

***Rhode Island Business Corporations Act
July 1, 2005***

The Revised Rhode Island Corporation Act ("The Act") became effective as of July 1, 2005. The revisions are extensive and are intended to provide a more user friendly version of the Act. This summary addresses several major changes to the Act and is not intended as an exhaustive survey.

1. Filing

The Act makes it permissible to file documents electronically or through facsimiles in order to avoid duplication and to provide a user friendly submission mechanism.

2. Articles of Incorporation

The Act reduces the amount of information required in the Articles of Incorporation. The Articles of Incorporation must include the name of the entity, the number of shares, the registered agent, and the name and address of the incorporators.

3. Shareholder's Preemptive Rights

Unless expressly provided for in the Articles of incorporation, for entities incorporated after July 1, 2005, a preemptive right to acquire shares has been eliminated statutorily. To create a preemptive right a simple statement in the Articles of Incorporation will suffice. The Act further limits the nature and scope of a preemptive right.

4. Indemnification

Court ordered indemnification now preempts a corporation's right to and ability to (or not to) indemnify directors. A corporation may provide broader indemnification than required by the Act if such provisions are included in the articles of incorporation.

5. Mergers

Shareholder approval is no longer necessary for mergers if:

- A. Each shareholder will hold the same number of shares after the merger takes place;
- B. The merger does not amend the articles of incorporation; and
- C. The securities issued in connection with the merger represent less than 20% of the total voting power of all outstanding shares entitled to vote for directors of the corporation after the merger.

Shareholder dissent is limited to actions that are the result of fraud or material misrepresentation, or actions that fail to comply with the Act, the articles of incorporation or the bylaws of the corporation.

6. The Duty of Care

Directors must discharge their duties with the care that a person in a like

position would reasonably believe appropriate under similar circumstances. This is an objective standard which replaces the prior subjective standard.

7. Books and Records

The office of legal counsel is now an authorized repository for books and records. Directors, shareholders, and holders of voting trust certificates have the right to inspect books and records, thus eliminating the 6 month holding period for stockholders and the 5% requirement for trusts.

8. Shares

The revised corporate statute modifies a number of aspects of corporate shares:

A. Acquire, Dispose and Cancel: The Board of Directors by resolution may acquire, dispose of and cancel shares at any time unless the Articles of Incorporation provide otherwise. Corporations cannot purchase or redeem redeemable or other reacquired shares if it would cause insolvency, or cause assets to be less than total liabilities.

B. Par Value: Unless otherwise stated in the Articles of Incorporation, shares that are silent as to par value have a par value of one cent per share for purpose of a statute or regulation imposing a tax or fee based on capitalization. Eliminated is the requirement that par value shares subject to option rights must have a price not less than the par value of such shares.

C. Issuance and Consideration: Contracts for future services as well as promissory notes are permitted consideration for shares. A corporation may escrow the shares used as consideration for future services or notes until they are fully performed, and if not performed they may cancel the shares.

D. Ownership Restrictions: The Act restricts transfer or ownership of shares to permit corporations to qualify as a real estate investment trust or investment company.

9. Distributions to Shareholders

There is no distinction between the payment of dividends and distributions from capital surplus. There is a distinction between distribution of shares and distributions other than shares.

No distribution other than shares may be made if the corporation would either be insolvent or total assets would be less than the sum of total liabilities plus the amount needed to satisfy preferential rights in the even of dissolution.

Distributions do not have to be paid from unreserved unrestricted capital surplus, shareholder votes are not required to authorize distributions, and full payment of preferential dividends prior to distribution is not required.

The Act adds the business judgment reliance principal permitting board members to rely on financial statements based on reasonable accounting principles when determining if non-share distributions are prohibited.

10. Actions by Shareholders

The revised statute completely revamps the process for shareholder actions.

A. Standing: Shareholders must fairly and adequately represent the corporation's interests.

B. Demand: Derivative actions may not be commenced until written demand has been made the corporation and 90 days has expired from the date the demand was made, unless the corporation has previously rejected the

demand or irreparable injury will result from waiting.

C. Stay of Proceeding: The court may stay a proceeding if the corporation commences an inquiry into the issue made by demand.

D. Motion to Dismiss: A court shall dismiss a derivative proceeding upon (1) a majority vote of independent directors present at a Board meeting so long as they constitute a quorum, or (2) a majority vote of a committee of at least 2 or more independent directors appointed by majority vote of independent directors present at a board meeting, whether or not such independent directors constitute a quorum, or (3) a decision by a panel of independent persons appointed by the court upon motion of the corporation, after such independent directors, committee or panel has determined in good faith after reasonable inquiry that the derivative proceeding is not in the corporation's best interests.

E. Independent: None of the following causes by itself causes a director to be considered not independent: (1) nomination of a director who is also a defendant in the proceeding; (2) naming of the director as a defendant; or (3) approval by the director of the challenged act if the act did not result in personal benefit to the director.

F. Rejection of Demand: If a derivative proceeding is commenced after a demand rejection, the complaint must show that the majority of the directors were not independent, or the determination was not made in good faith.

G. Discontinuance or settlement: A derivative action may not be discontinued or settled without court approval.

H. Payment of Expenses: The Act expands the scope of expenses and adds provisions for payment of the derivative expenses by the corporation if

they receive substantial benefit, payment by plaintiffs to defendants if the proceeding was commenced without reasonable cause or for improper purpose, and payment by either party of the others expense where any aspect of pleading, motion, or paper is not well grounded in fact or interposed for improper purpose.

11. Close Corporations

Close corporations are not required to hold annual shareholder meetings if so stated in the articles of incorporation. An annual meeting can be called if one or more shareholders deliver written notice requesting a meeting at least 30 days prior to the meeting date as stated in the bylaws.

12. Conclusion

The Revised Rhode Island Business Corporations Act is an update of Rhode Island corporate law. The Act places Rhode Island Corporate Law on par with other jurisdictions around the country. The purpose of this article is to give the user an overview of the most significant changes to The Act in order to convey a basic understanding as to how The Act will affect corporations in Rhode Island in the coming years.

Sources:

- 1. R.I. Gen. Laws § 7-1.2 (Supp. 2004).*
- 2. R.I. Gen. Laws § 7-1.1*
- 3. Getting Down to Business: A Pocket Guide to the Revised Rhode Island Business Corporation Act, 10 Roger Williams U. L. Rev. 719 (2005).*

This outline is not a complete analysis and may not be relied upon as legal advice. Please contact Gary R. Pannone, Esquire for further consultation at 401-824-5115 or send an email to him at gpannone@pld-law.com.