

Memorandum 76-33

Subject: Study 77.140 - Nonprofit Corporations (Bankruptcy Reorganizations and Arrangements)

Chapter 14 (Sections 1400-1403) of the new General Corporation Law concerns bankruptcy reorganizations and arrangements. Sections 4400-4405 of the old General Corporation Law (the predecessor provisions to Chapter 14) were applicable to nonprofit corporations under Section 9002. The staff draft of a chapter relating to bankruptcy reorganizations and arrangements attached to this memorandum is a revision of the provisions applicable to business corporations.

The purpose of Chapter 14 in the General Corporation Law is to make clear that the persons in charge of a corporation during reorganization or arrangement (generally under the Bankruptcy Act) have broad general powers which may be exercised as if exercised by unanimous action of the board of directors and the shareholders (members). Chapter 14 also makes some procedural provisions concerning filing of amendments, changes, and agreements with the Secretary of State and limits the rights of dissenting shareholders.

The important law, however, is contained in the Bankruptcy Act and Rules and the decisions interpreting that body of law. We do not intend to consider the substance of federal law here, except to note the general nature of the most important federal provisions. Arrangement refers to Chapter XI of the Bankruptcy Act and involves either extensions of time for the payment of debts or a scaling down of debts (composition). Arrangement is a voluntary proceeding and may affect only unsecured debts. Reorganization, primarily under Chapter X of the Bankruptcy Act, is more formal than arrangement. A plan of reorganization may affect secured debts. In the case of business corporations, reorganization may be voluntary or involuntary; there are no cases on whether a nonprofit corporation can be forced into reorganization (or straight bankruptcy proceedings).

There is some question about the importance of Chapter 14 in the business corporation laws. One commentator notes the existence of state provisions making inapplicable the normal requirements of action by the board of directors or shareholders, dissenters' rights, and the like,

and queries "whether such state law requirements could in any event interfere with a plan of reorganization valid under federal law." (H. Henn, Corporations § 389 (2d ed. 1970).) Furthermore, the provisions concerning reorganization and arrangement under the bankruptcy laws are much less important to nonprofit corporations than to business corporations. Oleck reports that use of Chapter XI (arrangements) by nonprofit organizations is "very uncommon," and that in

actual practice, non-profit corporations rarely employ Chapter X reorganization. Complex and specialized, it is intended primarily for the use of large business corporations whose stock is widely held by investors. [H. Oleck, Non-Profit Corporations, Organizations, and Associations §§ 319-320 (3d ed. 1974).]

Despite these factors which might suggest that provisions like Chapter 14 could just as well be omitted from the General Nonprofit Corporation Law, the staff has decided to recommend that they be included in order to preserve the parallelism between the two bodies of law, to continue the filing provision, and to avoid the doubt which might result from the omission of such provisions.

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

OUTLINE

CHAPTER 14. BANKRUPTCY REORGANIZATIONS AND ARRANGEMENTS

- § 6400. General power to carry out reorganization or arrangement under federal law
- § 6401. Specific powers
- § 6402. Filing of certificates and agreements
- § 6403. Execution and verification of certificates and agreements; contents
- § 6404. Filing fees
- § 6405. Applicability of chapter

CHAPTER 14. BANKRUPTCY REORGANIZATIONS AND ARRANGEMENTS

§ 6400. General power to carry out reorganization or arrangement under federal law

6400. A domestic nonprofit corporation with respect to which a proceeding has been initiated under any applicable statute of the United States, as now existing or hereafter enacted, relating to reorganizations or arrangements of corporations, has the power to carry out a plan of reorganization or arrangement and the orders of the court entered in the proceeding without further action by its board or members. Such power, whether exercised by a trustee or a majority of trustees, a master, or other representative appointed by the court or by the officers of the nonprofit corporation designated by the court, shall be exercised with like effect as if exercised by unanimous action of the board and members of the nonprofit corporation.

Comment. Section 6400 continues the substance of subdivision (a) of Section 1400 of the General Corporation Law and former Section 4400. The language has been simplified, but no substantive change is intended.

Chapter 14 continues the substance of former Sections 4400-4405 relating to bankruptcy reorganizations and arrangements which were applicable to nonprofit corporations as provided in former Section 9002.

§ 6401. Specific powers

6401. Without limiting the generality or effect of Section 6400, a nonprofit corporation subject to such reorganization or arrangement proceedings may do any of the following:

- (a) Amend its articles.
- (b) Alter, amend, or repeal its bylaws.
- (c) Constitute or reconstitute its board and name, or constitute or appoint directors and officers in place of or in addition to all or some of the directors or officers then in office.
- (d) Make any other amendment, change, alteration, or provision authorized by this division.
- (e) Dissolve, transfer all or part of its assets, or merge as permitted by this division, except that no member shall have any statutory dissenter's rights.
- (f) Change the location of its principal executive office or remove or appoint an agent to receive service of process.
- (g) Authorize and fix the terms, manner, and conditions of the issuance of bonds, debentures, or other obligations.
- (h) Lease its property and franchises to any business or nonprofit corporation, if permitted by law.

Comment. Section 6401 is the same in substance as subdivision (a) of Section 1400 of the General Corporation Law and former Section 4401. However references to "shareholders" have been changed to "members" and references to shares of stock have been deleted.

§ 6402. Filing of certificates and agreements

6402. A certificate of any amendment, change, alteration, or dissolution or an agreement of merger made by a nonprofit corporation pursuant to Section 6400 or 6401, executed as provided in Section 6403, shall be filed and upon filing is effective in accordance with its terms and the provisions of this chapter.

Comment. Section 6402 is substantively identical to subdivision (a) of Section 1401 of the General Corporation Law and the first sentence of former Section 4402. The second sentence of former Section 4402, which provided for the filing of a certified copy of the certificate in counties where the corporation holds real property and where the principal office is located, has not been continued.

§ 6403. Execution and verification of certificates and agreements;
contents

6403. A certificate, agreement, or other instrument filed pursuant to Section 6402 shall be signed and verified by the person described in Section 6400 who is authorized by the court to exercise the powers of the nonprofit corporation. The certificate, agreement, or other instrument shall state that provision for the making of the certificate, agreement, or instrument is contained in an order of a court having jurisdiction of a proceeding under a statute of the United States for the reorganization or arrangement of corporations, and shall identify the order.

Comment. Section 6403 is the same in substance as subdivision (b) of Section 1401 of the General Corporation Law.

§ 6404. Filing fees

6404. The fee for filing any paper pursuant to this chapter is the same as the fee payable by nonprofit corporations that are not in reorganization or arrangement proceedings upon the filing of a like paper.

Comment. Section 6404 is the same in substance as Section 1403 of the General Corporation Law.

§ 6405. Applicability of chapter

6405. This chapter ceases to apply to a nonprofit corporation upon the entry of a final decree in the reorganization or arrangement proceeding closing the case and discharging the trustee or trustees, if any, whether or not jurisdiction may be retained thereafter by the court for limited purposes which do not relate to the consummation of the plan.

Comment. Section 6405 is substantively identical to Section 1402.