directors and corporate management are subject to statutory mandate. The Act provides for considerable leeway in the management structure of a corporation. Although a board of directors is required,[199] its duties and powers may be reserved to the shareholders by the articles of incorporation.[200] Unlike the former law,[201] the Act provides no guidelines for the qualification of direc-

197. *Id.* § 10-007. See discussion note 92 *supra.*

198. ARIZ. REV. STAT. ANN. § 10-141 (Supp. Pamphlet 1975); *see* ARIZ. REV. STAT. ANN. §§ 12-2262 to -2263 (1956) (providing that business records, including reproductions and certified copies thereof, are competent, admissible evidence under certain circumstances).

199. ARIZ. REV. STAT. ANN. §§ 10-035 to -036 (Supp. Pamphlet 1975). See Annot. 18 *infra.* Although the former law made reference to directors, *see* former ARIZ. REV. STAT. ANN. §§ 10-191, -196 (Supp. Pamphlet 1975), a board of directors was not specifically required. *See* ARIZ. CONST. art. 14, § 10 (referring to directors or managers in the alternative); ARIZ. REV. STAT. ANN. § 10-122(7) (1956) (referring to officers' conducting the corporation's affairs).

200. ARIZ. REV. STAT. ANN. § 10-035 (Supp. Pamphlet 1975). See Annot. 18 *infra.* The 1969 version of section 35 of the Model Act, on which the Arizona Act is based, does not grant and impose the powers and duties of directors, as conferred by the Act, upon nondirector persons charged with running the business and affairs of the corporation by the articles of incorporation. Without this provision, it may be questioned whether the management of a corporation not run by a board of directors has either the statutory powers or duties imposed upon directors by the Act. This issue is of special concern to the close or sole corporation. *See* MODEL ACT § 35, Comment ¶ 2, at 755.

The 1969 Model Act version, and hence the Arizona Act, also fail to define the term "managed" in section 10-035's statement of a board of directors' functions, thus relegating the definition to custom and case law. *Id.* at 754; *see* Tovrea Land & Cattle Co. v. Linsenmeyer, 100 Ariz. 107, 142 P.2d 47 (1966); Fagerberg v. Phoenix Flour Mills Co., 50 Ariz. 227, 71 P.2d 1022 (1937). MODEL ACT § 35, Addendum B (1974 rev.) codifies the duty of good faith:

> A director shall perform his duties as a director, including his duties as a member of any committee of the board upon which he may serve, in good faith, in a manner he reasonably believes to be in the best interests of the corporation, and with such care as an ordinarily prudent person in a like position would use in similar circumstances. In performing his duties, a director shall be entitled to rely on information, opinions, reports or statements and other financial data, . . . but he shall not be considered to be acting in good faith if he has knowledge concerning the matter in question that would cause such reliance to be unwarranted.

The Bar Committee is currently studying this revision for possible recommendation to the Arizona legislature.

201. *See* former ARIZ. REV. STAT. ANN. § 10-199 (Supp. Pamphlet 1975) (requiring the certificate of conformance to state whether the proposed director has been convicted of a crime, or was subject to any court order, judgment, or decree relating to unlawful conduct in connection with security transactions).

tors.[202] Although the Act speaks to the number of directors, it places no limits thereon, stating only that the board shall consist of one or more members.[203] A large board may be classified in such a way as to provide representation of special interest groups.[204] Further flexibility is provided by the ability of the directors to fill vacancies[205] and by the expanded permissible indemnification, which may entice otherwise wary but qualified "outside" directors to accept membership on the board.[206]

Procedural requirements for board meetings are also more flexible under the Act. Unless otherwise required by the articles of incorporation or bylaws, a quorum is a majority of directors then serving.[207] Meetings may be held either within or without the state;[208] in the absence of a bylaw prescription, regular meetings require no notice, and special meetings require only such notice as the bylaws mandate.[209]

202. ARIZ. REV. STAT. ANN. § 10-035 (Supp. Pamphlet 1975). The new Act requires no preliminary statutory qualifications other than those prescribed by the corporation's articles of incorporation or bylaws. MODEL ACT § 35, Comment ¶ 2, at 755. See Model Article 7.3 & Annot. 19 *infra.*

203. ARIZ. REV. STAT. ANN. § 10-036 (Supp. Pamphlet 1975). See Annot. 17 *infra.* While the provision permitting a one-member board will be of benefit to many close corporations, caution should be exercised so as to avoid the unanticipated application of the "alter ego" theory.

204. ARIZ. REV. STAT. ANN. § 10-037 (Supp. Pamphlet 1975). *See* Bohannan v. Corporation Comm'n, 82 Ariz. 299, 313 P.2d 379 (1957). Arizona attorneys have given various interpretations to the *Bohannan* decision, in which the Arizona supreme court granted a petition for a preemptory writ of mandamus to require the filing by the Arizona Corporation Commission of articles of incorporation providing for a nine-member board of directors whose terms would be staggered so as to result in the election each year of three directors for 3-year terms. The court stated that the election of one member of a three-member board each year for a 3-year term "unquestionably . . . is illegal and void as coming within the implied prohibition of the Constitution [art. 14, § 10]." *Id.* at 301, 313 P.2d at 381. The applicability of the *Bohannan* decision to nonprofit corporations and the validity of other classified boards, such as a six-member board with staggered terms so that only two members are elected in any given year, are questions yet to be answered. The Act only indirectly resolves these issues. Section 10-037 permits the classification of directors only when the articles of incorporation provide for a board of directors of a fixed number of nine or more members. It also limits the classification to either two or three classes and requires that the number of each class be fixed as nearly equal as possible. Under any plan, no classification is effective prior to the first annual shareholders meeting. See Model Article 7.1A & Annot. 16 *infra.*

205. ARIZ. REV. STAT. ANN. § 10-038 (Supp. Pamphlet 1975). But see Model Article 7.5 & Annot. 21 *infra.* Absent a provision in the bylaws allowing directors to fill vacancies, this was not possible under common law since the election of directors was an exclusive right of the shareholders. *See* 2 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS § 286 (rev. 1954).

The new section 10-039 sets forth the procedure by which any or all directors may be removed from their positions on the board with or without cause by the shareholders. The power of removal under common law was limited to removal for cause. *See* H. HENN, *supra* note 11, § 192, at 377. This removal provision must be read in conjunction with ARIZ. CONST. art. 14, § 10, and ARIZ. REV. STAT. ANN. § 10-033(D) (Supp. Pamphlet 1975), providing for cumulative shareholder voting. *See id.* § 10-039(B).

206. See text & notes 99-116 *supra*; Model Articles 10A-B & Annot. 30 *infra.*

207. ARIZ. REV. STAT. ANN. § 10-040 (Supp. Pamphlet 1975). See Model Article 7.6 & Annot. 22 *infra.* A majority of the authorized number of directors, as distinguished from the number then in office, constituted a quorum of the board at common law. *See* H. HENN, *supra* note 11, § 209, at 420. Unlike the Arizona Act, section 40 of the Model Act adopts the common law view.

208. ARIZ. REV. STAT. ANN. § 10-043(A) (Supp. Pamphlet 1975).

209. *Id.* § 10-043(B). At common law all directors either had to be present at or

Additionally, the ability to hold directors' meetings by means of conference telephone or similar communications equipment, to take board action by unanimous written consent without a meeting,[210] and to appoint an executive committee and delegate board functions to it[211] will enable even small, privately held corporations to establish a board composed of nationally qualified members, no matter where they live or work.

The final important codification in this area deals with director conflicts of interest. The Act considerably expands the former statutory and common law by developing a specific standard of conduct for determining adherence to duty.[212] Contracts and other transactions between a corporation and an interested party or an entity in which the director has a financial interest are neither void nor voidable under the Act if the relationship was fully disclosed prior to ratification and if the contract or transaction is fair and reasonable to the corporation.[213]

(2) *Shareholders.* Many procedural aspects of the shareholder status also are regulated by statute for the first time in Arizona under the Act, including where meetings may be held, the notice required, and

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notified of all meetings, except specified regular meetings. *See* Lycette v. Green River Gorge, 21 Wash. 2d 859, 863, 153 P.2d 873, 875-76 (1944).

210. ARIZ. REV. STAT. ANN. § 10-043(A) (Supp. Pamphlet 1975). At common law, directors could act only at a meeting. *See* H. HENN, *supra* note 11, at § 209. *But see In re* Kirchoff Frozen Foods, Inc., 375 F. Supp. 156, 163-64 (D. Ariz. 1972), *aff'd*, 496 F.2d 84 (9th Cir. 1974) (holding that the acts of directors of a close corporation without a duly convened meeting are not illegal per se). A meeting requirement may be useful in some circumstances. See Model Article 7.9 & Annot. 25 *infra*.

211. ARIZ. REV. STAT. ANN. § 10-042 (Supp. Pamphlet 1975). See Annot. 24 *infra*. This section codifies the common law which gave the board of directors the power to appoint an executive committee composed of board members and to delegate to it functions and powers of the board not delegable to nondirectors. *See* H. HENN, *supra* note 11, at § 212. The Act also gives statutory authorization to the common law practice of allowing the board of directors to delegate ministerial functions to a committee which includes nondirectors among its members. *See id.*

212. *Compare* former ARIZ. REV. STAT. ANN. § 10-196 (Supp. Pamphlet 1975) *with* ARIZ. REV. STAT. ANN. § 10-041 (Supp. Pamphlet 1975). Arizona common law imposed on directors a fiduciary duty to the corporation and its stockholders. DePinto v. Landoe, 411 F.2d 297, 300 (9th Cir. 1969); Steinfeld v. Nielsen, 15 Ariz. 424, 444, 139 P. 879, 887-88 (1914); Hatch v. Emery, 1 Ariz. App. 142, 146, 400 P.2d 349, 353 (1965); *see* Slaughter, *Corporate Opportunity Doctrine*, 18 SW. L.J. 96 (1964); Wadland, *Conflicts of Interest*, 17 BUS. LAW. 48 (1961); Comment, *The Corporate Opportunity Doctrine: Has It Meaning in Arizona?*, 9 ARIZ. L. REV. 59 (1967).

213. ARIZ. REV. STAT. ANN. § 10-041(A) (Supp. Pamphlet 1975). A literal reading of section 10-041(A) reveals that the requirements of disclosure and ratification on the one hand, and of the transaction's fairness and reasonableness on the other, have been framed in the disjunctive. A general fairness requirement arguably may nevertheless be read into all three parts of section 10-041(A), thereby necessitating such a showing in all conflict of interest situations. *See* N. LATTIN, THE LAW OF CORPORATIONS § 80, at 291-93 (2d ed. 1971).

One interesting aspect of the Act is that it shifts the burden of proof on the issue of the fairness of transactions between directors and their corporations, previously placed upon the directors by Tovrea Land & Cattle Co. v. Linsenmeyer, 100 Ariz. 107, 123, 412 P.2d 47, 58 (1966), to the complaining party. ARIZ. REV. STAT. ANN. § 10-041(B) (Supp. Pamphlet 1975). This provision, not present in section 41 of the Model Act, is contrary to general law. *See* H. HENN, *supra* note 11, § 238; Marsh, *Are Directors Trustees?*, 22 BUS. LAW. 35, 44-45 (1966).

waiver thereof;[214] establishment of a record date to determine the shareholders entitled to notice or vote;[215] quorum requirements;[216] the taking of action without a meeting;[217] and various aspects of voting.[218]

One interesting aspect of the Act's shareholder voting provisions deals with the right of shareholders to vote on amendments to the articles of incorporation increasing the corporation's authorized stock. The Arizona constitution requires the consent of holders of the "larger amount in value of the stock" for an increase in the corporation's stock.[219] The Act, on the other hand, provides that amendments to the articles of incorporation may be adopted by an affirmative vote of the holders of a majority of the shares entitled to vote thereon or, if a class or series of shares is entitled to vote as such, by affirmative vote of a majority of shares of each voting class or series and a majority of the total number of shares entitled to vote thereon.[220] The only interpretation which seemingly would satisfy both the constitution and the Act in this context would require a consenting vote of both the majority of all shares entitled to vote thereon and of those holding the larger value of stock.[221]

214. ARIZ. REV. STAT. ANN. §§ 10-028 to -029, -144 (Supp. Pamphlet 1975). Section 10-028 permits shareholders' meetings to be held outside the state of incorporation. Section 10-029 alters the common law rule of implied notice of annual meetings when the times and places of such meetings are fixed in the articles or bylaws by requiring that written notice of regular as well as special meetings be given to all shareholders entitled to vote at the meetings. See text & notes 257-58 *infra*. Section 10-144 does not change the common law rule that shareholders may waive the requirement of notice, either prospectively or retrospectively. *See* H. HENN, *supra* note 11, § 191.

215. ARIZ. REV. STAT. ANN. § 10-030 (Supp. Pamphlet 1975). Section 10-030 grants the power, not present at common law, to determine voting and other rights on the basis of a record date. An express contradiction in the Act appears in the provisions dealing with the record date for determining shareholders entitled to express consent to corporate action in writing without a meeting as provided by section 10-145. *Compare id.* § 10-030(B)(2) *with id.* § 10-030(B)(3). Pending House Bill 2364 would eliminate this contradiction by repealing section 10-030(B)(3) in its entirety. H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 11 (1976). In addition no provision is made in the Act for the fixing of a record date for the payment of dividends if the directors fail to fix such date in advance. Under the Model Act, the record date in such circumstances is the date on which the board of directors determined to pay the dividend. MODEL ACT § 30.

216. ARIZ. REV. STAT. ANN. § 10-032 (Supp. Pamphlet 1975) (a majority of the shareholders entitled to vote unless otherwise provided by the articles of incorporation, but in no event less than one-third of the shares entitled to vote at the meeting). See Annot. 33 *infra*.

217. ARIZ. REV. STAT. ANN. § 10-145 (Supp. Pamphlet 1975) (requiring written consent to the action signed by all of the shareholders entitled to vote on the subject).

218. *See* ARIZ. REV. STAT. ANN. §§ 10-033, -059, -060, -143 (Supp. Pamphlet 1975). See Model Articles 13-13.3 & Annots. 33-35.

219. ARIZ. CONST. art. 14, § 6.

220. ARIZ. REV. STAT. ANN. § 10-059 (Supp. Pamphlet 1975).

221. It is possible that those with the "larger value" of stock would not be affected by an increase in authorized shares of a different class of stock. The constitutional restriction arguably could be interpreted to mean that only within the affected class would the "larger value" requirement of Arizona's constitution have to be met along with the Act's requirement of a majority of the total number of shares entitled to vote thereon. Such an interpretation seemingly would satisfy the intent of the constitutional restriction—preventing dilution of stock—although it circumvents the literal wording of the provision. In any event, determination of "value" for purposes of this constitutional

Another notable issue related to shareholder interests involves the voting provisions for mergers, consolidations, and acquisitions of stock or assets. Where a corporate reorganization is accomplished through an acquisition of stock or assets, the Act requires no vote of the acquiring shareholders so long as there are sufficient authorized but unissued shares to complete the purchase.[222] The shareholders of the acquired corporation, on the other hand, must approve a sale of assets[223] but not a sale of stock.[224] If the combination is achieved via merger or consolidation, in most cases the shareholders of both corporations must approve the plan.[225] In "short form" mergers, however, no vote of the surviving corporation's shareholders is required.[226] Shareholders' voting rights in these transactions may, of course, be increased by appropriate provision in the articles of incorporation.[227]

(3) *Issuance of Stock and Rights Thereto.* The issuance of stock and the rights thereto are subject to new statutory regulation under the Act. In particular, the new Act contains provisions initially regulating share subscriptions,[228] the type of consideration for which shares validly may be issued,[229] the payment of reasonable organization, reor-

provision is problematical. For a discussion of article 14, section 6 of the Arizona constitution, see McRae, *"Watered Stock"—Shareholder's Liability to Creditors*, 8 ARIZ. L. REV. 327 (1967).

222. *Cf.* ARIZ. REV. STAT. ANN. § 10-015, -054(A)(5) (Supp. Pamphlet 1975). Where an insufficient number of shares is authorized but unissued, an amendment to the articles increasing the stock authorization will be necessary. *See id.* § 10-058(B)(4). Such an amendment requires a vote of the shareholders, *id.* §§ 10-059 to -060, and must pass by the same margin required for a merger or consolidation. *Compare id.* § 10-059(A)(3) *with id.* § 10-073(B).

223. ARIZ. REV. STAT. ANN. §§ 10-079(2)-(3) (Supp. Pamphlet 1975). Approval is necessary only for a sale not in the regular course of business. *See id.* § 10-078; text & notes 164-74 *supra.*

224. Since stock is freely transferable under the Act, subjecting sales of stock to shareholder approval would contravene basic policies of the legal treatment of corporations.

225. ARIZ. REV. STAT. ANN. § 10-073 (Supp. Pamphlet 1975).

226. *Id; id.* § 10-075. See text & notes 181-84 *supra.* Such mergers, of course, entail little change in shareholder status.

227. *See id.* § 10-054(A)(12). *Cf.* Model Article 13.4 *infra.* There is a certain lack of uniformity in the Act's requiring shareholder approval for some, but not all, forms of reorganization. This is particularly true since the interest of the stockholders of the acquiring corporation is diluted by the substantial stock issuance no matter which form the acquisition takes. Accordingly, some states have regarded as unconscionable the exclusion of shareholders from decisions to acquire another corporation via purchase of stock or assets, and have tailored their statutes accordingly. An example is California's new corporation code applying uniform rules on shareholder voting to mergers, stock acquisitions and acquisitions of assets. CAL. CORP. CODE §§ 181, 1201 (West Supp. 1976) (effective Jan. 1, 1977).

228. ARIZ. REV. STAT. ANN. § 10-017 (Supp. Pamphlet 1975). The provision in section 10-017(A) that normally subscriptions shall be irrevocable for 1 year following their date may be in conflict with the provision in section 10-017(D) that the board of directors may release, settle, or compromise any subscription or claim related thereto. No such conflict exists, however, if the provision in section 10-017(D) is deemed to be incorporated in the "terms of the subscription" referred to in section 10-017(A).

229. *Id.* § 10-019. See Annot 7 *infra.* Consideration may be in the form of cash, tangible or intangible property, or labor and services actually performed for the corporation. ARIZ. REV. STAT. ANN. § 10-019(A) (Supp. Pamphlet 1975). Neither promissory

ganization, or financing expenses from the proceeds of issue,[230] the determination of the amount of stated capital,[231] the form and format of share certificates,[232] the creation and issuance of stock rights and options,[233] the issuance of fractional shares and script,[234] restrictions on the redemption or purchase of redeemable shares,[235] and preemptive rights.[236]

Perhaps one of the greatest potential problems under the Act is posed by the section abolishing Arizona's common law doctrine of preemptive rights.[237] At common law a shareholder had a vested right to subscribe to new shares subsequently issued in proportion to the pro rata shares of outstanding stock of the same class already held by him.[238] Arizona's former debt limitations on corporations[239] may have motivated corporations to authorize stock substantially in excess of any amounts reasonably expected to be issued initially. The ready possibility of new issues from those supplies of stock already authorized made shareholders' preemptive rights crucial in order for them to retain proportionate interests in the voting power, earnings, and assets of the company.[240] Prior to the Act, Arizona lacked any statutory authority regarding preemptive rights,[241] and therefore the ability of a corporation

notes nor services to be performed in the future, however, constitute consideration. *Id.* § 10-019(B). The prohibition against promissory notes probably applies to all forms of promises by the shareholder to pay in the future. A debt instrument accepted as valuable in the general business community, such as one issued by a substantial corporation, on the other hand, should not be included within this prohibition. In the absence of bad faith, the board of directors' judgment as to the adequacy of the consideration is conclusive. *Id.* § 10-019(C).

230. ARIZ. REV. STAT. ANN. § 10-022 (Supp. Pamphlet 1975). Section 10-022 permits organization and underwriting expenses to be paid out of consideration received in payment for shares without rendering the shares not fully paid or assessable. The Bar Committee recognized the possibility that this provision, new to Arizona law, might be interpreted as being in conflict with the proscription of article 14, section 6 of the Arizona constitution (disallowing issuance of stock, except to bona fide subscribers therefor, and declaring all fictitious increase of stock or indebtedness void). Section 10-022 was intended to clarify the meaning of the constitutional provision and to establish that the payment of these kinds of expenses in reasonable amounts was not within the intent of the prohibition. The Arizona blue sky law currently provides for the disclosure in certain instances of the amount of financing expenses, thereby implying that such expenses legally may be paid from the consideration received in exchange for the issuance of shares. *See* ARIZ. REV. STAT. ANN. § 44-1872(1)(c) (Supp. 1975-76); ARIZ. REV. STAT. ANN. § 44-1894(A)(6) (1956).

231. ARIZ. REV. STAT. ANN. § 10-021 (Supp. Pamphlet 1975).

232. *Id.* § 10-023.

233. *Id.* § 10-020. The term "stock rights" as used in this section includes stock warrants. *See* 4 W. FLETCHER, *supra* note 205, § 1370; MODEL ACT § 20, Comment ¶ 12, at 454. See Annots. 9-10 *infra.*

234. ARIZ. REV. STAT. ANN. § 10-024 (Supp. Pamphlet 1975).

235. *Id.* § 10-066. See also Annot. 12 *infra.*

236. *Id.* § 10-026.

237. *Id.*

238. N. LATTIN, *supra* note 213, § 128, at 493-98.

239. ARIZ. REV. STAT. ANN. § 10-173(A) (1956) (limiting corporate indebtedness to two-thirds of its authorized capital stock).

240. *See* N. LATTIN, *supra* note 213, § 128, at 493.

241. Arizona was one of few jurisdictions lacking statutory authority governing preemptive rights. *See* H. HENN, *supra* note 11, § 127, at 215.

to override common law preemptive rights by disavowing them in its articles of incorporation was dubious.[242]

The Act effectively abrogates any notion of common law preemptive rights in Arizona.[243] Only those preemptive rights expressly granted by articles of incorporation existing on the effective date of the Act will remain in effect,[244] in addition to preemptive rights subsequently granted by appropriate provision in the articles of incorporation.[245] Thus, unless the articles of incorporation of existing Arizona corporations already provide for preemptive rights, revision of the articles will be necessary in order to afford such rights to shareholders.

(4) *Other Areas.* Various other subjects statutorily governed for the first time by the Act include bylaws;[246] dividends,[247] distributions from capital surplus,[248] and special provisions relating to surplus and reserves;[249] amendment of articles of incorporation in reorganization proceedings;[250] voluntary dissolution by incorporators;[251] revocation of voluntary dissolution proceedings;[252] certain aspects of the regulation of foreign corporations;[253] financial reports to shareholders;[254] and certain regulatory matters.[255]

III. Matters Requiring Immediate Attention by Existing Corporations

Since many provisions of the Act are applicable on July 1, 1976, to

242. Another unanswered question under former Arizona law was whether a going corporation which previously had not denied preemptive rights could later amend its articles to abolish such rights, and if so, whether unanimous consent of the shareholders was necessary. *See* N. Lattin, *supra* note 213, § 128, at 500.

243. The constitutionality of eliminating prior common law vested rights perhaps may be challenged as a deprivation of property without due process of law. U.S. Const. amend. XIV, § 1; Ariz. Const. art. 2, § 4.

244. Ariz. Rev. Stat. Ann. § 10-026 (Supp. Pamphlet 1975).

245. *Id.* See Model Articles 5.1A-B & Annot. 6 *infra.*

246. *Compare* Ariz. Rev. Stat. Ann. §§ 10-004(A)(12), -027 (Supp. Pamphlet 1975) (vesting in the board of directors power to adopt original or new bylaws and, subject to repeal or change by shareholders, to alter, amend or repeal bylaws) *with* Arizona Southwest Bank v. Odam, 38 Ariz. 394, 397, 300 P. 195, 197 (1931) (board of directors cannot adopt bylaws unless they are authorized to do so by statute, by the articles of incorporation, or by vote of the shareholders), *and* Ariz. Rev. Stat. Ann. § 10-152(7) (1956). For a criticism of the power granted to the directors under new section 10-027, see Note, *Corporations—A Survey of the Pending West Virginia Corporation Act*, 77 W. Va. L. Rev. 50, 62 (1974).

The power to alter, amend, or repeal the bylaws or to adopt new bylaws may be reserved to the shareholders by the articles of incorporation. Ariz. Rev. Stat. Ann. § 10-027 (Supp. Pamphlet 1975). See Model Article 13.1 & Annot. 34 *infra.*

247. Ariz. Rev. Stat. Ann. § 10-045 (Supp. Pamphlet 1975). See text & note 267 *infra.* See also Annot. 32 *infra.*

248. Ariz. Rev. Stat. Ann. § 10-046 (Supp. Pamphlet 1975). See Annot. 27 *infra.*

249. Ariz. Rev. Stat. Ann. § 10-070 (Supp. Pamphlet 1975).

250. *Id.* § 10-065.

251. *Id.* § 10-082.

252. *Id.* §§ 10-088 to -091.

253. *Id.* § 10-117 (merger); *id.* § 10-118 (change of name or purpose); *id.* § 10-123 (applicability of Act to foreign corporations previously authorized to transact business).

254. *Id.* § 10-127. See text & note 263 *infra.*

255. Ariz. Rev. Stat. Ann. §§ 10-137 to -138 (Supp. Pamphlet 1975) (interroga-

all corporations organized under any general law of the State of Arizona,[256] certain of its provisions require immediate attention by such corporations and their legal counsel.

A. *Notice of Shareholders' Meetings*

One of the immediate steps necessary after the effective date of the Act is to ensure full compliance with the provisions for notice of shareholders' meetings. The Act requires written notice of every shareholders' meeting—annual, regular, and special[257]—and prescribes what the notice must contain, when and by whom the notice is to be given to the shareholders, and when a notice by mail is regarded as delivered.[258] The requirement of written notice for all shareholders' meetings changes the existing common law rule followed in Arizona that no notice was required if the articles of incorporation or bylaws fix the time and place of the annual meeting.[259]

B. *Maintenance of Corporate Books and Records*

Another provision of the Act immediately applicable to existing corporations which may be at variance with past conduct regards the maintenance of corporate books, records, and minutes.[260] For the first time, Arizona corporations are required to keep correct and complete books, records of account, and minutes of shareholders', directors', and committee meetings.[261] Additional duties are imposed upon the officer

tories by commission); *id.* § 10-139 (powers of commission); *id.* § 10-141 (certified copies as evidence); *id.* § 10-142 (forms).

256. See text accompanying notes 23-35 *supra.*

257. ARIZ. REV. STAT. ANN. § 10-029 (Supp. Pamphlet 1975). Section 10-144 provides for the waiver of the required written notice of shareholders meetings. Such waiver must be made either in writing or by operation of law based on the shareholder's attendance at the meeting for any purpose other than objecting to the transaction of business because the meeting was not called or convened lawfully. *Id.* Written waivers may be signed either before or after the meeting. *Id.*

258. ARIZ. REV. STAT. ANN. § 10-029 (Supp. Pamphlet 1975).

259. *See* N. LATTIN, *supra* note 213, § 89, at 360. *Compare* ARIZ. REV. STAT. ANN. § 10-029 (Supp. Pamphlet 1975) *with* Citrus Grower's Dev. Ass'n v. Salt River Water Users' Ass'n, 34 Ariz. 105, 268 P. 773 (1928) (holding that, in the absence of provision in the articles of incorporation or bylaws, notices of special shareholders' meetings need be in no particular form). See discussion note 214 *supra.* Section 10-029 should be read in conjunction with sections 10-144 (permitting any shareholder to waive notice either before or after a meeting), 10-145 (permitting all of the shareholders to take action upon written consent without a meeting), 10-073 (requiring a minimum of 20 days' notice for shareholder action on a plan of merger or consolidation), and 10-030 (permitting the determination of shareholders entitled to vote at any meeting to apply to any adjournment of the meeting).

260. ARIZ. REV. STAT. ANN. § 10-052 (Supp. Pamphlet 1975).

261. *Id.* Arizona corporate counsel following the common practice of drafting minutes and maintaining corporate minute books should be mindful of the potential exposure to liability for failure to comply with the new statutory standard. While civil and criminal sanctions imposed by sections 10-135 and 10-136 appear to be inapplicable to the simple failure to maintain complete books and records, the officers and directors of Arizona corporations could find themselves subject to common law liability for mismanagement or even to antitrust or securities law, or similar statutory liabilities arising from or attributable to such failure.

or agent with respect to the maintenance, arrangement, and availability for inspection of the corporation's voting record.[262] The Act also requires that every Arizona corporation with more than 10 shareholders supply each shareholder with a financial report, including the fiscal yearend balance sheet and statement of income, within 4 months after the end of the corporation's fiscal year.[263] In addition to the mandatory annual financial report, corporations must mail, not deliver, their most recent financial statements showing in "reasonable detail" their assets and liabilities and the results of their operations to requesting shareholders or holders of a beneficial interest in a voting trust.[264]

C. *Declaration and Payment of Dividends*

Existing corporations wishing to declare dividends should become familiar with the Act's altered treatment of this subject.[265] Ordinary dividends in cash or property may be paid from unrestricted and unreserved earned surplus or from the net earnings of the two immediately preceding fiscal years treated as a single accounting period.[266] Share dividends may be declared either from earned or capital surplus.[267]

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262. *Id.* § 10-031. In following the common practice of assuming control of the stock transfer books of corporate clients, Arizona corporate counsel who are also officers or agents for close corporations should be mindful of the potential exposure to liability for ministerial acts, imposed by section 10-031(C). The establishment by counsel of a corporation to act as transfer agent for his corporate clients would be a possible solution to this problem.

263. *Id.* § 10-127. No provision is made in the Act for waiver by the shareholders of this requirement. Although the financial report is not required to be certified, the penalties imposed upon officers and directors by sections 10-135 and 10-136 and the possible analogy offered by section 10-048(C) (director's reliance upon corporate financial statements) indicate the advisability of careful preparation of such reports.

264. *Id.* § 10-052(E).

265. *Id.* § 10-045. Attention must be given to the new statutory definitions of "insolvent," *id.* § 10-002(12) and "stated capital." *Id.* § 10-002(18). Reference also should be made to section 10-021, describing how stated capital is to be determined in certain circumstances; to sections 10-067 to -069 inclusive, describing events resulting in the reduction of stated capital; and to the definitions of "surplus," *id.* § 10-002(20), "earned surplus," *id.* § 10-002(9), "capital surplus," *id.* § 10-002(6), and "treasury shares." *Id.* § 10-002(21). All profits from the enterprise and all gains and losses, whether from operations or from transactions involving capital assets, are treated as earned surplus under the Act, *id.* § 10-002(9), and all other profits, gains, and losses constitute capital surplus. *Id.* § 10-002(6). Revaluation of assets and the utilization of values not yet realized are not subject to express provision in the Act.

266. *Id.* § 10-045(A)(1). Note should be taken of section 10-070(C) authorizing the directors to charge off any deficit, including one resulting from unfavorable operations, against capital surplus. The effect of such a charge-off would be to make available for dividends future earnings which otherwise would have been absorbed by the deficit. See also Model Article 9 & Annot. 27 *infra.*

267. ARIZ. REV. STAT. ANN. § 10-045(A) (Supp. Pamphlet 1975). If previously unissued shares are distributed as a dividend, an appropriate amount of surplus must be transferred to stated capital. *Id.* § 10-045(A)(4). In the case of par value shares, the amount transferred would be the aggregate par value of the dividend shares. *Id.* § 10-045(A)(4)(a). In the case of no par shares, the amount transferred is determined by the directors and reported to the shareholders. *Id.* § 10-045(A)(4)(b). Treasury shares also may be distributed as a dividend. *Id.* § 10-045(A)(3).

Special provision is made for corporations engaged in the exploitation of wasting assets. *Id.* § 10-045(A)(2). See Model Article 9.1 & Annot. 28 *infra.* The provision

D. *Provisions in the Articles of Incorporation or Bylaws Requiring Attention by Existing Corporations*

Certain portions of the Act provide for the Act's applicability unless another alternative is stated in the corporation's articles of incorporation or bylaws.[268] Provisions of this type require existing corporations to determine whether their present articles of incorporation and bylaws empower them to act in the way to which they have become accustomed. If the articles and bylaws currently do not adequately authorize customary or desired practice, the corporate shareholders or directors may wish to amend the appropriate corporate documents to expressly grant such authority. The following checklist is representative of areas requiring consideration.

(1) *Corporate Powers.* If existing corporations wish to limit the general powers set forth in the Act,[269] they must do so in their articles of incorporation.[270]

(2) *Matters Relating to Capital.* The following actions require express provision in the articles of incorporation of existing corporations:

(a) Reserving to shareholders the right to fix the issue price of the corporation's shares.[271]

(b) Regulating the issuance of stock rights and options, setting forth terms for their exercise, or removing from the shareholders the right of approval or ratification of the issuance of stock rights or options to directors, officers, or employees of the corporation or to any of its affiliates.[272]

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of section 45(b) of the Model Act that "dividends may be declared and paid in cash out of the depletion reserves" has been altered in the Act in such a way that the meaning of the provision is not readily apparent. *See* ARIZ. REV. STAT. ANN. § 10-045(A)(2) (Supp. Pamphlet 1975). Pending House Bill 2364 would clarify the provision by providing that these corporations may establish depletion reserves with respect to wasting assets and may declare and pay cash dividends out of such reserves if the dividends are identified and the amounts being paid from such reserves are disclosed at the time of payment to the shareholders receiving the dividends. H. 2364, 32d Ariz. Legis., 2d Reg. Sess. § 18 (1976).

268. See text & notes 269-92 *infra.*

269. ARIZ. REV. STAT. ANN. § 10-004(A) (Supp. Pamphlet 1975). See text & notes 78-92 *supra.*

270. ARIZ. REV. STAT. ANN. § 10-004(B) (Supp. Pamphlet 1975). See Model Article 4 & Annot. 4 *infra.*

271. ARIZ. REV. STAT. ANN. §§ 10-018(A)-(C) (Supp. Pamphlet 1975). See Model Articles 5.2A-C & Annot. 7 *infra.* In the absence of such a provision, the consideration is fixed by the board of directors, always subject to the constitutional limitation, however, that in the case of par value shares, the issue price so fixed not be less than the par value. ARIZ. CONST. art. 14, § 6; ARIZ. REV. STAT. ANN. § 10-018(A) (Supp. Pamphlet 1975). If the right is reserved to the shareholders, the determination may be made by a majority of the outstanding shares entitled to vote, unless a greater vote is required by the articles of incorporation. *Id.* § 10-018(D). See Model Article 5.3 & Annot. 8 *infra.*

272. ARIZ. REV. STAT. ANN. § 10-020 (Supp. Pamphlet 1975). See Model Articles 5.4-.5 & Annots. 9-10 *infra.* For purposes of the Act, the term "affiliate" includes

(c) Obligating a holder or subscriber of its shares to assume liability over and above the obligation to pay the full issue price.[273]

(d) Granting preemptive rights, not already expressly in existence on July 1, 1976, to acquire unissued or treasury shares of the corporation, securities convertible into such shares or subscription rights to such shares.[274]

(e) Imposing restrictions on the payment of dividends in addition to those provided by the Act, or providing for the payment of stock dividends between classes of stock.[275]

(f) Making distributions from capital surplus without express authorization of the holders of a majority of all the outstanding shares.[276]

(g) Restricting the application of all or any part of capital surplus to the reduction or elimination of any deficit.[277]

If existing corporations do not wish redeemed shares to be restored to the status of authorized but unissued shares, this also must be provided for in the articles of incorporation.[278] If such provision is made to disallow reissuance of the redeemed shares, the number of such shares which the corporation is authorized to issue must be reduced by the number of shares redeemed.[279]

(3) *Matters Relating to Shareholders.* The following actions require appropriate provision in the articles of incorporation or, where noted, the bylaws of existing corporations:

(a) Empowering persons other than the board of directors or the holders of not fewer than one-tenth of all the voting shares to call a special meeting of the shareholders.[280]

(b) Fixing a quorum requirement for shareholders' meetings equal to or greater than one-third but other than a majority of the shares entitled to vote at such meetings,[281] or providing that a greater than majority vote of the shares represented at the meeting and entitled to vote is necessary to constitute the act of the shareholders.[282]

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persons "controlling, controlled by or under common control with" a corporation. ARIZ. REV. STAT. ANN. § 10-002(2) (Supp. Pamphlet 1975).

273. ARIZ. REV. STAT. ANN. § 10-025(A) (Supp. Pamphlet 1975). See Model Article 5.6 & Annot. 11 *infra*.

274. ARIZ. REV. STAT. ANN. § 10-026 (Supp. Pamphlet 1975). See Model Articles 5.1A-B & Annot. 6 *infra*; text & notes 237-45 *supra*.

275. ARIZ. REV. STAT. ANN. § 10-045(A) (Supp. Pamphlet 1975).

276. *Id.* § 10-046(A)(2). See Model Article 9 & Annot. 27 *infra*.

277. ARIZ. REV. STAT. ANN. § 10-070(C) (Supp. Pamphlet 1975). See Model Article 9.2 & Annot. 29 *infra*.

278. ARIZ. REV. STAT. ANN. § 10-067(A) (Supp. Pamphlet 1975). See Model Article 5.7 & Annot. 12 *infra*.

279. ARIZ. REV. STAT. ANN. § 10-067(A) (Supp. Pamphlet 1975).

280. *Id.* § 10-028(C). This authority may be derived from either the articles or the bylaws.

281. *Id.* § 10-032. See Model Article 13 & Annot. 33 *infra*.

282. ARIZ. REV. STAT. ANN. §§ 10-032, -143 (Supp. Pamphlet 1975). The necessary

(c) Fixing the number of votes to which each share is entitled at some number other than one.[283]

(d) Reserving control over the management of the business and affairs of a corporation to the shareholders,[284] or reserving to the shareholders the power to alter, amend, or repeal the original bylaws or to adopt new bylaws.[285]

(e) Requiring stockholder authorization of mergers under certain conditions,[286] or protecting dissenting shareholders' rights in mergers or consolidations in certain circumstances.[287]

(4) *Matters Relating to Directors.* The following actions similarly require appropriate provision in the articles of incorporation, or, where noted, the bylaws of existing corporations:

(a) Fixing a quorum requirement for directors' meetings at other than a majority of the number of directors then serving,[288] or providing that a greater than majority vote of the directors present at a meeting is necessary to constitute the act of the board.[289]

(b) Denying directors the power to act by unanimous consent without a meeting.[290]

(c) Providing qualifications for directors or restricting the directors' authority to fix their compensation for services in any capacity.[291]

(d) Establishing an alternative to the Act's procedure for filling vacancies on the board of directors.[292]

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provision may be contained in the bylaws as well as the articles. The Act requires the affirmative vote of a majority of the outstanding shares entitled to vote, rather than those represented at the meeting, to amend the articles of incorporation, *id.* § 10-059, to merge or consolidate, *id.* § 10-073, to sell or mortgage assets not in the regular course of business, *id.* § 10-079, to dissolve voluntarily, *id.* § 10-084, and to revoke voluntary dissolution proceedings. *Id.* § 10-089. See Model Articles 13.2-.3 & Annot. 35 *infra.*

283. ARIZ. REV. STAT. ANN. § 10-033(A) (Supp. Pamphlet 1975).

284. *Id.* § 10-035. See Model Articles 7.2A-B & Annot. 18 *infra.*

285. ARIZ. REV. STAT. ANN. § 10-027 (Supp. Pamphlet 1975). See Model Article 13.1 & Annot. 34 *infra.*

286. ARIZ. REV. STAT. ANN. § 10-073(C) (Supp. Pamphlet 1975).

287. *Id.* § 10-080(C). See Model Article 13.4 & Annot. 36 *infra.*

288. ARIZ. REV. STAT. ANN. § 10-040 (Supp. Pamphlet 1975). If a number greater than a majority is desired, this increase may be fixed in either the bylaws or the articles. *Id.* Irrespective of provisions in the articles of incorporation or bylaws, a quorum cannot be fixed at less than one-third of the directors then serving nor less than two directors, except in the case of a 1-director board. *Id.* See Annot. 22 *infra.*

289. ARIZ. REV. STAT. ANN. § 10-040 (Supp. Pamphlet 1975). The necessary provision may be contained in either the bylaws or the articles. See Model Article 7.7 & Annot. 23 *infra.*

290. ARIZ. REV. STAT. ANN. § 10-044 (Supp. Pamphlet 1975). See Model Article 7.9 & Annot. 25 *infra.* The necessary provision may be contained in either the articles or bylaws.

291. ARIZ. REV. STAT. ANN. § 10-035 (Supp. Pamphlet 1975). See Model Article 7.3 & Annot. 19 *infra* (director qualifications); Model Article 7.4 & Annot. 20 *infra* (compensation authority). The necessary provisions may be contained in either the articles or bylaws.

292. ARIZ. REV. STAT. ANN. § 10-038 (Supp. Pamphlet 1975). See Model Article 7.5 & Annot. 21 *infra.*

IV. CONCLUSION

The new Arizona Business Corporation Act represents a much needed change in Arizona law. The Act largely eliminates the vagaries and deficiencies of former law. Its effect will be felt by all corporations doing business in this state. This Article was not intended to analytically survey the new law in depth, but rather to introduce its major aspects for the purpose of aiding those responsible for guiding both existing and future Arizona corporations in planning and conducting their affairs. As with all new legislation, some problem areas remain under the Act. Nevertheless, the Act's clarification of the law governing corporations in this state will be of immense benefit to the public, business interests, and attorneys in Arizona.

V. APPENDIX

MODEL ARTICLES OF INCORPORATION WITH ANNOTATIONS

The following is a model set of articles of incorporation for an Arizona corporation formed under the new law, with alternative provisions containing various options granted by the Act. In no case must all options be used. In fact, often none will be necessary, since the new law explicitly sets forth rules governing corporate transactions where no contrary provision is made in the articles of incorporation. Because the law requires publication of articles of incorporation, ARIZ REV. STAT. ANN. § 10-055 (C) (Supp. Pamphlet 1975), it is to the advantage of the incorporators that the articles be brief; however, the cost of publication must be balanced against the individual corporation's need for particular provisions.

The model articles that follow are numbered consecutively. The numbers in brackets refer to the annotations following the model articles. The unbracketed numbers represent the numbering system suggested for use in the actual articles filed with the Arizona Corporation Commission. Where these unbracketed numbers include letters, they are alternative variations of the basic provision, only one of which should be used in any set of articles. Of course, all paragraph and subparagraph numbers actually used should be consecutive.

The Act sets forth the minimum information that must be contained in articles of incorporation. ARIZ REV. STAT. ANN. § 10-054 (Supp. Pamphlet 1975). This information is set forth in model articles 1 (name), 2 (purpose), 3 (initial business), 5 (authorized capital), 6 (statutory agent), 7 (board of directors), and 8 (incorporators). A corporation validly may have articles of incorporation with only these provisions. Section 10-054 embodies presumptions in favor of perpetual existence and against preemptive rights; no provisions in these areas are necessary, therefore, unless these presumptions are to be negated. See Model Articles 5.1, 14.

Certain additional models are suggested for inclusion in all sets of articles of incorporation: model articles 9 (permitting distributions from capital surplus, dividends being restricted to earned surplus); 10 (providing for mandatory indemnification); and 11 (allowing repurchase of shares from capital surplus as well as earned surplus). Other model articles also are strongly recommended, but only in specific situations. If there is more than one class of stock, model article 12, permitting stock dividends in one class to be paid to the holders of another, is recommended. A corporation engaged in the exploitation of

natural resources should utilize model article 9.1, permitting cash distributions from depletion reserves. Other recommendations in regard to the use of specific model articles are contained in the appropriate annotations.

The models deal with all of the alternatives provided in the Act, but do not set forth all possible alternatives which may be utilized under the Act; the various ways of implementing the many opportunities provided by the new Act's flexibility are almost infinite. For example, in addition to the specific authority granted by the Act, section 10-054 (A)(12) provides that the articles may contain "any other provision, not inconsistent with law, which the incorporators elect to set forth."

The Model Articles

[1] 1. NAME. THE NAME OF THE CORPORATION IS [here insert the name, for example, SAMPLE CORPORATION].

Annotation 1. The name must contain one of the words "bank," "association," "corporation," "company," "incorporated," or "limited" or an abbreviation of one of these words. ARIZ. REV. STAT. ANN. § 10-008(A)(1) (Supp. Pamphlet 1975). The name cannot contain any word or phrase likely to mislead the public. *Id.* § 10-008(A)(2). The statute requires that the name not contain any word or phrase which indicates or implies that it is organized for any purpose other than any specific purpose contained in its articles of incorporation. *Id.* See note 72 *supra*; Annot. 2 *infra*. Therefore, if the only purpose stated in the articles of incorporation is the transaction of any and all lawful business, the corporate name must be general in nature and cannot refer to any specific business purpose. If it is desired that the name indicate a specific organizational purpose, that purpose must be so stated in the articles.

The corporate name cannot be the same as or deceptively similar to the name of any existing domestic corporation or any foreign corporation qualified in Arizona, a name reserved for use as a corporate name by someone else, or a trade name registered with the secretary of state. ARIZ REV. STAT. ANN. § 10-008(A)(3) (Supp. Pamphlet 1975); *see* text & notes 93-96 *supra*. The requirement of nonconflict with registered trade names may be eliminated by proposed legislation. *See* discussion note 95 *supra*.

A corporate name may be reserved for 120 days prior to use by making application with the Arizona Corporation Commission. ARIZ. REV. STAT. ANN. § 10-009 (Supp. Pamphlet 1975). Advance reservation of trade names with the secretary of state, however, is not possible. Moreover, due to lack of staff, the filing of trade name registrations

is not current, and it is impossible to determine accurately whether a specific name has been recently registered with the secretary. Hopefully, this problem will be resolved before the new law becomes effective.

[2] 2A. PURPOSE. THE PURPOSE FOR WHICH THIS CORPORATION IS ORGANIZED IS THE TRANSACTION OF ANY OR ALL LAWFUL BUSINESS FOR WHICH CORPORATIONS MAY BE INCORPORATED UNDER THE LAWS OF THE STATE OF ARIZONA, AS THEY MAY BE AMENDED FROM TIME TO TIME.

2B. PURPOSE. THE PURPOSE FOR WHICH THIS CORPORATION IS ORGANIZED IS THE TRANSACTION OF ANY OR ALL LAWFUL BUSINESS FOR WHICH CORPORATIONS MAY BE INCORPORATED UNDER THE LAWS OF THE STATE OF ARIZONA, AS THEY MAY BE AMENDED FROM TIME TO TIME, AND SPECIFICALLY BUT NOT IN LIMITATION THEREOF, THE PURPOSE OF [here insert the purpose indicated or implied by the corporate name, for example, BUYING, SELLING, DEVELOPING, AND DEALING WITH REAL PROPERTY].

2C. PURPOSE. THE PURPOSE FOR WHICH THIS CORPORATION IS ORGANIZED IS [here insert all specific purposes of the corporation in full and complete detail, for example, (2C continued) 2.1. THE REAL PROPERTY BUSINESS. THE BUSINESS OF BUYING, OWNING, HOLDING, OPERATING, LEASING (BOTH AS LESSOR AND LESSEE), MANAGING, IMPROVING, DEVELOPING, SUBDIVIDING, LAYING OUT, PLATTING, SELLING, AND OTHERWISE DEALING IN AND WITH (ALL OF THE FOREGOING AS CONTRACTOR, AS SUBCONTRACTOR, AS SPECIALTY CONTRACTOR, AS A SPECULATIVE BUILDER FOR RESALE, IN COMBINATION OR COOPERATION WITH OTHERS, AND IN ANY OTHER CAPACITY AND MANNER WHATSOEVER) REAL PROPERTY, BOTH IMPROVED AND UNIMPROVED, OF EVERY KIND AND CHARACTER, INCLUDING EVERY CHARACTER OF INTEREST AND RIGHT THEREIN WHETHER OR NOT IN POSSESSION].

[(2C continued) 2.2. RELATED BUSINESSES. THE BUSINESS OF ENGAGING IN ANY AND ALL OTHER BUSINESSES OF ANY TYPE WHATSOEVER GROWING OUT OF, RELATED TO, OR IN ANY MANNER WHATSOEVER IN CONNECTION WITH ANY OF THE ITEMS, BUSINESSES, RELATIONSHIPS, PURPOSES, AND POWERS DESCRIBED IN THESE ARTICLES. NO ENUMERATION HEREIN SET FORTH SHALL IN ANY MANNER BE

DEEMED TO BE EXCLUSIVE OF OBJECTS OR PURPOSES NOT ENUMERATED, BUT ON THE CONTRARY SUCH ENUMERATIONS SHALL BE CONSTRUED AS INCLUDING ALL OTHER AND FURTHER OBJECTS AND PURPOSES OF THE SAME OR SIMILAR TYPE OR CHARACTER, REGARDLESS OF HOW THIN, VAGUE, OR INDEFINITE THE RELATIONSHIP OR CONNECTION MAY BE].

Annotation 2. Although ARIZ. REV. STAT. ANN. § 10-054(A)(3) (Supp. Pamphlet 1975) requires the articles of incorporation to state the purpose or purposes for which the corporation is formed, it permits the purpose to be stated in the broad language set forth in model article 2A. See text & notes 70-72 *supra.*

As a result, model articles 2A and 2B are sufficient to authorize corporations to do anything legally permissible for corporations without more specific detail being placed in the articles of incorporation. If the general phrasing permitted by section 10-054(A)(3) is not contained in the articles, the Arizona constitution, article 14, section 4, requires that all purposes which the corporation will engage in be specifically set out as in model article 2C. Broad general language will not be sufficient; rather, particularity, similar to that required for Arizona corporations prior to July 1, 1976, will be necessary. See text & notes 74-89 *supra.*

Model articles 2A and 2B refer to "the laws of the state of Arizona," rather than merely to the Arizona Business Corporation Act. Although the Act adopted by the legislature and signed by the governor contained the title "Arizona Business Corporation Act," ch. 69, § 2, [1975] Ariz. Sess. Laws 1st Reg. Sess. 241, that entire section was deleted from the final version of the Act by the Office of Legislative Counsel. Therefore, no legal document can safely refer solely to the short title of the Act so long as section 10-001 is not effective.

[3] 3. INITIAL BUSINESS. THE CORPORATION INITIALLY INTENDS TO CONDUCT THE BUSINESS OF [here insert a brief statement of the character of the business to be initially conducted, for example, THE BUSINESS OF BUYING, SELLING, AND DEVELOPING REAL PROPERTY].

Annotation 3. The Act requires that the articles of incorporation provide a brief statement of the character of business which the corporation initially intends to conduct in this state. ARIZ. REV. STAT. ANN. § 10-054(A)(4) (Supp. Pamphlet 1975). See text & note 73 *supra.*

If model article 2B is chosen in order to justify a reference to a

specific purpose in the corporate name, that specific purpose will need to be restated in article 3, notwithstanding the previous use of identical language in article 2.

[4] 4. LIMITATION OF POWERS. THIS CORPORATION SHALL HAVE NO POWER OR AUTHORITY TO [here insert specific limitations to be placed on the corporation, for example, BUY, SELL, LEASE, OWN, DEVELOP, OR OTHERWISE ACQUIRE AND DEAL WITH REAL PROPERTY LOCATED OUTSIDE MARICOPA COUNTY, ARIZONA].

Annotation 4. The Act grants to all corporations a wide range of powers. ARIZ. REV. STAT. ANN. § 10-004 (Supp. Pamphlet 1975). See text & notes 78-81 *supra.* Nonetheless, a corporation may through its articles of incorporation deny or limit any of the powers which it would otherwise possess. ARIZ. REV. STAT. ANN. § 10-004(B) (Supp. Pamphlet 1975). See discussion note 72 *supra.* Such a provision might be desirable, for instance, where the corporation is a regulated industry prevented by law from entering into certain kinds of businesses. The articles of incorporation may incorporate such a limitation by providing that the corporation has only certain specified powers or that it has only the powers necessary to conduct a particular business or purpose. This type of provision, however, invites later disputes over the meaning of the restriction. It is therefore more advisable to specifically denote those powers which the corporation does not have rather than to attempt an exhaustive statement of the powers it has.

[5] 5A. [One Class] AUTHORIZED CAPITAL. THE CORPORATION SHALL HAVE AUTHORITY TO ISSUE [here insert the number, for example, ONE THOUSAND (1000)] SHARES OF COMMON STOCK, [here insert the par value, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE, or, WITHOUT PAR VALUE].

5B. [Two Classes—One Class Nonvoting] AUTHORIZED CAPITAL. THE CORPORATION SHALL HAVE AUTHORITY TO ISSUE A TOTAL OF [here insert the number, for example, TWO THOUSAND (2000)] SHARES OF STOCK OF WHICH [here insert the number, for example, ONE THOUSAND (1000)] SHARES SHALL BE [here insert the description, for example, CLASS A COMMON] STOCK, [here insert par value information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE, or, WITHOUT PAR VALUE] AND [here insert the number, for example, ONE THOUSAND (1000)] SHARES SHALL BE [here insert the description, for example, CLASS B COMMON] STOCK, [here insert par value

information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE, or, WITHOUT PAR VALUE]. THE [here insert description, for example, CLASS A COMMON] STOCK AND THE [here insert description, for example, CLASS B COMMON] STOCK SHALL BE IDENTICAL IN ALL RESPECTS EXCEPT THAT THE HOLDERS OF [here insert description of nonvoting stock, for example, CLASS B COMMON] STOCK SHALL HAVE NO VOTING POWER FOR ANY PURPOSE AND SHALL NOT BE ENTITLED TO NOTICE OF ANY MEETING OF SHAREHOLDERS. THE HOLDERS OF [here insert description of voting stock, for example, CLASS A COMMON] STOCK SHALL HAVE ONE (1) VOTE PER SHARE ON ANY MATTER SUBMITTED TO A VOTE OF OR FOR CONSENT OF SHAREHOLDERS.

5C. [Two Classes—Common and Preferred] AUTHORIZED CAPITAL. THE AUTHORIZED CAPITAL OF THE CORPORATION SHALL BE DIVIDED INTO [here insert number, for example, THREE MILLION (3,000,000)] SHARES OF COMMON STOCK, [here insert par value information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE, or, WITHOUT PAR VALUE] AND [here insert number, for example, TEN THOUSAND (10,000)] SHARES OF PREFERRED STOCK, [here insert par value information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE, or, WITHOUT PAR VALUE]. EACH SHARE OF PREFERRED STOCK SHALL BE ENTITLED TO RECEIVE, WHEN AND AS DECLARED BY THE BOARD OF DIRECTORS OF THIS CORPORATION, DIVIDENDS AT THE RATE OF [here insert dividend rate, for example, SIX PERCENT (6%) OF ITS PAR VALUE, or, SIX DOLLARS ($6)] PER ANNUM, BEFORE ANY DIVIDENDS MAY BE PAID ON ANY COMMON STOCK. [Here insert whether or not cumulative, for example, DIVIDENDS ON PREFERRED STOCK SHALL NOT BE CUMULATIVE.] AFTER SUCH PREFERRED DIVIDENDS HAVE BEEN PAID, THE PREFERRED STOCK SHALL BE ENTITLED TO PARTICIPATE EQUALLY IN ANY FURTHER DIVIDENDS WITH THE COMMON STOCK. UPON ANY LIQUIDATION OR DISTRIBUTION OF CAPITAL ASSETS, THE HOLDER OF EACH SHARE OF PREFERRED STOCK SHALL BE ENTITLED TO RECEIVE THE PAR VALUE OF SUCH SHARE BEFORE ANY DISTRIBUTION SHALL BE MADE TO THE COMMON STOCK. FOLLOWING SUCH PREFERENTIAL DISTRIBUTION, THE COMMON STOCK SHALL BE ENTITLED TO THE REMAINDER OF THE ASSETS DISTRIBUTED IN EXCESS OF THE PAR VALUE OF THE PREFERRED STOCK.

EXCEPT AS OTHERWISE PROVIDED BY LAW, THE HOLDERS OF PREFERRED SHARES SHALL NOT BE ENTITLED TO VOTE AT ANY MEETING OF THE SHAREHOLDERS FOR THE ELECTION OF DIRECTORS OR FOR ANY OTHER PURPOSE, OR OTHERWISE TO PARTICIPATE IN ANY ACTION TAKEN BY THE CORPORATION OR THE SHAREHOLDERS THEREOF, OR TO RECEIVE NOTICE OF ANY MEETING OF SHAREHOLDERS.

5D. [Two Classes—One Redeemable and Convertible] AUTHORIZED CAPITAL. THE TOTAL NUMBER OF SHARES OF ALL CLASSES WHICH THE CORPORATION SHALL HAVE AUTHORITY TO ISSUE SHALL BE [here insert total number, for example, FIFTY-TWO THOUSAND (52,000)] SHARES CONSISTING OF [here insert number, for example, TWO THOUSAND (2000)] SHARES OF [here insert title of stock, for example, CONVERTIBLE REDEEMABLE PREFERRED] STOCK, [here insert par value information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE, or, WITHOUT PAR VALUE] AND [here insert number, for example, FIFTY THOUSAND (50,000)] SHARES OF COMMON STOCK, [here insert par value information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE]. EACH SHARE OF STOCK, REGARDLESS OF CLASS, SHALL BE ENTITLED TO ONE (1) VOTE PER SHARE.

AT ANY TIME SUBSEQUENT TO [here insert date, for example, THREE (3) YEARS] FROM THE DATE IT IS ISSUED, AFTER [here insert notice requirement, for example, THIRTY (30) DAYS' WRITTEN NOTICE] TO THE REGISTERED OWNER, EACH [here insert name of redeemable class, for example, CONVERTIBLE REDEEMABLE PREFERRED] SHARE SHALL BE REDEEMABLE BY THE CORPORATION [here insert terms of redemption, for example, BY THE PAYMENT OF TWO DOLLARS ($2) PER SHARE].

AT ANY TIME [here insert date convertibility begins, for example, AFTER THE FIFTH ANNIVERSARY OF ITS DATE OF ISSUE], EACH [here insert name of convertible class, for example, CONVERTIBLE REDEEMABLE PREFERRED] SHARE SHALL BE CONVERTIBLE, AT THE OPTION OF THE HOLDER, [here insert terms of conversion, for example, INTO TEN (10) SHARES OF COMMON STOCK].

EACH SHARE OF PREFERRED STOCK SHALL BE ENTITLED TO RECEIVE, WHEN AND AS DECLARED BY THE BOARD OF DIRECTORS OF THIS CORPORATION, DIVIDENDS AT THE RATE OF [here insert dividend rate,

for example, SIX PERCENT (6%) OF ITS PAR VALUE, or, SIX DOLLARS ($6)] PER ANNUM, BEFORE ANY DIVIDENDS MAY BE PAID ON ANY COMMON STOCK. DIVIDENDS ON PREFERRED STOCK SHALL [here insert whether or not cumulative, for example, NOT BE CUMULATIVE]. AFTER SUCH PREFERRED DIVIDENDS HAVE BEEN PAID, THE PREFERRED STOCK SHALL BE ENTITLED TO PARTICIPATE EQUALLY IN ANY FURTHER DIVIDENDS WITH THE COMMON STOCK. UPON ANY LIQUIDATION OR DISTRIBUTION OF CAPITAL ASSETS, THE HOLDER OF EACH SHARE OF PREFERRED STOCK SHALL BE ENTITLED TO RECEIVE THE PAR VALUE OF SUCH SHARE BEFORE ANY DISTRIBUTION SHALL BE MADE TO THE COMMON STOCK. FOLLOWING SUCH PREFERENTIAL DISTRIBUTION, THE COMMON STOCK SHALL BE ENTITLED TO THE REMAINDER OF THE ASSETS DISTRIBUTED IN EXCESS OF THE PAR VALUE OF THE PREFERRED STOCK.

5E. [Two Classes—One Serial Preferred] AUTHORIZED CAPITAL. THE AUTHORIZED CAPITAL STOCK OF THIS CORPORATION IS TO BE [here insert total number, for example, FOUR MILLION, FIVE HUNDRED THOUSAND (4,500,000)] SHARES DIVIDED INTO [here insert number, for example, THREE MILLION (3,000,000)] SHARES OF COMMON STOCK, [here insert par value information, for example, PAR VALUE ONE DOLLAR ($1) PER SHARE], AND [here insert number, for example, ONE MILLION, FIVE HUNDRED THOUSAND (1,500,000)] SHARES OF SERIAL PREFERRED STOCK, NO PAR VALUE. EACH ISSUED AND OUTSTANDING SHARE OF COMMON STOCK WILL ENTITLE THE HOLDER THEREOF TO ONE (1) VOTE ON ANY MATTER SUBMITTED TO A VOTE OF OR FOR CONSENT OF SHAREHOLDERS. ISSUED AND OUTSTANDING SHARES OF SERIAL PREFERRED STOCK WILL ENTITLE THE HOLDERS THEREOF ONLY TO THOSE VOTES, IF ANY, WHICH MAY EXPRESSLY BE FIXED AS HEREINAFTER PROVIDED FOR THE RESPECTIVE SERIES THEREOF AND TO VOTING RIGHTS ON CERTAIN MATTERS, AND IN CERTAIN CIRCUMSTANCES, AS SET FORTH IN THIS ARTICLE.

SUBJECT TO THE TERMS AND PROVISIONS OF THIS ARTICLE, THE BOARD OF DIRECTORS IS AUTHORIZED TO PROVIDE FROM TIME TO TIME FOR THE ISSUANCE OF SHARES OF SERIAL PREFERRED STOCK IN SERIES AND TO FIX FROM TIME TO TIME BEFORE ISSU-

ANCE THE DESIGNATION, PREFERENCES, PRIVILEGES, AND VOTING POWERS OF THE SHARES OF EACH SERIES OF SERIAL PREFERRED STOCK AND THE RESTRICTIONS OR QUALIFICATIONS THEREOF, INCLUDING, WITHOUT LIMITING THE GENERALITY OF THE FOREGOING, THE FOLLOWING:

A. THE SERIAL DESIGNATION AND AUTHORIZED NUMBER OF SHARES;

B. THE DIVIDEND RATE, THE DATE OR DATES ON WHICH SUCH DIVIDENDS WILL BE PAYABLE, AND THE EXTENT TO WHICH SUCH DIVIDENDS MAY BE CUMULATIVE;

C. THE AMOUNT OR AMOUNTS TO BE RECEIVED BY THE HOLDERS IN THE EVENT OF VOLUNTARY OR INVOLUNTARY DISSOLUTION OR LIQUIDATION OF THE CORPORATION;

D. THE PRICE OR PRICES AT WHICH SHARES MAY BE REDEEMED AND ANY TERMS, CONDITIONS, AND LIMITATIONS UPON SUCH REDEMPTION;

E. ANY SINKING FUND PROVISIONS FOR REDEMPTION OR PURCHASE OF SHARES OF SUCH SERIES; AND

F. THE TERMS AND CONDITIONS, IF ANY, ON WHICH SHARES MAY BE CONVERTED AT THE ELECTION OF THE HOLDERS THEREOF INTO SHARES OF OTHER CAPITAL STOCK, OR OF OTHER SERIES OF SERIAL PREFERRED STOCK, OF THE CORPORATION.

EACH SERIES OF SERIAL PREFERRED STOCK, IN PREFERENCE TO THE COMMON STOCK, WILL BE ENTITLED TO DIVIDENDS, FROM FUNDS OR OTHER ASSETS LEGALLY AVAILABLE THEREFOR, AT SUCH RATES, PAYABLE AT SUCH TIMES AND CUMULATIVE TO SUCH EXTENT AS MAY BE FIXED BY THE BOARD OF DIRECTORS PURSUANT TO THE AUTHORITY HEREIN CONFERRED UPON IT. IN THE EVENT OF DISSOLUTION OR LIQUIDATION OF THE CORPORATION, VOLUNTARY OR INVOLUNTARY, THE HOLDERS OF THE SERIAL PREFERRED STOCK, IN PREFERENCE TO THE COMMON STOCK, WILL BE ENTITLED TO RECEIVE SUCH AMOUNT OR AMOUNTS AS MAY BE FIXED BY THE BOARD OF DIRECTORS PURSUANT TO THE AUTHORITY HEREIN CONFERRED UPON IT.

EACH SERIES OF SERIAL PREFERRED STOCK MAY BE SUBJECT TO REDEMPTION IN WHOLE OR IN PART AT SUCH PRICE OR PRICES AND ON SUCH TERMS, CONDITIONS, AND LIMITATIONS AS MAY BE FIXED BY THE BOARD OF DIRECTORS PRIOR TO THE ISSUANCE OF SUCH SERIES. IF LESS THAN ALL OF THE SHARES OF ANY SERIES OF THE SERIAL PREFERRED STOCK ARE TO BE REDEEMED, THEY WILL BE SELECTED IN SUCH MANNER AS THE BOARD OF DIRECTORS SHALL THEN DETERMINE. NOTHING HEREIN CONTAINED IS TO LIMIT ANY RIGHT OF THE CORPORATION TO PURCHASE OR OTHERWISE ACQUIRE ANY SHARES OF ANY SERIES OF THE SERIAL PREFERRED STOCK. ANY SHARES OF SERIAL PREFERRED STOCK REDEEMED OR OTHERWISE ACQUIRED BY THE CORPORATION AND WHICH REVERT TO THE STATUS OF AUTHORIZED AND UNISSUED SHARES SHALL BE UNDESIGNATED AS TO SERIES, AND MAY THEREAFTER, IN THE DISCRETION OF THE BOARD OF DIRECTORS AND TO THE EXTENT PERMITTED BY LAW, BE SOLD OR REISSUED FROM TIME TO TIME AS PART OF ANOTHER SERIES OR (UNLESS PROHIBITED BY THE TERMS OF SUCH SERIES AS FIXED BY THE BOARD OF DIRECTORS) OF THE SAME SERIES, SUBJECT TO THE TERMS AND CONDITIONS HEREIN SET FORTH.

NOTICE OF THE INTENTION OF THE CORPORATION TO REDEEM SHARES OF ANY SERIES OF THE SERIAL PREFERRED STOCK SHALL BE MAILED AT LEAST THIRTY (30) DAYS BFORE THE DATE OF REDEMPTION TO EACH HOLDER OF RECORD OF SHARES TO BE REDEEMED AT HIS OR HER LAST KNOWN POST OFFICE ADDRESS AS SHOWN BY THE RECORDS OF THE CORPORATION. AT ANY TIME AFTER SUCH NOTICE HAS BEEN MAILED AS AFORESAID, THE CORPORATION MAY DEPOSIT (SEPARATELY AS TO EACH SERIES) THE AGGREGATE REDEMPTION PRICE PAYABLE WITH RESPECT TO THE SHARES TO BE REDEEMED (OR THE PORTION THEREOF NOT ALREADY PAID IN THE REDEMPTION OF SUCH SHARES) WITH ANY BANK OR TRUST COMPANY IN THE UNITED STATES NAMED IN THE NOTICE OF REDEMPTION. SUCH DEPOSITS ARE TO BE PAYABLE IN AMOUNTS AS AFORESAID TO THE RESPECTIVE ORDERS OF THE HOLDERS OF RECORD OF THE SHARES TO BE REDEEMED ON ENDORSEMENT (IF REQUIRED) AND SURRENDER OF THEIR CERTIFI-

CATES. THEREUPON SUCH HOLDERS WILL CEASE TO BE SHAREHOLDERS WITH RESPECT TO SAID SHARES AND, FROM AND AFTER THE MAKING OF SUCH DEPOSIT, SUCH HOLDERS WILL HAVE NO INTEREST OR CLAIM AGAINST THE CORPORATION WITH RESPECT TO SAID SHARES, BUT WILL BE ENTITLED ONLY TO RECEIVE FROM SUCH BANK OR TRUST COMPANY, WITHOUT INTEREST, THE MONEYS SO DEPOSITED WITH IT.

SO LONG AS ANY SHARES OF SERIAL PREFERRED STOCK ARE OUTSTANDING, THE CORPORATION WILL NOT, WITHOUT THE AFFIRMATIVE VOTE OR CONSENT OF THE HOLDERS OF AT LEAST [here insert size of majority required, for example, TWO-THIRDS (⅔)] OF THE OUSTANDING SHARES OF THE SERIAL PREFERRED STOCK, VOTING AS A CLASS: (i) AUTHORIZE, BY AMENDMENT OF THE ARTICLES OF INCORPORATION, ANY STOCK RANKING PRIOR IN ANY RESPECT TO THE SERIAL PREFERRED STOCK or (ii) MAKE ANY CHANGE, BY AMENDMENT OF THE ARTICLES OF INCORPORATION OR OTHERWISE, IN THE TERMS AND PROVISIONS OF THE SERIAL PREFERRED STOCK OR ANY SERIES OF THE SERIAL PREFERRED STOCK OF WHICH ANY SHARES ARE THEN OUTSTANDING THAT WOULD ADVERSELY AFFECT THE RIGHTS AND PREFERENCES OF THE HOLDERS OF THE SERIAL PREFERRED STOCK; PROVIDED, HOWEVER, THAT IF THE PROPOSED AMENDMENT OR OTHER CHANGE WILL ADVERSELY AFFECT LESS THAN ALL OF THE SERIES OF SERIAL PREFERRED STOCK OF WHICH SHARES ARE THEN OUTSTANDING, ONLY THE AFFIRMATIVE VOTE OR CONSENT OF THE HOLDERS OF AT LEAST [here insert size of majority required, for example, TWO-THIRDS (⅔)] OF THE OUTSTANDING SHARES OF EACH SERIES THAT WILL BE ADVERSELY AFFECTED (EACH SUCH SERIES VOTING AS A CLASS) WILL BE REQUIRED, AND IN SUCH EVENT THE AFFIRMATIVE VOTE OR CONSENT OF THE HOLDERS OF [here insert size of majority required, for example, TWO-THIRDS (⅔)] OF THE OUTSTANDING SHARES OF ALL SERIES OF SERIAL PREFERRED STOCK, VOTING AS A CLASS, WILL NOT BE REQUIRED.

IF, AT THE TIME OF ANY ANNUAL MEETING OF SHAREHOLDERS, CUMULATIVE DIVIDENDS PAYABLE ON ANY SERIES OF THE SERIAL PREFERRED STOCK ARE ACCRUED AND UNPAID IN AN AMOUNT EQUAL TO

[here insert delinquency required to trigger rights, for example, SIX (6) QUARTERLY DIVIDENDS], THE HOLDERS OF THE SERIAL PREFERRED STOCK, VOTING AS A SINGLE CLASS FOR SUCH PURPOSE, WILL BE ENTITLED TO ELECT [here insert number of directors to be elected by serial preferred stock, for example, TWO (2)] DIRECTORS. WHENEVER THIS RIGHT IS VESTED IN THE HOLDERS OF THE SERIAL PREFERRED STOCK, THE BOARD OF DIRECTORS WILL, AT LEAST TEN (10) DAYS PRIOR TO SUCH ANNUAL MEETING AT WHICH SUCH DIVIDENDS REMAIN ACCRUED AND UNPAID, CAUSE A NOTICE TO THAT EFFECT TO BE MAILED TO EACH SHAREHOLDER AT HIS OR HER LAST KNOWN POST OFFICE ADDRESS AS SHOWN BY THE RECORDS OF THE CORPORATION. AT ALL MEETINGS OF SHAREHOLDERS WHERE THE HOLDERS OF THE SERIAL PREFERRED STOCK HAVE SUCH RIGHT TO ELECT DIRECTORS, THE PRESENCE IN PERSON OR BY PROXY OF THE HOLDERS OF A MAJORITY OF THE AGGREGATE NUMBER OF OUTSTANDING SHARES OF SERIAL PREFERRED STOCK WILL BE REQUIRED TO CONSTITUTE A QUORUM FOR THE ELECTION OF SUCH DIRECTORS; PROVIDED, HOWEVER, THAT THE ABSENCE OF A QUORUM OF THE HOLDERS OF THE SERIAL PREFERRED STOCK WILL NOT PREVENT THE ELECTION AT ANY SUCH MEETING OR ADJOURNMENT THEREOF OF THE REMAINING DIRECTORS IN THE USUAL MANNER BY THE HOLDERS OF ALL CLASSES OF STOCK IF THE NECESSARY QUORUM REQUIRED THEREFOR IS PRESENT IN PERSON OR BY PROXY AT SUCH MEETING. WHEN ALL DIVIDENDS ACCRUED AND UNPAID ON THE SERIAL PREFERRED STOCK HAVE BEEN PAID, OR DECLARED AND SET APART FOR PAYMENT, HOLDERS OF THE SERIAL PREFERRED STOCK WILL, AT THE NEXT ANNUAL MEETING, BE DIVESTED OF THEIR RIGHTS IN RESPECT TO SUCH ELECTION OF DIRECTORS, AND THE VOTING POWER OF THE HOLDERS OF THE SERIAL PREFERRED STOCK AND THE HOLDERS OF THE COMMON STOCK WILL REVERT TO THE STATUS EXISTING BEFORE THE FIRST DIVIDEND PAYMENT DATE ON WHICH DIVIDENDS ON THE SERIAL PREFERRED STOCK WERE NOT PAID IN FULL; BUT ALWAYS SUBJECT TO THE SAME PROVISIONS FOR VESTING SUCH SPECIAL RIGHTS IN THE HOLDERS OF THE SERIAL PREFERRED STOCK IN THE EVENT DIVIDENDS ON ANY SERIES OF THE SERIAL PREFERRED STOCK

SHOULD AGAIN BECOME ACCRUED AND UNPAID IN AN AMOUNT EQUAL TO [here insert delinquency required to trigger rights, for example, SIX (6) QUARTERLY DIVIDENDS]. VACANCIES AMONG DIRECTORS ELECTED BY HOLDERS OF THE SERIAL PREFERRED STOCK DURING ANY PERIOD FOR WHICH SUCH DIRECTORS HAVE BEEN SO ELECTED ARE TO BE FILLED, UNTIL THE NEXT ANNUAL OR SPECIAL MEETING FOR THE ELECTION OF DIRECTORS, BY THE VOTE OF THE REMAINING DIRECTORS OF THE CORPORATION.

DIVIDENDS MAY BE PAID UPON THE COMMON STOCK ONLY WHEN DIVIDENDS HAVE BEEN PAID, OR FUNDS HAVE BEEN SET APART FOR THE PAYMENT OF DIVIDENDS, ON THE SERIAL PREFERRED STOCK FROM THE DATE AFTER WHICH DIVIDENDS ON THE SERIAL PREFERRED STOCK BECAME CUMULATIVE TO THE BEGINNING OF THE THEN CURRENT DIVIDEND PERIOD, BUT WHENEVER THERE SHALL HAVE BEEN PAID, OR FUNDS SHALL HAVE BEEN SET APART FOR THE PAYMENT OF, ALL SUCH DIVIDENDS UPON THE SERIAL PREFERRED STOCK, THEN DIVIDENDS UPON THE COMMON STOCK MAY BE DECLARED FOR PAYMENT THEN OR THEREAFTER OUT OF ANY REMAINING FUNDS OR OTHER ASSETS LEGALLY AVAILABLE FOR SUCH PAYMENT. AFTER THE PAYMENT OF THE DESIGNATED DIVIDENDS, AND AMOUNTS PAYABLE UPON DISSOLUTION OR LIQUIDATION, IF ANY, TO WHICH THE SHARES OF THE SERIAL PREFERRED STOCK ARE EXPRESSLY ENTITLED IN PREFERENCE TO THE COMMON STOCK IN ACCORDANCE WITH THE PROVISIONS HEREIN SET FORTH, THE COMMON STOCK IS TO RECEIVE ALL FURTHER SUCH DIVIDENDS AND AMOUNTS.

A CONSOLIDATION, MERGER, OR AMALGAMATION OF THIS CORPORATION WITH OR INTO ANY OTHER CORPORATION OR CORPORATIONS SHALL NOT BE DEEMED A DISTRIBUTION OF ASSETS OF THE CORPORATION WITHIN THE MEANING OF ANY PROVISIONS HEREOF.

Annotation 5. All corporations must have common stock; therefore, if only one class of stock is to be issued, it must be common stock. *See, e.g.*, 11 W. FLETCHER, *supra* note 205, §§ 5086, 5283 (rev. 1971). Redeemable common stock may not be issued unless there is at least one class of common stock outstanding which is not redeemable. ARIZ REV. STAT. ANN. § 10-015(C) (Supp. Pamphlet 1975).

Thus, this article must contain the basic prerequisite of at least one class of nonredeemable common stock, plus any additional classes to be authorized. The alternative models are addressed to some of the possible stock mixes a corporation might wish to authorize.

The Act provides great flexibility for establishing classes and series of stock and their rights and preferences. Of paramount importance in drafting articles relating to various classes of stock is a clear delineation of the rights and preferences of the respective classes. Sections 10-015 and 10-016, setting forth the statutory requirements with respect to classes and series of stock, enumerate only two restrictions: stock that is entitled to vote for directors must have cumulative voting rights, *id.* § 10-015 (A); ARIZ. CONST., art. 14, § 10, and redeemable shares must be redeemable only at the option of the corporation unless the corporation is a registered investment company, in which case the holder may be granted an option to redeem. ARIZ REV. STAT. ANN. § 10-015(D) (Supp. Pamphlet 1975). Although the Arizona constitution provides that shares entitled to vote for directors must be permitted to vote cumulatively, ARIZ. CONST. art. 14, § 10, it does not require that all shares carry voting rights. Therefore, nonvoting stock or stock entitled to vote on the election of directors only in certain circumstances is permissible. Model article 5E contains such an authorization.

If a corporation plans to issue noncommon stock that is to be redeemable, to have cumulative, noncumulative, or partially cumulative dividends, to have preference as to dividends, to have preference in liquidation, or to be convertible into another security, such provisions must be set forth in the articles of incorporation. The attributes of any series within an authorized class of stock may be fixed by the articles of incorporation, ARIZ. REV. STAT. ANN. § 10-016(B) (Supp. Pamphlet 1975), or may be left to the discretion of the board of directors. *Id.* § 10-016(D). If the latter course is to be followed, division of the class into series must be specifically authorized in the articles of incorporation, as must the directors' discretion to make such determinations. *Id.* Additionally, at the time any such series is issued a description of the stock issued must be filed with the Arizona Corporation Commission. *Id.* §§ 10-016(F)-(H). Model article 5E illustrates a provision for this type of stock issuance.

Model articles 5A through 5E illustrate various options available to incorporators. These models are not intended to be exhaustive, and other provisions with respect to the rights and characteristics of classes of stock may be used. Model article 5A should be used by corporations wanting only one class of stock. Where two classes of stock iden-

tical except that one is voting and one is nonvoting are planned, model article 5B illustrates the appropriate form. Model article 5C creates a class of common stock and a class of nonvoting preferred stock. The preferred stock can be made voting stock by the deletion of the last paragraph of the model. Model article 5D provides for a class of common stock and a class of convertible redeemable preferred stock. This model may be adapted to authorize preferred stock with fewer than all of these features merely by striking the language relating to features not desired. Where a preferred stock is to be divided into series with the board of directors having authority to set forth the attributes of those series when issued, model article 5E may be used. Model 5E is designed to contain as much detail as possible about the issuance of various types of stock and to provide the greatest possible discretion to the board of directors. In the normal situation not all of the provisions of model 5E will be desired and those found unnecessary can be deleted accordingly.

It is no longer necessary to authorize an artificially high amount of capital stock, the power of the corporation to incur indebtedness being no longer dependent upon the amount of capital stock authorized. See text & note 38 *supra*; text accompanying note 239 *supra*. Although the amount of authorized capital is immaterial for reporting or taxation purposes in Arizona, many states have qualification fees and franchise taxes based upon authorized capital. Therefore, if it is likely that the corporation will be required to qualify to do business in another state, it is advisable to keep the authorized capital relatively low, consonant with sound business practices.

[6] 5.1A. PREEMPTIVE RIGHTS. THE HOLDERS FROM TIME TO TIME OF THE [here insert the classes of stock to have preemptive rights, for example, COMMON] STOCK OF THE CORPORATION SHALL HAVE PREEMPTIVE RIGHTS AS TO THE [here insert the classes of stock to which preemptive rights apply, for example, COMMON] STOCK THEN OR THEREAFTER AUTHORIZED TO BE ISSUED [here insert whether treasury stock is to be included, for example, INCLUDING TREASURY STOCK]. NO RESOLUTION OF THE BOARD OF DIRECTORS AUTHORIZING THE ISSUANCE OF STOCK TO WHICH PREEMPTIVE RIGHTS SHALL ATTACH MAY REQUIRE SUCH RIGHTS TO BE EXERCISED WITHIN LESS THAN [here insert minimum time limit, for example, SIXTY (60) DAYS].

5.1B. PREEMPTIVE RIGHTS. THE HOLDERS FROM TIME TO TIME OF THE [here insert the classes of stock to

have preemptive rights, for example, COMMON] STOCK OF THE CORPORATION SHALL HAVE PREEMPTIVE RIGHTS AS TO ANY [here insert the classes of stock to which preemptive rights apply, for example, NEW OR EXISTING CLASSES OF] STOCK THAT MAY BE AUTHORIZED BY AMENDMENT TO THE ARTICLES OF INCORPORATION INCREASING AUTHORIZED CAPITAL AND THEREAFTER AUTHORIZED BY THE BOARD OF DIRECTORS TO BE ISSUED. NO PREEMPTIVE RIGHTS SHALL ATTACH WITH RESPECT TO STOCK AUTHORIZED BY THE ORIGINAL ARTICLES OF INCORPORATION. NO RESOLUTION OF THE BOARD OF DIRECTORS AUTHORIZING THE ISSUANCE OF STOCK TO WHICH PREEMPTIVE RIGHTS SHALL ATTACH MAY REQUIRE SUCH RIGHTS TO BE EXERCISED WITHIN LESS THAN [here insert minimum time limit, for example, SIXTY (60) DAYS].

Annotation 6. Under ARIZ. REV. STAT. ANN. § 10-026 (Supp. Pamphlet 1975) shareholders have no automatic preemptive right to acquire any unissued or treasury shares of the corporation or securities convertible into or carrying a right to subscribe to or acquire shares, except to the extent that such right is provided in the articles of incorporation. See text & notes 237-45 *supra.* Therefore, if no preemptive rights are intended, no provision need be made in the articles. If preemptive rights are desired, however, either model article 5.1A or 5.1B may be used.

Model article 5.1A provides preemptive rights to the existing shareholders in all newly-issued shares to be issued by the corporation, whether or not such shares are authorized by amendments to the articles of incorporation or instead have already been authorized but merely have not been issued. Model article 5.1B grants preemptive rights only to previously unauthorized shares that may be issued only following an authorizing amendment to the articles of incorporation. This model may be desirable in forming a small corporation in which the original organizers intend to seek one or more additional persons to invest at some time after the original organization of the corporation. The articles of incorporation in this situation could authorize shares intended to be issued subsequently to those new investors, while providing for preemptive rights in any additional shares authorized and issued after the original shares are outstanding.

The broad language of section 10-026 makes it possible for holders of one class of stock to have preemptive rights in a different class. For example, holders of common stock could have preemptive rights in the issuance of any new class of stock, common or preferred. Hold-

ers of a specific class of preferred stock may be given preemptive rights in the issuance of a different class of preferred stock, and indeed may even be given preemptive rights with respect to additional issues of common stock. In model articles 5.1A and 5.1B, the first insertion denominates the class of stock of the corporation, ownership of which gives rise to the right to buy additional shares. The second insertion indicates the class or classes of stock which those holders are entitled to buy.

The articles of incorporation should specifically provide that preemptive rights attach to treasury stock if that is intended. Because of the statutory provision permitting cancellation of treasury stock only if appropriate statements are filed with the Arizona Corporation Commission, ARIZ. REV. STAT. ANN. § 10-068 (Supp. Pamphlet 1975), it is probable that corporations repurchasing their shares will normally hold those repurchased shares as treasury stock, making it important to provide for preemptive rights, if desired, in the articles of incorporation. Since model article 5.1B grants preemptive rights with respect only to shares newly authorized by shareholders, treasury shares will never be encompassed if that model article is used.

[7] **5.2A. CONSIDERATION FOR SHARES. SHARES HAVING A PAR VALUE MAY BE ISSUED FOR SUCH CONSIDERATION EXPRESSED IN DOLLARS, NOT LESS THAN THE PAR VALUE THEREOF, AS SHALL BE FIXED FROM TIME TO TIME BY THE SHAREHOLDERS OF THE CORPORATION.**

5.2B. CONSIDERATION FOR SHARES. SHARES WITHOUT PAR VALUE MAY BE ISSUED FOR SUCH CONSIDERATION EXPRESSED IN DOLLARS AS MAY BE FIXED FROM TIME TO TIME BY THE SHAREHOLDERS OF THE CORPORATION.

5.2C. CONSIDERATION FOR SHARES. TREASURY SHARES, WITH OR WITHOUT PAR VALUE, MAY BE DISPOSED OF BY THE CORPORATION FOR SUCH CONSIDERATION EXPRESSED IN DOLLARS AS MAY BE FIXED FROM TIME TO TIME BY THE SHAREHOLDERS OF THE CORPORATION.

Annotation 7. The consideration for the issuance of new shares or treasury shares is normally fixed by the board of directors, and no provision concerning consideration need be inserted in the articles if this practice is to be followed. The consideration must be at least par value for newly-issued par value shares, ARIZ. REV. STAT. ANN. § 10-018(A) (Supp. Pamphlet 1975), but may be any amount for shares without par value, *id.* § 10-018(B), and for treasury shares. *Id.* § 10-

018(C). The right to fix the consideration may, however, be reserved to the shareholders by the articles of incorporation, in which case the board of directors would have no power to determine the amount for which shares are issued, although the board of directors could still determine to whom the shares would be issued. *Id.* § 10-018(D). Model article 5.2A provides for shareholders' power to fix consideration for par value shares, model article 5.2B for shares without par value, and model article 5.2C for treasury shares. These models are not exclusive, and model article 5.2C can be combined with either 5.2A or 5.2B. All three models can be used if the corporation has authority to issue two or more classes of stock, one with par value and one without. For a discussion of the type of consideration for which shares may validly be issued, see note 229 *supra.*

[8] 5.3. SHAREHOLDER MAJORITY REQUIRED. IN FIXING THE CONSIDERATION FOR SHARES OF THIS CORPORATION, THE SHAREHOLDERS SHALL ACT BY THE AFFIRMATIVE VOTE OR CONSENT OF THE HOLDERS OF [here insert majority required, for example, THREE-FIFTHS (⅗)] OF THE OUTSTANDING SHARES ENTITLED TO VOTE THEREON.

Annotation 8. The Act specifically provides that if the articles of incorporation reserve to the shareholders the right to determine the consideration for the issue of any shares, the shareholders can act by a majority vote of the outstanding shares entitled to vote thereon. ARIZ. REV. STAT. ANN. § 10-018(D) (Supp. Pamphlet 1975). The statute allows the articles to require a greater vote, however, and model article 5.3 accordingly requires a vote of more than a majority.

[9] 5.4. STOCK RIGHTS AND OPTIONS. [Here insert any restrictions on the creation and issuance of rights or options to purchase shares of stock of the corporation and restrictions on the terms pursuant to which stock rights or options can be issued, for example, THE CORPORATION MAY CREATE AND ISSUE WARRANTS, PUTS, CALLS, RIGHTS, OR OPTIONS ENTITLING THE HOLDERS THEREOF TO PURCHASE FROM THE CORPORATION SHARES OF ANY CLASS OR CLASSES OR WARRANTS, PUTS, CALLS, OR OTHER RIGHTS CONVERTIBLE INTO SUCH SHARES ONLY IF SUCH CREATION AND ISSUANCE, INCLUDING THE TERMS THEREOF, ARE APPROVED IN ADVANCE BY THE HOLDERS OF TWO-THIRDS (⅔) OF THE ISSUED AND OUTSTANDING VOTING STOCK OF THE CORPORATION AT A DULY CALLED MEETING OF SHAREHOLDERS.]

Annotation 9. The normal rule with respect to stock rights and options is set forth in ARIZ. REV. STAT. ANN. § 10-020 (Supp. Pamphlet 1975). The board of directors may, without shareholder approval, create and issue rights or options entitling the holders thereof to purchase from the corporation shares of any authorized but unissued stock of the corporation. The articles of incorporation, however, may change this rule by requiring shareholder approval of any such action. The articles also may set the terms of such options or prevent their issuance altogether, as though stock rights and options were authorized classes of stock. Any restrictions on the terms of stock options or rights or any prohibition of their issuance by the articles of incorporation can, of course, be later amended. If the articles are silent, the board of directors has the discretion to create and issue stock rights and options.

[10] 5.5. STOCK RIGHTS AND OPTIONS—OFFICERS. [Here insert any provisions altering the requirement of shareholder approval of stock rights or options to directors, officers, or employees, for example, THE CORPORATION MAY ISSUE RIGHTS AND OPTIONS TO PURCHASE SHARES OF STOCK OF THE CORPORATION TO DIRECTORS, OFFICERS, OR EMPLOYEES OF THE CORPORATION OR OF ANY AFFILIATE THEREOF, AND NO SHAREHOLDER APPROVAL OR RATIFICATION OF ANY SUCH ISSUANCE OF RIGHTS AND OPTIONS SHALL BE REQUIRED.]

Annotation 10. The Act permits stock option plans and the issuance of stock options for the benefit of directors, officers, and employees of the corporation or of any affiliate. ARIZ. REV. STAT. ANN. § 10-020 (Supp. Pamphlet 1975). However, unlike the normal rule with respect to stock options, section 10-020 requires shareholder approval either of the specific stock option or, if the option is issued pursuant to a plan, shareholder approval of that plan. The statute does provide, however, that the articles of incorporation can alter this rule. Model article 5.5 completely removes the requirement of shareholder approval. Other types of alterations might be restrictions on the classes of persons to whom stock options could be given, such as employees who are not directors, or restrictions on the terms on which the stock options could be granted. If such restrictions are desired, however, it is not necessary to place them in the articles in advance, since shareholder approval of the options or of an amendment to the articles will be necessary to authorize these types of options if the articles are silent. *Id.*

[11] 5.6. LIABILITY OF SUBSCRIBERS AND SHAREHOLDERS. SHAREHOLDERS OF THE CORPORATION SHALL BE SUBJECT TO ASSESSMENT ONLY PUR-

SUANT TO THE TERMS OF THIS ARTICLE. IN THE EVENT THE BOARD OF DIRECTORS DETERMINES THAT ADDITIONAL CAPITAL IS REQUIRED BY THE CORPORATION TO COMPLETE PAYMENT FOR OR MAINTAIN REAL PROPERTY OWNED BY THE CORPORATION, IT MAY RECOMMEND TO A SHAREHOLDERS' MEETING THAT AN ASSESSMENT BE LEVIED. AT LEAST FIFTEEN (15) DAYS' ADVANCE WRITTEN NOTICE OF THE MEETING SHALL BE GIVEN TO EACH SHAREHOLDER, AND THE NOTICE SHALL CONTAIN A SUMMARY OF THE PROPOSAL BY THE BOARD OF DIRECTORS. IF THE SHAREHOLDERS APPROVE THE ASSESSMENT BY THE AFFIRMATIVE VOTE OF THE HOLDERS OF AT LEAST EIGHTY PERCENT (80%) OF THE SHARES TO BE ASSESSED, THE ASSESSMENT SHALL BE MADE. THE RIGHT TO ENFORCE PAYMENT OF THE ASSESSMENT SHALL IMMEDIATELY BECOME ABSOLUTE, BUT SHALL BE VESTED ONLY IN THE CORPORATION, ITS SUCCESSORS, ITS RECEIVERS AND TRUSTEES. EXCEPT AS PROVIDED IN THIS ARTICLE, A HOLDER OF OR SUBSCRIBER FOR SHARES OF A CORPORATION SHALL BE UNDER NO OBLIGATION TO THE CORPORATION OR ITS CREDITORS WITH RESPECT TO SUCH SHARES OTHER THAN THE OBLIGATION TO PAY TO THE CORPORATION THE FULL CONSIDERATION FOR WHICH SUCH SHARES WERE ISSUED OR TO BE ISSUED.

Annotation 11. The Act provides that a holder of or subscriber for shares of a corporation shall have no liabilities to the corporation or to its creditors with respect to the shares other than the obligation to pay to the corporation a full consideration for which such shares were issued or to be issued, thus granting to shareholders the limited liability which is normally the objective of incorporation. ARIZ. REV. STAT. ANN. § 10-025 (Supp. Pamphlet 1975). See text & notes 85-89 *supra.* Section 10-025 does specifically allow for alteration of this rule in the articles of incorporation. Because of its divergence from basic corporate objectives, however, imposition of liability through language such as that in model article 5.6 is not advised except in very unusual circumstances. For instance, provision must be made for the liability of shareholders of banks or insurance companies in order to meet the mandate of article 14, section 11 of the Arizona constitution. In general, however, a corporation's future capital needs can amply be met through the sale of additional stock. Model article 5.6 is suggested only for those rare instances where, although it is necessary that all par-

ticipants be assessable proportionately for as long as the enterprise exists, a limited partnership form of organization is impossible or undesirable.

[12] 5.7. REISSUANCE OF REDEEMABLE SHARES PROHIBITED. REDEEMABLE SHARES OF THE CORPORATION, WHEN REDEEMED OR REPURCHASED BY THE CORPORATION, SHALL BE CANCELLED AND SHALL NOT BE REISSUED.

Annotation 12. Model article 5.7 has no application unless there exists a class of redeemable shares. See Model Articles 5D & 5E *supra.* Redeemable shares, for the purpose of the Act, are those shares which by their terms and the terms of the articles of incorporation may be repurchased at stated times or at stated prices at the option of the corporation. *See* ARIZ. REV. STAT. ANN. § 10-015(B)(1) (Supp. Pamphlet 1975). Where the issuance of redeemable shares is authorized by the organizers or shareholders for the purpose of raising money for a specific purpose and it is intended that no new redeemable shares be issued after the funds for that purpose have been raised, model article 5.7 should be included in the articles. Such a provision is expressly allowed for by the Act. *Id.* § 10-067(A). In order to raise money for the corporation by subsequent issuance of redeemable shares, the board of directors would have to request of the shareholders that a new class of redeemable shares be authorized or that model article 5.7 be removed from the articles by an amendment. In either event, the shareholders would retain control of this type of financing.

[13] 6. STATUTORY AGENT. THE NAME AND ADDRESS OF THE INITIAL STATUTORY AGENT OF THE CORPORATION IS [here insert name and address, for example, BENJAMIN DISRAELI, 123 KEW GARDENS DRIVE, PHOENIX, ARIZONA 85132].

Annotation 13. The designation of a statutory agent is required by ARIZ. REV. STAT. ANN. § 10-054(A)(9) (Supp. Pamphlet 1975). The statutory agent may be either an individual who has lived in the state for 3 years, a domestic corporation, or a foreign corporation authorized to transact business in Arizona. *Id.* § 10-012(2). It is not necessary to state the qualifications of the statutory agent, a statement of the name and address being sufficient. The address of the statutory agent will be legally regarded as the known place of business of the corporation unless otherwise indicated. *Id.* § 10-012(1). See Annot. 14 *infra.*

[14] 6.1. KNOWN PLACE OF BUSINESS. THE KNOWN PLACE OF BUSINESS OF THE CORPORATION

SHALL BE [here insert address, for example, ONE WEST MAIN STREET, PHOENIX, ARIZONA 85132].

Annotation 14. Model article 6.1 is to be used where the known place of business is to be some address other than that of the statutory agent. *See* ARIZ. REV. STAT. ANN. § 10-012 (Supp. Pamphlet 1975). Alternatively, the known place of business may be designated by a statement filed with the Arizona Corporation Commission after incorporation. *Id.* § 10-013. A known place of business is required by article 14, section 8 of the Arizona constitution. Its primary significance, other than determining the county where required publications must be made, *id.* § 10-055(C), is in serving as the site upon which the Arizona Corporation Commission makes service of process when the statutory agent has resigned. *See id.* § 10-014(B).

[15] 7. BOARD OF DIRECTORS. THE INITIAL BOARD OF DIRECTORS SHALL CONSIST OF [here insert number, for example, TWO (2)] DIRECTORS. THE PERSONS WHO ARE TO SERVE AS DIRECTORS UNTIL THE FIRST ANNUAL MEETING OF SHAREHOLDERS OR UNTIL THEIR SUCCESSORS ARE ELECTED AND QUALIFY ARE: [here insert names and addresses, for example,

HENRY PLANTAGENET	**ANNE BOLEYN**
142 TUDOR DRIVE	**146 TUDOR DRIVE**
TUCSON, ARIZONA 85764	**TUCSON, ARIZONA 85764].**

Annotation 15. The number of the initial directors and their names and addresses must be stated. ARIZ. REV. STAT. ANN. § 10-054(A)(10) (Supp. Pamphlet 1975). The number of directors to serve thereafter need not be stated in the articles, but instead may be left to the bylaws; if this course is followed, some mention of that fact should be made in the articles. See Model Article 7.1C *infra*. Although no maximum number of directors is required, there must be provision for at least one. ARIZ. REV. STAT. ANN. § 10-036 (Supp. Pamphlet 1975). Directors need not be either shareholders or residents of the state. *Id.* § 10-035.

[16] 7.1A. CLASSIFICATION OF DIRECTORS. THERE SHALL BE [here insert total number of directors, for example, NINE (9)] MEMBERS OF THE BOARD OF DIRECTORS. THE DIRECTORS SHALL BE CLASSIFIED IN SUCH MANNER THAT EACH DIRECTOR SHALL SERVE A TERM OF [TWO (2) or THREE (3)] YEARS AND IN SUCH MANNER THAT THE TERMS OF APPROXIMATELY [ONE-HALF (½) or ONE-THIRD (⅓)] OF THE WHOLE NUMBER OF DIRECTORS SHALL EXPIRE ANNUALLY.

Annotation 16. The Act permits the classification of directors so that either one-half of the directors are elected each year to serve a 2-year term or one-third of the directors are elected each year to serve a 3-year term. ARIZ. REV. STAT. ANN. § 10-037 (Supp. Pamphlet 1975). This concept has been attacked as being in derogation of the constitutional right of stockholders to cumulative voting for directors. ARIZ. CONST. art. 14, § 10. The Arizona supreme court, however, has held that so long as the board of directors consists of at least nine persons and the classification is not in more than three classes, it is permissible. Bohannan v. Arizona Corporation Comm'n, 82 Ariz. 299, 304, 313 P.2d 379, 382 (1957). See discussion note 204 *supra.* Accordingly, the statute requires that there be at least nine members of the board of directors before classification will be permitted. ARIZ. REV. STAT. ANN. § 10-037 (Supp. Pamphlet 1975). If classification is desired, therefore, model article 7.1A must provide for a fixed number of at least nine directors.

Section 10-037 also provides that no classification of directors shall be effective prior to the first annual meeting of the shareholders, thereby preventing specification in the articles of incorporation as to which directors shall serve initially 3-year, 2-year, and 1-year terms. A statement to the effect that the initial classification of directors shall occur at the first annual meeting of shareholders could be inserted in model article 7.1A, but would merely be surplusage since section 10-037 already contains this requirement. If classification is intended at some time other than the first annual meeting of shareholders, however, a statement to that effect should be inserted in model article 7.1A.

[17] 7.1B. NUMBER OF DIRECTORS. THE NUMBER OF PERSONS TO SERVE ON THE BOARD OF DIRECTORS SHALL BE FIXED BY THE SHAREHOLDERS AT THE ANNUAL MEETING OR ANY SPECIAL MEETING CALLED FOR THAT PURPOSE, [here insert any restrictions, for example, EXCEPT THAT THE BOARD OF DIRECTORS SHALL ALWAYS CONSIST OF NOT FEWER THAN TWO (2) PERSONS NOR MORE THAN TEN (10) PERSONS].

7.1C. NUMBER OF DIRECTORS. THE NUMBER OF PERSONS TO SERVE ON THE BOARD OF DIRECTORS SHALL BE FIXED BY THE BYLAWS.

Annotation 17. Although the Act requires that the articles state the number of persons constituting the initial board of directors, there is no requirement that the articles also state the number of directors to serve in the future. *See* ARIZ. REV. STAT. ANN. § 10-054(A)(10)

(Supp. Pamphlet 1975). That number, or the procedure for its determination, may be fixed in either the articles of incorporation or the bylaws. *Id.* § 10-036. If this is to be done in the bylaws, a statement to that effect, such as model article 7.1C, should be included in the articles. Model 7.1B, on the other hand, illustrates a provision providing complete flexibility to the shareholders in fixing the number of directors from time to time. Alternatively, a more restrictive provision specifically setting the number of directors could be inserted. The Act permits the number of directors to be set as low as one, with no upper limit specified. *Id.* See text & note 203 *supra.* The articles or bylaws may also prescribe the method for increasing or decreasing the number of directors, if this is to be done by some procedure other than the amendment process. ARIZ. REV. STAT. ANN. § 10-036 (Supp. Pamphlet 1975). When the provisions relating to number of directors appear in the corporate bylaws, they may be changed by a board of directors having such authority. If such provisions appear in the articles, however, they may be changed only by the shareholders.

If a staggered term for the board of directors is desired, the number of directors must be fixed. *Id.* § 10-037. In this situation, model article 7.1A rather than model 7.1B or C would be appropriate. See Annot. 16 *supra.*

[18] 7.2A. MANAGEMENT. THE BUSINESS AND AFFAIRS OF THE CORPORATION SHALL BE MANAGED BY THE BOARD OF DIRECTORS EXCEPT THAT [here insert limitations, for example, SHAREHOLDER APPROVAL SHALL BE REQUIRED FOR ANY PURCHASE OR SALE OF REAL PROPERTY BY THE CORPORATION].

7.2B. MANAGEMENT. [For use if all management is to be vested in the shareholders, for example, SO LONG AS THE TOTAL NUMBER OF SHAREHOLDERS OF THE CORPORATION SHALL BE FEWER THAN FIVE (5), THE BUSINESS AND AFFAIRS OF THE CORPORATION SHALL BE MANAGED BY THE SHAREHOLDERS. ALL PROVISIONS WITH RESPECT TO ACTIONS OF THE BOARD OF DIRECTORS CONTAINED IN LAW, THESE ARTICLES, AND OTHER DOCUMENTS BY WHICH THE CORPORATION IS BOUND SHALL APPLY TO AND BE BINDING UPON ACTIONS OF THE SHAREHOLDERS IN MANAGEMENT OF THE CORPORATION.]

Annotation 18. The Act provides that the board of directors shall manage the business and affairs of a corporation except to the extent it is reserved to the shareholders by the articles. ARIZ. REV. STAT. ANN. § 10-035 (Supp. Pamphlet 1975). The shareholders, therefore,

may either have specific powers over certain actions of the board of directors, see Model Article 7.2A *supra*, or, if desired, be granted by the articles all of the powers of the board of directors. See Model Article 7.2B *supra*. To the extent powers are reserved to the shareholders, the board of directors has no authority to act or bind the corporation. Such a reservation of power may be particularly desirable to a closely held corporation preferring to vest the management power in the shareholders. Even though no power is left to the board, it is still necessary that a board of directors be named in the articles of incorporation and that the board remain in existence. See Annot. 15 *supra*.

[19] 7.3. QUALIFICATIONS OF DIRECTORS. [Here insert qualifications, for example, EACH MEMBER OF THE BOARD OF DIRECTORS MUST BE A RESIDENT OF THE CITY OF PHOENIX WHILE SERVING, or, AT ALL TIMES, NO FEWER THAN ONE-HALF (½) OF THE WHOLE NUMBER OF DIRECTORS MUST QUALIFY AS POOR PERSONS ACCORDING TO THE GUIDELINES THEN IN FORCE PROMULGATED BY THE UNITED STATES OFFICE OF ECONOMIC OPPORTUNITY.]

Annotation 19. If the bylaws and articles of incorporation are silent as to qualifications, any person, whether or not a resident of the state or a shareholder, may serve as a director of a corporation. ARIZ. REV. STAT. ANN. § 10-035 (Supp. Pamphlet 1975). If specific qualifications are to be required, therefore, they must be placed in the articles or bylaws. See text & notes 201-02 *supra*. Model article 7.3 illustrates the type of qualification that might be required in corporations dealing with projects in certain geographical areas or relating to persons in certain income levels.

[20] 7.4. DIRECTORS' COMPENSATION. THE BOARD OF DIRECTORS SHALL NOT HAVE THE AUTHORITY TO FIX COMPENSATION OF DIRECTORS FOR SERVICES IN ANY CAPACITY. ALL SUCH COMPENSATION SHALL BE ESTABLISHED, CHANGED, AND TERMINATED BY ACTS OF THE SHAREHOLDERS.

Annotation 20. If the subject of compensation of corporate employees is not covered in the bylaws or articles of incorporation, the board of directors has authority to set the salaries of all officers of the corporation, including those of directors. ARIZ. REV. STAT. ANN. § 10-035 (Supp. Pamphlet 1975). An action establishing directors' salaries will be valid so long as it conforms to the general rules governing director conflicts of interest. *Id.* § 10-041. Section 10-041 provides that

a transaction between a corporation and one of its directors will be upheld if it is fair, if the relationship is disclosed and the shareholders authorize it, or if the relationship is disclosed and a majority of the board of directors who are disinterested approve. See text & notes 212-13 *supra*. The rule with respect to compensation can, however, be changed in the articles or bylaws. Model article 7.4 removes from the directors the authority to fix their own compensation and requires that it be done by the shareholders.

[21] 7.5. VACANCIES IN BOARD OF DIRECTORS. NO DIRECTOR WHO HAS SUBMITTED HIS OR HER RESIGNATION FROM THE BOARD OF DIRECTORS EFFECTIVE AT A FUTURE TIME SHALL BE PERMITTED TO VOTE UPON THE FILLING OF ANY VACANCY OR VACANCIES ON THE BOARD OF DIRECTORS, INCLUDING THE VACANCY TO BE CREATED BY HIS OR HER RESIGNATION.

Annotation 21. Unless the articles of incorporation or bylaws are to the contrary, a director can submit his or her resignation to be effective at a future date and then participate in the election of a successor. ARIZ. REV. STAT. ANN. § 10-038 (Supp. Pamphlet 1975). This provision enables a board of directors to be totally changed in connection with a change of control of the corporation, without the formality of separate resignations and elections. A provision to the contrary is contained in model article 7.5. Although not preventing a change of board of directors by individual resignations and elections, it would prevent the complete change in one election.

[22] 7.6. QUORUM. A QUORUM AT A MEETING OF THE BOARD OF DIRECTORS SHALL CONSIST OF [here insert requirement desired, for example, TWO (2)] DIRECTORS.

Annotation 22. The Act permits the articles of incorporation to fix a quorum of the board of directors at one-third or more of the total number of directors, but in no event less than two unless a 1-member board is authorized. ARIZ. REV. STAT. ANN. § 10-040 (Supp. Pamphlet 1975). A quorum requirement greater than a majority may be established in the bylaws, but a quorum of less than majority may be authorized only by the articles. *Id.* In the absence of different provision in the articles or bylaws, a majority of the number of directors then serving constitutes a quorum. *Id.* See text & note 207 *supra*. Requiring less than a majority may be useful in situations in which directors are scattered geographically, making it infeasible to assemble a majority with any frequency. On the other hand, setting a quorum at a higher

percentage than majority may be advisable in situations in which only a few interests are represented in the ownership of the corporation, each needing veto power. Veto power can be obtained by setting the quorum requirement high enough that the nonattendance of one interest at any meeting precludes the conducting of business.

[23] 7.7. VOTING REQUIRED. THE AFFIRMATIVE VOTE OF [here insert the majority required, which must be a majority or greater, for example, FOUR-FIFTHS (4/5)] OF THE DIRECTORS PRESENT AND VOTING AT A MEETING AT WHICH A QUORUM IS PRESENT SHALL BE REQUIRED FOR ANY ACT OF THE DIRECTORS.

Annotation 23. Once a quorum is present, the action of a majority of the directors present at the meeting will constitute valid acts of the board. ARIZ. REV. STAT. ANN. § 10-040 (Supp. Pamphlet 1975). However, the articles of incorporation or bylaws may require a higher than majority vote. *Id.* Such a provision may be useful in situations where a director or group of directors desires veto power: if the number required is high enough, the assent of such director or group of directors will be necessary for valid corporate action.

[24] 7.8. COMMITTEES. [Here insert the designation of any specific committees of the board of directors to be inserted in the articles of incorporation and the restrictions, if any, on their duties and powers, for example, THERE SHALL BE AN EXECUTIVE COMMITTEE OF THE BOARD OF DIRECTORS, WHICH SHALL CONSIST OF THREE (3) MEMBERS OF THE BOARD OF DIRECTORS APPOINTED BY THE BOARD AT THE ANNUAL MEETING OF THE BOARD OF DIRECTORS EACH YEAR. THE EXECUTIVE COMMITTTEE SHALL HAVE ALL OF THE POWERS AVAILABLE TO THE BOARD OF DIRECTORS BY LAW AND PURSUANT TO THESE ARTICLES OF INCORPORATION AND BYLAWS EXCEPT THAT IT SHALL NOT HAVE AUTHORITY TO (i) DECLARE DIVIDENDS OR DISTRIBUTIONS, (ii) APPROVE OR RECOMMEND TO SHAREHOLDERS ACTIONS OR PROPOSALS REQUIRED BY THIS ACT TO BE APPROVED BY SHAREHOLDERS, (iii) DESIGNATE CANDIDATES FOR THE OFFICE OF DIRECTOR, FOR PURPOSES OF PROXY SOLICITATION OR OTHERWISE, OR FILL VACANCIES ON THE BOARD OF DIRECTORS OR ANY COMMITTEE THEREOF, (iv) AMEND THE BYLAWS, (v) APPROVE A PLAN OF MERGER NOT REQUIRING SHAREHOLDER APPROVAL, (vi) REDUCE EARNED OR CAPITAL SURPLUS, (vii) AUTHOR-

IZE OR APPROVE THE REACQUISITION OF SHARES UNLESS PURSUANT TO A GENERAL FORMULA OR METHOD SPECIFIED BY THE BOARD OF DIRECTORS, OR (viii) AUTHORIZE OR APPROVE THE ISSUANCE OR SALE OF, OR ANY CONTRACT TO ISSUE OR SELL, SHARES, OR DESIGNATE THE TERMS OF A SERIES OF A CLASS OF SHARES. ALL ACTIONS TAKEN BY THE EXECUTIVE COMMITTEE WITHIN THE SCOPE OF ITS AUTHORITY AS SET FORTH IN THIS ARTICLE SHALL BE VALID AND BINDING UPON THIS CORPORATION AS THOUGH SUCH ACTION HAD BEEN TAKEN BY THE BOARD OF DIRECTORS.]

Annotation 24. The Act permits the board of directors to designate committees of board members to undertake some of the board's duties. ARIZ. REV. STAT. ANN. § 10-042 (Supp. Pamphlet 1975). See text & note 211 *supra*. These committees may be formed pursuant to resolution without authority from the articles of incorporation or bylaws, but may also be authorized by provision in either of those documents. ARIZ. REV. STAT. ANN. § 10-042 (Supp. Pamphlet 1975). Normal corporate practice is to include standing committees in the bylaws of the corporation and to create ad hoc committees by resolution. The directors not on a certain committee may be entitled to place greater reliance on an official committee provided for in the articles or bylaws than on one created by resolution. This factor will be of importance should a dispute arise as to whether a director exercised the care and diligence required of him by his position. See, for example, the discussion of proposed amendments to the Model Act in *1975 Report, supra* note 8, at 501-12.

There may be situations where provision for such committees in the articles, rather than the bylaws, would be advisable. If the committee structure is provided for in the articles of incorporation, any change will require shareholder vote. In contrast, if the committee structure is contained in the bylaws, it can be changed by amendment of the bylaws, normally a function of the board of directors unless specifically reserved to the shareholders. *See* ARIZ. REV. STAT. ANN. § 10-027 (Supp. Pamphlet 1975). If committees are established by the board, they can be altered, changed, or eliminated by action of the board. Thus, establishment of committees in the articles is advisable, for instance, where the number of committee members or the powers of the committee have been negotiated among the persons establishing the corporation in advance of its formation. Model article 7.8 provides for the creation of a standing committee for a specific continuing purpose. The restrictions on the authority of the committee set forth in the model

are taken from a proposal to amend section 42 of the Model Act made by the ABA Committee on Corporate Laws. *1975 Report, supra* note 8, at 509-12.

[25] 7.9. NO ACTION WITHOUT MEETING. NO ACTION REQUIRED BY LAW OR THESE ARTICLES OF INCORPORATION TO BE TAKEN BY THE BOARD OF DIRECTORS AT A MEETING MAY BE TAKEN WITHOUT A MEETING DULY CALLED IN ACCORDANCE WITH THE REQUIREMENTS OF THE BYLAWS AND ACTUALLY HELD.

Annotation 25. Any action required to be taken by the board of directors at a meeting may be taken by unanimous written consent without a meeting. ARIZ. REV. STAT. ANN. § 10-044 (Supp. Pamphlet 1975). See text & note 210 *supra.* Section 10-044 provides, however, that this rule may be changed by the articles of incorporation. Model article 7.9 suggests such a change. The purpose of the prior Arizona common law rule requiring a meeting before the board could take any valid action was to ensure actual discussion of any issue before action was taken thereon. The discussion process supposedly permits minds to be changed and people to be persuaded from positions they might otherwise hold. Ames v. Goldfield Merger Mines Co., 227 F. 292, 301-02 (W.D. Wash. 1915); 2 W. FLETCHER, *supra* note 205, § 392. However, if all of the directors have agreed on an action, the advantages of discussion are minimal. Accordingly, the Model Act as adopted in Arizona does not require the empty formality of an actual meeting in such circumstances and reflects the existing practice in many close corporations of having minutes, signed and approved by all directors, prepared of meetings that have not in fact occurred. The purpose of requiring meetings as in model article 7.9 would be to meet the fears of one or more directors that their opinions may not be sufficiently taken into account if the dominant or majority directors are allowed to formulate action and then present it to the others as an accomplished fact.

[26] 8. INCORPORATORS. THE INCORPORATORS OF THE CORPORATION ARE: [here insert the name and address of each, for example,

A.B. LAWYER
FORD LAW BUILDING
PHOENIX, ARIZONA 85123

C.D. SECRETARY
FORD LAW BUILDING
PHOENIX, ARIZONA 85123].

ALL POWERS, DUTIES AND RESPONSIBILITIES OF THE INCORPORATORS SHALL CEASE [here insert the time when the incorporators' duties will cease, for example, AT THE TIME OF DELIVERY OF THESE ARTICLES OF IN-

CORPORATION TO THE ARIZONA CORPORATION COMMISSION FOR FILING, or, IMMEDIATELY FOLLOWING ADOPTION OF THE INITIAL BYLAWS OF THE CORPORATION].

Annotation 26. There must be at least two incorporators, ARIZ. REV. STAT. ANN. § 10-053 (Supp. Pamphlet 1975), and the name and address of each must be stated in the articles. *Id.* § 10-054(A)(11). Incorporators must be "persons capable of contracting," *id.* § 10-053, but need not be otherwise associated with the corporation, nor need they be residents of Arizona. Corporations are considered persons pursuant to Arizona law, ARIZ. REV. STAT. ANN. § 1-215(24) (1975), and as such may act as incorporators if they have the power so to act. Arizona corporations have been given this power by ARIZ. REV. STAT. ANN. § 10-004(A)(15) (Supp. Pamphlet 1975).

The sole duty of the incorporators is to sign and file the articles of incorporation. They may, however, also adopt the initial bylaws of the corporation. *Id.* § 10-027. No method for adoption is suggested, and if the incorporators are to adopt bylaws, they should do so prior to the first meeting of the board of directors mandated by section 10-057. The last sentence of model article 8 clarifies the time at which all duties and responsibilities of the incorporators cease.

[27] 9. DISTRIBUTIONS FROM CAPITAL SURPLUS. THE BOARD OF DIRECTORS OF THE CORPORATION MAY, FROM TIME TO TIME, DISTRIBUTE ON A PRO RATA BASIS TO ITS SHAREHOLDERS OUT OF THE CAPITAL SURPLUS OF THE CORPORATION A PORTION OF ITS ASSETS, IN CASH OR PROPERTY.

Annotation 27. Model article 9 allows distributions of the type usually referred to as distributions in partial liquidation of the corporation. It permits distributing assets to shareholders in situations where the corporation does not possess sufficient earned surplus to permit dividends of the amount desired. This type of distribution may also be treated differently from a dividend by the distributee shareholders for tax purposes. INT. REV. CODE of 1954, §§ 331(a)(2), 346. Such distributions can be made without provision in the articles of incorporation, but advance approval by a majority of the outstanding shares of each class of stock, voting or nonvoting, would then be required. ARIZ. REV. STAT. ANN. § 10-046(A)(2) (Supp. Pamphlet 1975).

Whether permitted by the articles or approved by shareholders, the distribution must comply with the restrictions of section 10-046(A). The corporation must not be rendered insolvent by the distribution; all cumulative dividends accrued must be paid first; the assets

remaining after distribution must be at least enough to pay the liquidating value of all preference shares; and the nature of the distribution must be disclosed to the shareholders receiving the distribution.

This type of distribution is frequently used in so-called "spin-off" transactions to distribute to shareholders of a corporation the shares of a wholly owned subsidiary. Such a distribution may now require registration under the Securities Act of 1933. See 17 C.F.R. § 231.4982 (1975); SEC Securities Act Release No. 33-4982 (July 2, 1969).

[28] 9.1. DIVIDENDS FROM DEPLETION RESERVES. THE BOARD OF DIRECTORS MAY FROM TIME TO TIME DECLARE AND CAUSE THE CORPORATION TO PAY CASH DIVIDENDS FROM THE DEPLETION RESERVES ESTABLISHED BY THE CORPORATION.

Annotation 28. Model article 9.1 can be used only by corporations engaged in the exploitation of wasting assets, as authorized by ARIZ. REV. STAT. ANN. § 10-045(A)(2) (Supp. Pamphlet 1975). This section was garbled by typographical errors in printing and should be corrected by proposed legislation. *See* discussion note 267 *supra.* The comparable section of the Model Act, which limits distribution of dividends from depletion reserves to corporations engaged in the business of exploiting natural resources, provides:

> If the articles of incorporation of a corporation engaged in the business of exploiting natural resources so provide, dividends may be declared and paid in cash out of the depletion reserves, but each such dividend shall be identified as a distribution of such reserves and the amount per share paid from such reserves shall be disclosed to the shareholders receiving the same concurrently with the distribution thereof.

MODEL ACT § 45(b). Without the permitted provision in the articles of incorporation, the board of directors will be restricted in the payment of cash dividends to the normal sources, that is, earned surplus and—if permitted by the articles—distributions, but not dividends, from capital surplus. These limitations normally would not allow the cash resulting from the sale of extracted natural resources to be distributed to shareholders until the corporation was dissolved, because most extractive corporations charge depletion against profits, thereby making it unavailable for dividends under the normal rule. *Id.*, Comment ¶ 2. It is possible that the lack of such a provision until now has been a factor in the decision of all the major mining corporations operating in Arizona to incorporate elsewhere.

[29] 9.2. REDUCTION OF DEFICITS. THE CORPORATION MAY APPLY ANY PART OR ALL OF ITS CAPITAL SURPLUS TO THE REDUCTION OR ELIMINATION

OF ANY DEFICIT ARISING FROM LOSSES, HOWEVER INCURRED, BUT ONLY AFTER FIRST ELIMINATING THE EARNED SURPLUS, IF ANY, OF THE CORPORATION BY APPLYING SUCH LOSSES AGAINST EARNED SURPLUS AND ONLY TO THE EXTENT THAT SUCH LOSSES EXCEED THE EARNED SURPLUS, IF ANY, AND ONLY UPON THE AFFIRMATIVE VOTE OF THE HOLDERS OF [here insert the majority required, for example, A MAJORITY] OF THE ISSUED AND OUTSTANDING VOTING STOCK OF THE CORPORATION AT A MEETING DULY AND PROPERLY NOTICED AND HELD.

Annotation 29. Frequently the capital account of a corporation will show a substantial amount of capital surplus (original capital contributions in excess of par or stated value) as well as large accumulated losses. The Act permits the board of directors by resolution to offset the one against the other, after first eliminating earned surplus, unless the articles provide otherwise. ARIZ. REV. STAT. ANN. § 10-070(C) (Supp. Pamphlet 1975). Model article 9.2, permitting the offset to be made only with shareholder approval, illustrates one way in which the articles can provide otherwise.

[30] 10A. INDEMNIFICATION OF OFFICERS, DIRECTORS, EMPLOYEES, AND AGENTS. THE CORPORATION SHALL INDEMNIFY ANY PERSON WHO INCURS EXPENSES BY REASON OF THE FACT HE OR SHE IS OR WAS AN OFFICER, DIRECTOR, EMPLOYEE, OR AGENT OF THE CORPORATION. THIS INDEMNIFICATION SHALL BE MANDATORY IN ALL CIRCUMSTANCES IN WHICH INDEMNIFICATION IS PERMITTED BY LAW.

10B. INDEMNIFICATION OF OFFICERS, DIRECTORS, EMPLOYEES, AND AGENTS. SUBJECT TO THE FURTHER PROVISIONS HEREOF, THE CORPORATION SHALL INDEMNIFY ANY AND ALL OF ITS EXISTING AND FORMER DIRECTORS, OFFICERS, EMPLOYEES, AND AGENTS AGAINST ALL EXPENSES INCURRED BY THEM AND EACH OF THEM, INCLUDING BUT NOT LIMITED TO LEGAL FEES, JUDGMENTS, PENALTIES, AND AMOUNTS PAID IN SETTLEMENT OR COMPROMISE, WHICH MAY ARISE OR BE INCURRED, RENDERED, OR LEVIED IN ANY LEGAL ACTION BROUGHT OR THREATENED AGAINST ANY OF THEM FOR OR ON ACCOUNT OF ANY ACTION OR OMISSION ALLEGED TO HAVE BEEN COMMITTED WHILE ACTING WITHIN THE SCOPE OF EMPLOYMENT AS DIRECTOR, OFFICER, EMPLOYEE, OR AGENT OF THE CORPORATION, WHETHER OR NOT ANY ACTION IS OR HAS BEEN FILED AGAINST

THEM AND WHETHER OR NOT ANY SETTLEMENT OR COMPROMISE IS APPROVED BY A COURT. INDEMNIFICATION SHALL BE MADE BY THE CORPORATION WHETHER THE LEGAL ACTION BROUGHT OR THREATENED IS BY OR IN THE RIGHT OF THE CORPORATION OR BY ANY OTHER PERSON. WHENEVER ANY EXISTING OR FORMER DIRECTOR, OFFICER, EMPLOYEE, OR AGENT SHALL REPORT TO THE PRESIDENT OF THE CORPORATION OR THE CHAIRMAN OF THE BOARD OF DIRECTORS THAT HE OR SHE HAS INCURRED OR MAY INCUR EXPENSES, INCLUDING BUT NOT LIMITED TO LEGAL FEES, JUDGMENTS, PENALTIES, AND AMOUNTS PAID IN SETTLEMENT OR COMPROMISE IN A LEGAL ACTION BROUGHT OR THREATENED AGAINST HIM OR HER FOR OR ON ACCOUNT OF ANY ACTION OR OMISSION ALLEGED TO HAVE BEEN COMMITTED BY HIM OR HER WHILE ACTING WITHIN THE SCOPE OF HIS OR HER EMPLOYMENT AS A DIRECTOR, OFFICER, EMPLOYEE, OR AGENT OF THE CORPORATION, THE BOARD OF DIRECTORS SHALL, AT ITS NEXT REGULAR OR AT A SPECIAL MEETING HELD WITHIN A REASONABLE TIME THEREAFTER, DETERMINE IN GOOD FAITH WHETHER, IN REGARD TO THE MATTER INVOLVED IN THE ACTION OR CONTEMPLATED ACTION, SUCH PERSON ACTED, FAILED TO ACT, OR REFUSED TO ACT WILLFULLY OR WITH GROSS NEGLIGENCE OR WITH FRAUDULENT OR CRIMINAL INTENT. IF THE BOARD OF DIRECTORS DETERMINES IN GOOD FAITH THAT SUCH PERSON DID NOT ACT, FAIL TO ACT, OR REFUSE TO ACT WILLFULLY OR WITH GROSS NEGLIGENCE OR WITH FRAUDULENT OR CRIMINAL INTENT IN REGARD TO THE MATTER INVOLVED IN THE ACTION OR CONTEMPLATED ACTION, INDEMNIFICATION SHALL BE MANDATORY AND SHALL BE AUTOMATICALLY EXTENDED AS SPECIFIED HEREIN; PROVIDED, HOWEVER, THAT NO SUCH INDEMNIFICATION SHALL BE AVAILABLE WITH RESPECT TO LIABILITES UNDER THE SECURITIES ACT OF 1933, AND, PROVIDED FURTHER, THAT THE CORPORATION SHALL HAVE THE RIGHT TO REFUSE INDEMNIFICATION IN ANY INSTANCE IN WHICH THE PERSON TO WHOM INDEMNIFICATION WOULD OTHERWISE HAVE BEEN APPLICABLE SHALL HAVE UNREASONABLY REFUSED TO PERMIT THE CORPORATION, AT ITS OWN EXPENSE AND THROUGH COUNSEL OF ITS OWN CHOOSING, TO DEFEND HIM OR HER IN THE ACTION.

Annotation 30. Statutory indemnification by a corporation of its officers, directors, employees, and agents is permitted, but not required, by ARIZ. REV. STAT. ANN. § 10-005 (Supp. Pamphlet 1975), even if the articles of incorporation and bylaws are silent. This indemnification is extremely broad, permitting the corporation to indemnify its officers, directors, employees, and agents for expenses, including attorneys' fees, judgments, and amounts paid in settlement, incurred in direct actions by aggrieved third parties, in actions by the corporation itself, and in actions brought derivatively in the name of the corporation.

Section 10-005(F) provides that the statutory indemnification is not exclusive, and model articles 10A and 10B accordingly are intended to expand the available indemnification. Model article 10A makes the statutory indemnification mandatory on the corporation. Model article 10B goes farther by requiring indemnification if a finding of good faith is made by the board of directors, even though such board consists of other persons also parties to the same action. See text & note 107 *supra.* It will be noticed that both model articles 10A and 10B apply to all existing and former officers, directors, employees, or agents of the corporation. Each corporation should adjust the model chosen to those classes of persons to whom the indemnification provision of the articles is to apply.

The statutory section further permits other rights to indemnification through bylaws, agreement, vote of shareholders or disinterested directors, or otherwise. This would appear to permit provisions such as model articles 10A and 10B to be contained in bylaws rather than in articles. However, it may be advisable to include such provisions in the articles in order to give them added strength in the event of a future court challenge. See discussion note 105 *supra.* Because section 10-005 is merely the grant of corporate power and not a mandated corporate activity, the power of the corporation to indemnify officers, directors, employees, and agents can be restricted. If such restriction is desired, it should be expressly articulated in the corporate articles. ARIZ. REV. STAT. ANN. § 10-054(A)(12) (Supp. Pamphlet 1975).

[31] 11. REPURCHASE OF SHARES. THE BOARD OF DIRECTORS OF THE CORPORATION MAY, FROM TIME TO TIME, CAUSE THE CORPORATION TO PURCHASE ITS OWN SHARES TO THE EXTENT OF THE UNRESERVED AND UNRESTRICTED EARNED AND CAPITAL SURPLUS OF THE CORPORATION.

Annotation 31. A corporation may purchase or otherwise deal in its own capital stock. ARIZ. REV. STAT. ANN. § 10-006(A) (Supp.

Pamphlet 1975). As is generally true with corporate action, the board of directors has the unilateral authority to cause the corporation to purchase, take, receive, or otherwise acquire, hold, own, pledge, transfer, or otherwise dispose of its own shares. There is, however, one exception to this authority granted to the board of directors. If, in purchasing the shares, the earned surplus of the corporation is exhausted and it is necessary or desirable that capital surplus of the corporation be used, shareholder approval is necessary unless the articles of incorporation specifically grant the power to the board of directors. *Id.* Model article 11 grants this power, allowing any legal repurchase by a corporation of its own shares to be authorized by the board of directors without shareholder approval. Repurchase by the corporation of its own shares is not permitted in any event, however, if the stated capital of the corporation would be impaired as a result. *Id.* § 10-006(D).

The Act makes a distinction between repurchase by a corporation of its shares and redemption of shares. The term redemption refers only to situations where shares of stock may be repurchased by the corporation at the instance of the corporation or of the shareholders, as the case may be, because of provisions in the articles of incorporation authorizing such redemption. Different statutory requirements exist as to each of these methods for corporate acquisition of its own stock. See *id.* §§ 10-067 to -068. Any type of shares, whether stated to be redeemable or not, may be repurchased by the corporation pursuant to the authority of section 10-006(A).

Section 10-006(C) lists four situations in which the restrictions of the section do not apply: purchases of shares of the corporation for the purpose of eliminating fractional shares, collecting or compromising indebtedness to the corporation, paying dissenting shareholders entitled to payment for their shares, and effecting the retirement of redeemable shares by redemption or by purchase at not to exceed the redemption price. If any of these four conditions is met, it is permissible for the purchase to impair capital and to be authorized by the board of directors even though the articles do not contain model article 11.

[32] 12. DIVIDENDS. THE BOARD OF DIRECTORS MAY AUTHORIZE THE PAYMENT OF DIVIDENDS TO THE HOLDERS OF SHARES OF ANY CLASS OF STOCK PAYABLE IN SHARES OF ANY OTHER CLASS.

Annotation 32. The Act permits dividend payments to be made in stock of a class different from the class held by those receiving the dividend only in two circumstances: if the articles of incorporation so provide, such a stock dividend may be authorized by the board of direc-

tors; or if the articles are silent on the subject, approval of the holders of a majority of the shares in which the dividend is to be paid as well as authorization by the board of directors is required. ARIZ. REV. STAT. ANN. § 10-045(A)(5) (Supp. Pamphlet 1975). Model article 12 eliminates the need for such shareholder approval. Conversely, if it is desired that no dividends be paid in stock of one class to holders of another class of stock, such a prohibition can validly be placed in the articles.

[33] 13. PROVISIONS RELATING TO SHAREHOLDERS—QUORUM. A QUORUM AT A MEETING OF SHAREHOLDERS SHALL CONSIST OF [here insert requirement desired, for example, FOUR-FIFTHS (4/5) OF THE SHARES ENTITLED TO VOTE, REPRESENTED IN PERSON OR BY PROXY].

Annotation 33. The Act provides that a quorum at a shareholders meeting shall be a majority of the shares entitled to vote, unless the articles of incorporation provide otherwise. ARIZ. REV. STAT. ANN. § 10-032 (Supp. Pamphlet 1975). In the organization of a corporation with a small number of shareholders, it may be desirable to raise the quorum requirement to a percentage so high that any one of the shareholders has veto power on corporate action. On the other hand, in the case of a corporation with many shareholders in which it may be difficult to secure a quorum, a reduction of the quorum requirement may be beneficial. A corporation with an equal number of shares held by persons in two locations, may desire the quorum requirement to be lowered to permit meetings to be validly held in one of those localities without requiring the other group's presence.

[34] 13.1. BYLAWS. THE POWER TO ALTER, AMEND, OR REPEAL THE BYLAWS OR ADOPT NEW BYLAWS SHALL BE VESTED IN THE SHAREHOLDERS, WHO MAY AMEND, ALTER, REPEAL, AND REPLACE BYLAWS BY THE AFFIRMATIVE VOTE OF THE HOLDERS OF [here insert the majority required, for example, A MAJORITY] OF THE ISSUED AND OUTSTANDING VOTING SHARES OF THE CORPORATION.

Annotation 34. The Act provides that the original bylaws of the corporation shall be adopted by the incorporators or by the initial board of directors. ARIZ. REV. STAT. ANN. § 10-027 (Supp. Pamphlet 1975). The power to alter, amend, or repeal the bylaws or adopt new bylaws, however, may be vested in the shareholders by the articles of incorporation. If no contrary provision is made in the articles, that power will vest in the board of directors.

[35] 13.2. VOTING REQUIRED. THE AFFIRMATIVE VOTE OF THE HOLDERS OF [here insert the majority required, which must be greater than a majority, for example, FOUR-FIFTHS (4/5)] OF THE STOCK OF THE CORPORATION PRESENT AND VOTING AT A MEETING AT WHICH A QUORUM IS PRESENT SHALL BE REQUIRED FOR ANY ACT OF THE SHAREHOLDERS.

13.3. VOTING BY CLASSES. ANY MATTER PRESENTED TO THE SHAREHOLDERS FOR VOTE SHALL NOT BE ADOPTED EXCEPT WITH THE AFFIRMATIVE VOTE OF THE HOLDERS OF [here insert the majority required which must be a majority or greater, for example, A MAJORITY] OF EACH CLASS OF ISSUED AND OUTSTANDING STOCK VOTING SEPARATELY AS A CLASS.

Annotation 35. Once a quorum is present, the action of a majority of the shares then represented will constitute valid shareholder action. ARIZ. REV. STAT. ANN. § 10-032 (Supp. Pamphlet 1975). Provision in the articles of incorporation, however, can instead require either voting by classes for all matters, a higher than majority vote, or both, to validate action by shareholders. Section 10-143 specifically permits a higher than majority vote to be required by articles on any issue. See text & note 282 *supra.* Model article 13.2 should be used where the proportion necessary for valid shareholder action is to be greater than the majority vote required by the Act. Model 13.3 not only provides for raising the requirement to a greater than majority vote if desired but also requires voting by classes in all matters. Such a provision for class voting is not usually needed unless the rights accorded separate classes need special protection.

[36] 13.4. DISSENTING RIGHTS. THE RIGHT OF A SHAREHOLDER TO DISSENT FROM A PLAN OF MERGER OR CONSOLIDATION OR A SALE OR EXCHANGE OF ALL OR SUBSTANTIALLY ALL OF THE PROPERTY AND ASSETS OF THE CORPORATION NOT MADE IN THE USUAL AND REGULAR COURSE OF ITS BUSINESS SHALL NOT BE ABRIDGED BY THE REGISTRATION ON A NATIONAL SECURITIES EXCHANGE OF THE SHARES OF STOCK HELD BY THE SHAREHOLDERS OR THE FACT THAT THE CLASS OF STOCK HELD BY THE SHAREHOLDER IS HELD BY MORE THAN TWO THOUSAND (2000) SHAREHOLDERS.

Annotation 36. The Act provides dissenters' rights to shareholders when corporations merge, consolidate, or sell all or substantially all of their assets. ARIZ. REV. STAT. ANN. §§ 10-080 to -081 (Supp. Pamphlet 1975). The statutory scheme permits the dissenting share-

holder to have his or her shares valued and requires the corporation to purchase those shares at that value. The statutory scheme is complex and must be followed precisely.

The statute withholds dissenters' rights, however, from shareholders of a class of stock that is registered on a national securities exchange or is held by more than 2000 shareholders. *Id.* § 10-080(C). See text & notes 177-80 *supra.* In such cases it is presumed that a ready over-the-counter securities market exists enabling a disenchanted stockholder to sell his or her shares easily at the market value. Dissenters' rights in such circumstances can nevertheless be provided by the articles and may be necessary to protect adequately shareholders. A shareholder who dissents from a merger or sale is, under the statutory scheme, entitled to the fair market value of his or her shares, a figure which may or may not correspond to the actual market value. Furthermore, even though the shares are registered or widely held, they may be in insufficient demand to enable a shareholder to sell. Failure of a widely held corporation to include model article 13.4 in its articles, therefore, may substantially diminish the rights of shareholders. Such curtailment of shareholder rights is particularly likely in the event the controlling shareholders are attempting to eliminate the minority interests in the corporation—the "going private" phenomenon. Corporations whose shares are not widely held and which therefore do not fall within the statutory exclusion need not utilize 13.4.

[37] 14. DURATION. THE EXISTENCE OF THIS CORPORATION SHALL TERMINATE [here insert the length of the duration of the corporation or the date of its termination, for example, TWENTY-FIVE (25) YEARS AFTER ITS CERTIFICATE OF INCORPORATION IS ISSUED BY THE ARIZONA CORPORATION COMMISSION, or, ON JANUARY 1, 2001].

Annotation 37. Each corporation shall have perpetual succession unless a limited period of duration is stated in its articles of incorporation. ARIZ. REV. STAT. ANN. § 10-004(A)(1) (Supp. Pamphlet 1975). See text & note 82-84 *supra.* Model article 14 is intended for use in those rare circumstances where a limited period of duration is desired. If it later becomes necessary to extend the corporation's existence, the articles of incorporation can be amended either to change the expiration date or to eliminate the section. ARIZ. REV. STAT. ANN. § 10-058(B)(2) (Supp. Pamphlet 1975). A corporation may make such amendment within 5 years after the expiration of its period of duration, and thereby revive its corporate existence. *Id.* § 10-105.