



FARM COMMONS

Farmer's Guide to C Corporations

LAST UPDATED:
December 1, 2015

FIRST PUBLISHED:
December 1, 2015

**By: Rachel Armstrong, Erin Hannum,
Laura Fisher and Lisa Schlessinger**

www.farmcommons.org

DISCLAIMER: This guide does not provide legal advice or establish an attorney client relationship between the reader and author. Always consult an attorney regarding your specific situation.

TABLE OF CONTENTS

SECTION 1: C Corporation Fundamentals

C Corporations at a Glance	4
Introduction	5
Basic Characteristics of the C Corporation	5
How the C Corporation Compares to the LLC and the S Corporation	9
Forming a C Corporation	11
Implementing Good Business Practices for Your C Corporation	17

SECTION TWO: Going Deeper into C Corporations

Introduction	24
Checklist: Creating a Farm Business as a C Corporation	25
C Corporation Sample Bylaws with Annotations	41
Sample Annual Shareholder Meeting Minutes with Annotations	59



This product was developed with support from the Sustainable Agriculture Research and Education (SARE) program which is funded by the U.S. Department of Agriculture -- National Institute of Food and Agriculture (USDA-NIFA). Any opinions, findings, conclusions or recommendations expressed within do not necessarily reflect the view of the SARE program or the U.S. Department of Agriculture. USDA is an equal opportunity provider and employer.



FARM COMMONS

Section 1: C Corporation Fundamentals

DISCLAIMER: This guide does not provide legal advice or establish an attorney client relationship between the reader and author. Always consult an attorney regarding your specific situation.

AT A GLANCE CHART: C CORPORATION

	General Concept	Terminology
C Corporation Terminology	Name	“Farm Name, Inc”
	Owners / Investors are called:	“Shareholders” or “Stockholders”
	Persons who make management decisions are called:	The “Board of Directors” are responsible for making key decisions, the “Officers” are responsible for the day-to-day management
	Creation document is called:	“Articles of Incorporation”
	Organizing Document is called:	“Bylaws”
	An owner’s investment in the company is called:	“Equity Investment”
	An ownership share is called:	“Shareholder Equity,” or “Shares”
	A payment of the company’s profits to the owners is called:	“Dividend”
	Is there Personal Liability?	Limited to a shareholder’s investment
	How many participants can you have?	One or more, unless elect S corporation tax status*
	Are annual meeting required?	Required
	Are different shareholder classes allowed?	Allowed, unless elect S corporation tax status*
	Is an EIN necessary?	Required
Who files the tax return?	Entity files an income tax return and pays corporate taxes; individuals also pay taxes on any dividends they receive from the corporation. Option to elect S corporation federal tax status*	
C Corporation with S Corporation Federal Tax Status	How many participants can you have?	Maximum 100 persons; all must be U.S. citizens and all must be human beings, estates, tax exempt entities, or certain qualified trusts
	Are different shareholder classes allowed?	Not allowed
	Who files the tax return?	Pass-through, but entity must file informational Form 1120S with the IRS, distribute schedule K-1 to each owner, and file all schedule K-1s with the IRS

“Most know the C corporation as just “corporation.” Nowadays, the letter “C” is often included as a prefix to prevent confusion between the S corporation and the B corporation.”

See chapter 4 on S corporations and chapter 5 on B corporations for more details on each (part 2, chapters 4 and 5 in the *Farmer’s Guide to Choosing a Business Entity*).

Introduction

The C corporation is the ordinary, traditional corporation. Most know it as just “corporation.” Nowadays the letter “C” is often included as a prefix to prevent confusion, as there’s been a recent rise of new corporate forms such as the S corporation federal tax status (where the “S” stands for small) and the B corporation (where the “B” stands for benefit).

This section explores significant aspects of the C corporation, how the entity is formed, and what needs to be done to maintain it. The following section, Going Deeper into C Corporations, gives you some tools to help you navigate the process of creating and operating a C corporation. It includes a checklist for creating a C corporation as well as sample bylaws and annual meeting minutes with explanations.

Basic Characteristics of the C Corporation

C corporations protect personal assets from business liabilities

Forming a C corporation, or any business entity, is a fundamental way to help protect personal assets of the owners from the farm business’ liabilities. The C corporation offers farm operation owners peace of mind in keeping the risks of their business separate from their personal assets. As long as corporate formalities are upheld, the shareholders—which is the C corporation term for the business owners—are not at risk of losing personal assets if another person or business secures a court judgment against the shareholder. The shareholders can, however, lose up to the amount they have invested in the company. Whatever cash, property, or other resources a shareholder invests in the C corporation is considered her equity investment. It reflects her risk or stake in the business so to speak. The potential gain is a return on the investment in the form of profits based on her ownership percentage or equity in the company. The potential loss is losing all that she invested. No more, no less. That’s because once a shareholder transfers ownership of the cash or property invested, it is thereafter owned by the C corporation itself.

Running a small farm operation is not easy, and there’s no guarantee it will succeed. Equipment breakdown, crop failure, unpredictable weather, or a number of other events could lead to no profit or even a loss in a given season. If the farm doesn’t turn a profit and uses up all the company’s money or capital in the process, the owners of the C corporation won’t even get their equity investment back.

There's nothing left. Taking it a step further, let's say the C corporation had taken out a loan to pay for some farm equipment and is no longer able to pay on its debt. It won't be long before the creditors come knocking on the farm business's door. However, given the C corporation protects shareholders from personal liability, the shareholders do not have to worry so much that creditors will come knocking on their doors and snatch up their lake house or their boat if the farm business starts going south. The creditor could still lay claim to any remaining assets of the C corporation, but nothing more. This is one advantage of creating a business entity such as a C corporation.

The C corporation protection on personal assets requires adherence to certain principles

“The rules and procedures a C corporation must follow vary from state to state; however they all require the business owners to follow some fundamental principles.”

In return for this privilege, state corporation statutes require business owners to follow certain rules and procedures. Each state has its own corporation statute, which establishes what is required to form and maintain a C corporation in that state. The rules and procedures a C corporation must follow vary from state to state; however, they all require the business owners to follow some fundamental principles.

C corporations require a strict governance structure: shareholders, directors and officers

All state C corporation statutes require a very strict governance structure, which includes having shareholders, a board of directors, and officers. Each of these titles carries its own roles and responsibilities.

Shareholders are those who contribute assets—or an equity investment—to fund the farm operation. They are the owners. They generally have little say or right to run the the day-to-day operations of the company. However, they get to elect the board of directors and have the right to remove directors as they wish. The board of directors are elected by the shareholders each year at the annual meeting. The directors may or may not be shareholders themselves. The directors have high-level responsibilities for running the business, including making certain big decisions such as whether the company should take on a major financial liability like a loan to buy farmland, start a new business segment like value added products, or sell off a significant part of the farm operation. Another key role of the board of directors is to appoint the corporation's officers. Like the directors, the officers may or may not be directors or shareholders. The officers of a corporation are the ones on the ground, running the day-to-day operation of the business and making management decisions. The

officers include the President (or Chief Executive Officer–CEO), Vice President (or Chief Operations Officer–COO), Treasurer (or Chief Financial Officer–CFO), and Secretary. One person can hold multiple positions, or even all of them. This might sound silly, but acting with these separate hats is an essential formality that must be upheld to maintain the integrity of a C corporation entity. We’ll discuss each of these positions in a bit more detail later.

What if you have just one or a few business owners?

It is of note that one person can fill all the roles of the shareholder, board, and officer(s). If this were the case, that person would make decisions in different capacities. For example, let’s say a mother and daughter decide to form a business entity for an organic goat cheese operation they’ve gone in on together. They call it Momma Earth Farms, Inc. It’s just the two of them, and they need to figure out how they will fill all of these roles. Let’s say they both invest some cash as an equity investment, so they are both shareholders. As shareholders, they elect the board of directors. They elect each other! Then, as directors, they decide who will be the officers. Together they agree that Mom will serve as President and Treasurer and Daughter will serve as Vice President and Secretary. As officers, they now get to decide day-to-day matters such as how many goats to have, what types of cheese to make, and things like that. Any big decisions such as getting a substantial loan to buy farmland would need to be made by them as directors. If they decide the company needs more money for a new milking parlor, they would act as shareholders when writing a personal check to the business as an equity investment.

Be sure the farm operation has enough money and keep the C corporation’s financial affairs separate from the shareholders’ financial affairs

In addition, like the LLC, the owners of the farm operation must also abide by certain principles to maintain the C corporation’s protection from personal liability. If the farm business does not follow certain standards, then the courts can reach around the C corporation’s personal liability shield and allow creditors to access the individual owners’ personal assets. Just as for an LLC, the two essential ways to protect the shareholders’ personal assets are to adequately capitalize the C corporation and keep the C corporation’s financial affairs separate from the owners’ personal financial affairs.

////////////////////////////////////
“Two essential ways to protect the shareholders’ personal assets are to adequately capitalize the C corporation and keep the C corporation’s financial affairs separate from the owners’ personal financial affairs.”
////////////////////////////////////

First, as a basic rule of thumb, a company is adequately capitalized if it can make due on its debts, or pay its monthly bills so to speak. Anything less would be undercapitalized. In other words, if you start incurring more debt than you can reasonably pay off based on estimated revenue, the C corporation will be considered undercapitalized. As a result, the shareholders may be personally liable to cover the business' debt. The directors and officers need to be smart about how much debt they allow the C corporation to take on.

Courts are also able to access personal assets if the shareholders fail to keep the business separate from their personal affairs. This includes commingling funds such as drawing on business assets to pay for personal expenses or not keeping separate business and personal bank accounts. The take away here is that just as business assets are available for business liabilities, personal assets are available for personal liabilities--each needs to remain separate and not be commingled. Be sure to keep separate bank accounts, credit cards, and accounting records for the business entity and keep these all distinct from the personal financial affairs of the shareholders. For example, do not use the business' assets to pay a shareholder's personal bills, including credit card bills and rent payments.

Also keep in mind that even if the C corporation is properly maintained, some creditors may require shareholders to personally guarantee farm debt. Creditors know that if there's nothing left in the business entity there will be nothing left for them. What this means is that creditors may require the shareholders to commit to loan payments as an individual not just as a shareholder to the C corporation. Shareholders will have to negotiate whether and to what extent a personal guarantee is required with creditors on a case-by-case basis.

C corporations do not substitute for insurance or reduce the likelihood of liabilities

Forming a C corporation, or any business entity, is not a substitute for insurance. Some farmers mistakenly believe creating an C corporation reduces the likelihood of liability. Creating a C corporation does nothing to change the landscape of a farm's potential liability. It only limits the assets available to satisfy that liability, should it materialize, to business assets. All the farm's assets are entirely available to anyone with a successful claim against a C corporation. Good liability insurance provides the farm with a defense in court and a source of funds to pay out on a court claim if it is successful. Farm Commons strongly urges any farm business, no matter what business entity it adopts, to maintain adequate insurance coverage.

////////////////////////////////////
“Be sure to keep separate bank accounts, credit cards, and accounting records for the business entity and keep these all distinct from the personal financial affairs of the shareholders.”
////////////////////////////////////

How the C Corporation Compares to the LLC and the S Corporation

Should I choose an LLC or a C corporation?

Flexibility v. Formality

This is a good question that many farmers ask. For all intents and purposes, the liability protection offered by an LLC and a corporation are the same. However, in practice, the statutory flexibility of the LLC with respect to how the entity is governed may lead many to mismanage it, degrading that protection. For example, LLC statutes do not require separate directors and officers with such defined roles and responsibilities, though an LLC can certainly appoint individuals with such authority. Also, most state LLC statutes do not require the owners to hold an annual meeting. State C corporation statutes require the owners to hold an annual shareholders meeting, which provides an opportunity for everyone to review the financials and elect next year's board of directors. The board of directors must also meet annually to appoint the officers. The formality of annual meetings helps keep the board and the officers in check. As stated above, liability protection can be lost through mismanagement, including undercapitalization or the commingling of business and personal financial affairs. The formalities of a C corporation, including its strict governance structure and required annual meetings, may make mismanagement less likely. However, to non-lawyers, the formalities involved with a C corporation can look like too much pageantry. To many, the formalized processes of decision-making and authority are unwelcome. To these folks, the statutory obligations of a C corporation are a detraction. They may prefer an LLC.

Newness v. Tradition

On the other hand, while the LLC has been around for over 35 years and is a very stable entity in the eyes of the law, the reality is that C corporations have been around a lot longer. The courts' interpretation and application of laws governing corporations are very well detailed. Now, much of this case law or precedent on corporations is being applied to LLCs, which lends further credibility to the LLC entity. Nevertheless, some farmers feel more comfortable with the traditional C corporation. This is also why some folks set up their LLC exactly like a corporation—with a similar governance structure and required annual meetings—even though it's not required. They want to rest assured that they will have the benefits of the stable, thorough body of law controlling corporate governance.

“Unlike for LLCs, state C corporation statutes require the owners to hold annual shareholder meetings.”

Ultimately, the decision may come down to personal inclination and comfort with what they are used to seeing in their family, town, or region.

Financing options

Some other factors to consider in the choice between an LLC or C corporation relate to financial issues. First, if a farm operation anticipates it will need to raise a large amount of capital that exceeds what they can or want to get a loan for and is more than what the initial farm operation owners can afford, it may be beneficial to form a C corporation. This will preserve the option to raise capital from venture capitalists and angel investors. These are individuals with a significant amount of money that invest in small businesses in hopes of making a profit. Venture capitalists and angel investors typically prefer the formal C corporation structure and may even require it before making an investment. Also, if you think that your company will go public by advertising and offering ownership shares to the public at large through what's called an indirect public offering (IPO), then the law requires a C corporation structure. Conducting an IPO is a very costly and time-consuming process that involves very complex securities law. It is typically done by multi-million dollar companies like Google and Amazon, for example. But maybe your farm operation has the next big idea! Of note, both a C corporation and an LLC can advertise and offer ownership interests directly to members of the public with whom they have a connection—like customers or suppliers. This is called a DPO. However, the LLC's choices on what it can offer through a DPO are a bit more limited than the C corporation.

////////////////////////////////////
“If you think your farm operation will go public by advertising and offering ownership shares to the public at large, then the law requires a C corporation structure.”
////////////////////////////////////

These financing issues are beyond the scope of this chapter. The point here is that these types of considerations can certainly come into play in the decision of which entity to choose, especially if the farm operation is considering a creative financing option to raise additional capital at the outset or in the future.

Tax implications

Finally, there are significant tax differences between a C corporation and an LLC. The LLC is a pass-through entity, so the entity itself does not have to pay federal income taxes. Instead the individual members report their share of the LLC's income on their individual tax returns. The C corporation, on the other hand, is subject to double taxation. The entity first pays corporate tax on the business' taxable income, and then the owners have to pay taxes on any earnings or profits they receive from the company. Granted, the individual owners are taxed

at the dividend tax rate, which is currently less than for ordinary income. But the total taxes paid on business income for some small business owners can be astronomically high. Many small farm operations see this as a huge pitfall of a C corporation and a reason to form an LLC.

Should I choose a C corporation or an S corporation?

If you decide you prefer the assurance of the formalities and stability of the C corporation, you still have an option to circumvent the double taxation dilemma. Unlike the LLC or the C corporation, the S corporation is actually not a separate entity created at the state level. The S corporation is simply a federal tax status issued by the IRS. In effect, either an LLC or a C corporation can become an S corporation for federal tax purposes. Basically, the S corporation tax status allows the entity to be taxed as a pass-through entity, just like an LLC. It also provides some potential tax benefits related to self employment taxes that neither the C corporation nor LLC provide on their own right.

With S corporation tax status, if the corporation has just a single shareholder, the entity would be taxed as if it was a sole proprietorship. If there are multiple shareholders, it would be taxed as if it was a general partnership. Each shareholder would report the company's earnings and pay applicable taxes through his or her own individual tax return. Accordingly, the farm operation owners will end up paying different tax rates depending on their overall financial situation. This could be very advantageous to certain farm business owners.

The IRS requires an entity to meet certain criteria to be eligible for the S corporation tax status and to complete annual tax documents to maintain the status. To be eligible, the entity must have less than 100 owners, all owners must be U.S. citizens, no owners can be for profit entities such as an LLC or a C corporation (they all must be human beings, estates, tax exempt entities, or certain qualified trusts), and the entity can only have one class of owners. Review the S corporation chapter in this Guide for more details on eligibility criteria, annual tax form requirements, and how to elect S corporation tax status.

Forming a C Corporation

Now that we've provided some basic background and characteristics of the C corporation, we can dive into the process of creating one. This includes appointing the initial directors, filing the articles of incorporation, creating the bylaws,

“If you decide you prefer the assurance of the formalities and stability of the C corporation, you still have an option to circumvent the double taxation dilemma by electing S corporation federal tax status.”

See chapter 4 on S corporations for more details on the criteria and requirements for electing S corporation tax status.

appointing the officers, and issuing shares to the initial shareholders. This section should be read in conjunction with the Creating a C Corporation Checklist that is part of the Dive Deeper section of this chapter.

Who can form a C corporation?

Most state corporation statutes allow C corporations to be created by a single person or multiple people. There are no restrictions on how many people may participate. Another business entity, such as an LLC or a trust, could be a shareholder.

“One of the first steps a new C corporation will take is to appoint the members of its board of directors.”

Appoint the initial directors, the deciders of big decisions

One of the first steps a new C corporation will take is to appoint the members of its board of directors. This is a bit tricky, as it needs to happen before the entity is actually formed. Usually, initial directors are identified in the “articles of incorporation,” which is the formation document filed with the state. Often the initial directors are selected in the interim by the person who takes the initial step of incorporating the business (sometimes called the “incorporator”). Once the corporation is up and running, directors are typically elected by shareholders at annual meetings.

The directors do what their name says: they direct the corporation along its path and make big decisions that impact the financial affairs of the company. This includes approving contracts and agreements, making decisions about significant purchases such as land or expensive farm equipment, and approving overarching corporate policies including employee handbooks and such. The directors are also who decide when and whether to pay dividends to the shareholders. Dividends are payments made to the shareholders when the business makes a profit. Dividends reflect the shareholder’s return on investment, or bang for their buck. The handing out of profit to the shareholders is not automatic. It’s ultimately a significant business decision. That’s why it’s left for the directors to decide. The directors very well may decide that it’s in the best interest of the farm operation to keep all or a part of the profits in the company. This way they can better grow the farm business, like investing in more equipment or capital, such as a greenhouse or a new parcel of farmland.

The board of directors is also fundamentally on the legal hook, so to speak, for the corporation’s actions. First and foremost, the board of directors is accountable

to the shareholders. They also have what's called a "fiduciary duty" to the corporation, which includes both a duty of care and a duty of loyalty. A duty of care is to diligently act on behalf of the best interests of the corporation. For example, if the farm operation wants to buy a piece of property, the directors need to really look into their options. Are there sufficient water rights, what is the going rate for a similar parcel, what's the quality of soil like, etc. They need to take special care that the decision they make is not at all arbitrary and is in the best interest of the corporation. A duty of loyalty is to put the interest of the corporation above their own personal interest. So, for example, if a director owns a piece of land that he wants to sell to the corporation, she needs to realize that this presents a conflict of interest. As a landowner, she has an interest to sell the property at the highest price possible. As a director of the corporation that is a potential buyer, she needs to get the best deal possible. In all actuality, to fully abide by her duty of loyalty, she should really refrain from voting on the matter. The same goes for a director or officer making a decision on her salary. It can be helpful to keep all of these things in mind when appointing your directors.

////////////////////////////////////
"You can have as many or as few directors as you want. The ideal number usually depends on the size of the farm operation."
////////////////////////////////////

How many directors should there be? You can have as many or as few as you want. The ideal number usually depends on the size of the farm operation. A small farm operation might just have one director, who also serves as the sole owner or shareholder and plays all the roles of the officers. A larger farm operation may have more directors. It's generally recommended to have an odd number, as that will ensure there are no deadlocks on voting. Many recommend having fewer than 10 directors, as it can be unwieldy to manage the opinions of a lot of directors. However, it's entirely up to you.

Draft and file the articles of incorporation with your state

Once the initial board of directors is appointed, the next step in creating a C corporation is filing the "articles of incorporation." This is done at the state level, usually through the state's Secretary of State office. Many states provide a form that can be easily downloaded or even filed online. Other states simply list the information required, in which case you can create your own document that includes this information. An Internet search for "file a corporation and [your state's name]" should bring up a form and more information. Each state charges different fees, which vary between \$25 to \$1000. Once your articles of incorporation and fee are filed and processed, you'll get a confirmation from from the filing agency that your C corporation is now recognized as an official business entity in your state.

A few key terms you'll need to know when filing the articles of incorporation are the "registered agent" and the "incorporator." The registered agent is basically the person that will receive "service of process," which is an official notice that the C corporation is being sued. It does not in any way mean this individual is liable or responsible for the outcome. It simply means that the agent is required to pass on the notice to the other shareholders of the corporation so that the corporation is officially on notice. Some businesses select a shareholder to be the agent. Others choose to work with one of the many independent businesses that provide agent of process services for a small fee. An incorporator is an individual who organizes and arranges for the articles of incorporation to be filed with the Secretary of State. The incorporator must verify that all the included information is true and correct, and sign the articles of incorporation. This could be a shareholder. It is often the entity's attorney.

Annual Fee: Note that most states also require an annual fee. It's a good idea to find out upfront whether your state charges an annual fee and, if so, how much. The amount of the fee may be a factor in your decision on whether to form a C corporation.

////////////////////////////////////
"In addition to the articles of incorporation, state corporation statutes also require corporations to have bylaws."
////////////////////////////////////

Draft the bylaws

In addition to the articles of incorporation, state corporation statutes also require corporations to have bylaws. The bylaws set the ground rules amongst the shareholders, directors, and officers for how the corporation must be governed. They include baseline procedural guidelines for corporate governance. State corporation statutes often set specific parameters for certain governance matters that are to be included in bylaws, such as when and how shareholders must be informed about annual meetings, items that must be voted on at annual meetings, how voting must take place, and restrictions on who can decide what, etc. These details can vary from state to state. So, if you decide to draft your own bylaws, be sure to check your state's corporation statute or consult with an attorney who is familiar with your state's statute to ensure that your bylaws are fully in compliance with state law. The bylaws don't need to be filed with the state. However, they must be officially adopted by the board of directors. For more information about bylaws and examples of common language used with explanations, see the Sample Bylaws for Momma Earth Farms, Inc. included in the Dive Deeper section of this chapter.

While many states do not require LLCs to create a governing document (the operating agreement) all states require C corporations to adopt a governing document (the bylaws).

Hold an organizational meeting

Adopt bylaws

After you have filed the articles of incorporation and drafted the bylaws, the board of directors should hold an organizational meeting. At this meeting, the directors should first officially adopt the bylaws. All directors should have read them and agreed to them by this point. It's important to document the board's approval of the bylaws in the minutes of the organizational meeting.

Elect officers

Next, the directors should elect officers, if they haven't already done so. The officers are responsible for the day-to-day management of the company. The board is responsible for appointing them and designating their salary. Officer positions include a president (or chief executive officer, CEO), a Vice President (or chief operations officer, COO), a treasurer (or chief financial officer, CFO), and a secretary. The President has ultimate responsibility for the corporation's activities. The president reports to the board of directors; however, he or she generally has the authority to sign off on contracts and other legally-binding actions on behalf of the corporation. The vice president is optional, depending on the size of the farm operation. Typically, a vice president is charged with managing the corporation's day-to-day affairs. There can be multiple vice presidents if there are multiple segments of the business. Or, if the business is small and streamlined, this role is oftentimes filled by the president. The treasurer is responsible for the corporation's financial matters, including keeping the farm's accounting system up to date and in check. The secretary is in charge of maintaining the corporation's records, documents, and "minutes" from shareholder and board meetings. Note that a director can serve as an officer and that one person can serve multiple offices. Like directors, the officers owe a fiduciary duty to the company (i.e. a duty of care and a duty of loyalty). Be sure to keep this in mind when deciding who the initial officers will be.

Approve issuance of stock

The directors should also officially approve the issuance of shares or stock in the company. Let's say that the articles of incorporation specified that the corporation is authorized to issue 10,000,000 shares. The board could decide to issue all the shares to the founding shareholders. Or, they could decide to set some shares aside, say 1,000,000 for future investors or stock option benefits for employees.

////////////////////////////////////
“The officers are responsible for the day-to-day management of the company.”
////////////////////////////////////

These are decisions that have financial implications for the company and should be made in consultation with a corporate attorney or a tax accountant.

Decide whether to elect S corporation federal tax status

In addition, if the corporation will be an S corporation (i.e. elect S corporation federal tax status), the directors should approve the election at this time.

Be sure to follow the voting parameters set forth in your bylaws when voting on these matters. Also, written minutes must be kept for this organizational meeting and all meetings held by the board of directors and shareholders to evidence what happened should a dispute or issue ever arise.

“Before engaging in any business activity as the corporation, the corporation needs to formally issue the shares authorized by the board to the founding shareholders.”

Issue stock

Before engaging in any business activity as the corporation, the corporation needs to formally issue the shares authorized by the board to the founding shareholders. This is the formal process of dividing up the ownership in the company. It is also required by law if you are doing business as a corporation. Again, issuing stock can be complicated. Farm Commons strongly recommends that you have an attorney that is familiar with corporate and securities law handle the stock issuance for you.

First, both federal and state securities laws may apply. Unless you qualify for an exemption at both the federal and state level, you will have to file a securities registration. This process can be timely and expensive. Fortunately, most small farm operations will qualify for an exemption. For example, the Securities Exchange Commission (SEC) rules and most state securities laws provide a “private offering” exemption. This basically means that you’ll likely be exempt from securities filings if you don’t advertise investment opportunities in your company to the general public and you only have a small number of people investing that are actively participating in running the business. Be sure to confirm with your attorney whether this or any other exemption applies. Security filings can be very time consuming and expensive. The stakes are high if you do not comply, as you could face fines and potentially be required to give investments back in full to the shareholders.

When you’re ready to issue the actual shares to your founding shareholders, you’ll need to put the following in writing: the initial shareholders names and mailing addresses, the number of shares each shareholder will purchase, and how each shareholder will pay for her shares, which can be cash, property, and services (also known as “sweat equity”). Keep in mind that most states have a minimum amount

of stock that can be issued. Note also that if you plan on electing S corporation tax status, you can only issue one class of stock, which is generally common stock, meaning one vote per share. This information should be included in your bylaws.

Next, you can prepare and issue stock certifications. A stock certificate is a way to document stock ownership and is given to the shareholder. This step is not actually necessary, as most states no longer require corporations to issue actual stock certificates. However, shareholders have come to expect it and it provides another layer of evidence of who owns how many shares. If you do issue a stock certificate, states generally require that you include the following information on the face of the certificate: the name of the corporation, the state where the corporation was formed, the name and number of shares issued to the shareholder, and a signature authenticating the document. Finally, some states require that you file a “notice of stock transaction” with your state’s business agency or secretary of state. This is typically a simple form, but it’s important that you file it if it’s required. Otherwise you risk the state saying that the issuance of shares is invalid.

Create a shareholder agreement, if the shareholders want one

While shareholder agreements are not required, they can be useful to set forth specific terms that all shareholders must abide by and follow amongst each other. A shareholder agreement provides even more detail than the bylaws on how the corporation will be run. Shareholder agreements can be particularly important in closely held corporations, where the shares are held between a small group of people and are not offered to the general public. In addition, shareholder agreements can be a useful way to protect minority shareholders, who may fear that their voice will be overpowered on everything. For example, the shareholder agreement could require that certain decisions be agreed to by all the shareholders. Shareholder agreements also often include procedures for dispute resolution, which can help keep matters out of court, as well as restrictions to prevent unwanted parties or strangers from acquiring shares in the company.

“Shareholder agreements can be particularly important in closely held corporations, where the shares are held between a small group of people.”

Implementing Good Business Practices for Your C Corporation

Now that you’ve formed your C corporation (by filing the articles of organization) and have established the governing rules (by finalizing and officially adopting your bylaws), you now must follow through by acting like you have a separate business.

This means upholding good business practices by keeping your business affairs separate from your personal affairs, abiding by the provisions of your bylaws, filing applicable annual maintenance fees with the state, and filing your taxes.

Keep your business and personal financial affairs separate

It is essential that you maintain a clear and distinct level of separateness between the C corporation’s business affairs and each of your shareholder’s personal affairs. Primarily, this means maintaining separate bank accounts and accounting records. This also includes not paying your personal debts or bills with the business assets. Of course, shareholders can pay for legitimate expenses related to the C corporation with their personal funds so long as they account for and properly record these expenses and record them as business expenses. Be sure to keep all the receipts in case of an audit. The shareholder can either write these “business expenses” off on her individual tax return or she can request to be reimbursed directly by the C corporation. If the company reimburses the expense, then she cannot also write it off. That would be a sure way of abusing the integrity and separateness of the business entity!

Another key requirement for keeping the business affairs separate is to properly allocate assets to the C corporation. Any land, equipment, or other asset that is contributed to the C corporation as shareholder’s equity investment needs to be formally transferred over. Officially allocating assets in this way helps make absolutely clear who owns what. It also clarifies the extent of each shareholder’s liability if the farm operation turns sour. Recall that if the C corporation upholds good business practices, each shareholder’s liability extends only to the value of his or her equity investment. If the lines aren’t clear, the courts can reach around and grab more.

Follow your bylaws and hold annual meetings

Be sure to follow what the bylaws say, as well as any shareholder agreements should you decide to enter into them. Legally speaking, these are contracts that all the shareholders are now bound by. You should make copies, or make it available in electronic form, so that every shareholder, director, and officer has it and can refer to it as needed. Following the rules and procedures your bylaws set gives the business legitimacy in court.

For example, your bylaws should designate a general time and place for an annual shareholders meeting as well as specify particular requirements for how and when

“It is essential that you maintain a clear and distinct level of separateness between the C corporation’s business affairs and each of your shareholder’s personal affairs.”

to let shareholders know about the details of the meeting. Be sure to follow these procedures, otherwise anything that's conducted at a meeting could be deemed invalid by a court. You should take minutes to record what happened. The minutes don't have to be elaborate, just enough for the shareholders present to recall what was discussed and decided, and for anyone not present to understand what happened. A sample of minutes from a shareholder's meeting is included in the Dive Deeper section of this chapter for a guide.

Also, if you decide to make changes to your bylaws, you'll need to follow the procedure it sets for making amendments. If the shareholders or board of directors properly agree to an amendment, be sure to document it in the minutes.

It's a good idea to keep your bylaws, any shareholder agreements, as well as all meeting minutes and any amendments in one binder so that it is readily available. This also helps prove the legitimacy of your C corporation by showing you are taking the separate entity seriously. Whenever you have a doubt about what's required for making a decision, or how to deal with a specific scenario when it arises, refer to your bylaws or shareholder agreements for guidance.

////////////////////////////////////

“Most states require an annual fee to continue to operate as a C corporation. Be sure you pay this fee each year, on time.”

////////////////////////////////////

Pay your state's annual maintenance fees

This is simple, but it's amazing how many business entities fail to follow up. Most states require an annual fee to continue to operate as a C corporation. Be sure you pay this fee each year, on time. Otherwise, you could incur late fees. Or, at worse, your C corporation could be administratively dissolved. You would then have to start the whole process over again, which no farmer has time to do.

Designate your tax status

As a C corporation, you can choose to be taxed as a C corporation or an S corporation. While this guide is not intended to provide tax advice, we will provide a brief overview to help with basic understanding as you work with your accountant or tax attorney to decide what designation is best for your farm operation.

The default federal tax status for a C corporation is to pay corporate taxes. Basically, the farm operation will be taxed separately from the owners. Any profit remaining in the company at the end of its tax year will be taxed at corporate tax rates. If the corporation distributes profits to the shareholders, the shareholders will also have to report this as income on their individual tax returns. Many say this is disadvantageous, as the owners end up having to pay double taxes. First, they pay corporate taxes on the net earnings of the company and then they pay

“The S corporation tax status allows the C corporation to be taxed as a pass-through entity.”

For more more on S corporations see chapter 4 (part 2, chapter 4 of the *Farmer's Guide to Choosing a Business Entity*).

taxes on any profits they get from the corporation in the form of dividends.

Another option is to be elect the S corporation tax status with the IRS. It's simple to do, you just have to fill out and file IRS Form 2553 “Election by a Small Business Corporation.” The S corporation tax status allows the C corporation to be taxed as a pass-through entity, just like the LLC. Instead of the entity having to pay corporate taxes, all earnings of the company are reported by the shareholders on their individual tax returns in accordance with their equity share in the company. The shareholders then pay taxes the company's income based on their individual tax rate.

In addition, the S corporation tax status handles self-employment taxes slightly differently than any other entity. Basically, in addition to a “reasonable” salary that can be paid to the owners or shareholders of the farm operation, the owners can also receive income in the form of “distributions.” Distributions are taxed at a lower rate and are free from self-employment taxes including Social Security and Medicare taxation. This can equate to about 15% savings in federal taxes. Distributions can of course only be made if there are sufficient profits in your farm operation. Otherwise, your company will be considered undercapitalized. Recall that if this happens, the shareholders may be personally liable to cover the business' debt.

To be eligible for S corporation tax status, the entity has to meet certain criteria. In addition, while the C corporation doesn't have to pay taxes, it does have to distribute tax forms to the shareholders each year and file certain forms with the IRS, including Form 1120S. This is the informational tax document used to report the income, losses, and dividends of S corporation shareholders.

Deciding on salaries of owners

Farmers may be motivated to keep their salary as low as possible so that the remainder is taxed at a lower rate. If you elect S Corporation tax status, keep in mind that the IRS does not look fondly on artificially low salaries and can reclassify dividends as salary. The IRS will look at many different factors in determining what a reasonable salary should be. Anything above that could be reclassified and taxed as dividends. Factors the IRS will consider include the following:

- training and experience,
- duties and responsibilities,
- time and effort devoted to the business,

- dividend history,
- payments to non-shareholder employees,
- timing and manner of paying bonuses to key people,
- what comparable businesses pay for similar services, compensation agreements, and
- the use of a formula to determine compensation.

This begs the question, what is a reasonable salary for a farmer? Where do we draw the line? According to the Bureau of Labor Statistics, in 2014, the average annual income for supervisors of farms and farmworkers was \$47,540. If you own and run your own farm operation, which includes supervisory duties, the IRS may consider this as the baseline. Let's say an owner of an C corporation with net annual income of \$50,000 tried to claim that just \$20,000 of that was a reasonable salary in hopes of getting a tax break on the remaining \$30,000. You might have an uphill battle convincing the IRS that a farmer of similar skill and responsibilities could only reasonably expect \$20,000.

Tax designation choices for the C corporation

- Do nothing. The default will apply. The entity will be required to file and pay its own corporate taxes. The shareholders will have to report and pay taxes on any dividends they receive from the company.
- File IRS form 8832, "Entity Classification Election" and elect corporation and then file IRS tax form 2553 "Election by a Small Business Corporation." You will be taxed as an S corporation. The income of the corporation passes through to the shareholders, who each report and pay taxes based on their individual tax rate.

Note that this is simply for federal tax status. You will still need to pay any applicable corporate taxes in your state!

Fulfill your tax obligations

Once you decide on your tax designation and file the appropriate forms, you'll then need to be sure the entity and each of its shareholders fulfills the annual tax obligations. This includes distributing forms, filing forms, and, of course, paying taxes when due. The following provides a basic breakdown of what is required based on the tax status you choose for your farm operation. Again, Farm Commons

“Working with a tax expert will help guarantee you’re doing everything properly; it could also end up saving you money by finding ways to minimize your tax burden.”

strongly recommends that you seek guidance from your accountant or tax attorney come tax season. Tax law is very particular. Working with a tax expert will help guarantee you’re doing everything properly; it could also end up saving you money by finding ways to minimize your tax burden.

If you go with the default tax status, the C corporation will have to file Form 1120, the U.S. Corporation Income Tax Return, and pay its own taxes. In addition, the shareholders will each have to individually report and pay taxes on any dividends they receive.

If you elect to be taxed as an S corporation, you’ll have to file the annual Form 1120S with the IRS. This is an informational tax document used to report the income, losses, and dividends of S corporation shareholders. The entity itself will not have to pay taxes, as it passes through to the individual shareholders. In addition, the company will have to provide each of the shareholders with a schedule K-1. The schedule K-1 is similar to a W-2, the end of the year wage statement that employees receive from their employers. The schedule K-1 shows the self-employment income each of the shareholders receives from the company. The company must also submit a copy of schedule K-1 to the IRS for each shareholder. This allows the IRS to be sure that each shareholder is properly reporting any self-employment income he or she receives from the corporation.

Tax forms a C corporation must file and distribute based on tax status

- **C corporation status:** File Form 1120, the U.S. Corporation Income Tax Return, with the IRS and pay taxes as a corporation. Each shareholder will report and pay taxes on any income (i.e. salary and distribution of profits) he or she received from the entity on his or her individual income tax return.
- **C Corporation with S corporation tax status:** File Form 1120S with the IRS, which is purely informational. Distribute schedule K-1 to each shareholder and file schedule K-1 for each shareholder with the IRS. Each shareholder reports and pays taxes on the individual tax return for his or her share of the corporation’s income.

Maintain accurate accounting records

Finally, the business and all shareholders need to keep good records of the business’ financial affairs, including all receipts of business expenses in case of an audit. It’s also advisable that you use a reliable accounting system such as Quickbooks or hire an accountant to handle your accounting and taxes for you.



FARM COMMONS

Section 2: Going Deeper into C Corporations

DISCLAIMER: This guide does not provide legal advice or establish an attorney client relationship between the reader and author. Always consult an attorney regarding your specific situation.

Introduction and How to Use these Resources

With an initial decision in hand to form a C corporation, farmers need to know exactly what it takes to form one. How does a person set up the C corporation? What documents need to be filed and with who? What should be included in the bylaws? This section is filled with hands-on tools to help guide you through the process of creating and maintaining a C corporation as well as preparing your bylaws.

The **Checklist: Creating a C Corporation** sketches the basic process a farmer follows to form and organize a C corporation. It is designed to help farmers understand the big picture as they comply with the laws and gear their farm for success. It's best to start with the checklist to get a sense of all that will be required.

The **Bylaws for Momma Earth Farms Inc with Annotations** includes the foundational provisions that are particularly important to include in a C corporation's bylaws. The sample provisions serve as examples of the ways a farm operation organized as a C corporation may want to handle certain situations should they arise. Note that rather than simply adopting someone else's bylaws, including those provided here, it's best to take the time to think through the various issues and craft provisions that are best for your particular farm operation. The annotations to the bylaws provide some alternative ideas as well as questions to illicit the best response and result that is specific to your situation. Upon reviewing these bylaws and the annotations, you can take a crack at drafting your own bylaws using the sample provisions as a guide. Or, you can jot down some key notes and take them to an attorney who will then be able to efficiently draft up your bylaws. Either way, Farm Commons advises that you have an attorney familiar with the laws in your state look over your bylaws before they are finalized. This will ensure that they comply with your state's corporation statute and that there are no conflicting provisions within the bylaws, which will only lead to confusion down the road.

Finally, C corporations are required by law to hold annual meetings and to keep minutes to provide evidence of what happens in case an issue or dispute arises. Annual meetings offer an opportunity for the shareholders to get together to elect the upcoming year's board of directors, review the financials, and strategize. They also help foster open communication and engagement from the owners. The sample **Annual Shareholder Meeting Minutes with Annotations** included in this section illustrate how straightforward it is to take minutes. You can use these to guide you through the minute-taking process when you're holding your annual meetings.

“Rather than simply adopting someone else's bylaws, it's best to take the time to think through various issues and craft provisions that are best for your particular farm operation.”



Checklist: Creating a Farm Business as a C Corporation

With S Corporation Tax Status Option

Introduction

This checklist guides farmers who have made the careful decision to establish their farm operation as a C corporation. This checklist sketches the basic process a farmer follows to form and organize a C corporation at the state level. The C corporation entity can help farmers develop clear decision-making procedures, outline roles and responsibilities of the owners, plan an exit strategy, and more. It also provides a layer of protection over the owners' personal assets from the business' liability. Note that state corporate statutes vary on the specifics of how a C corporation must be organized and operated. Be sure to review your state's statute carefully. Given that these statutes vary from state to state, Farm Commons highly recommends that you work with an attorney to help you through the process.

“This checklist sketches the basic process a farmer follows to form and organize a C corporation at the state level.”

Many farm owners that form a C corporation at the state level also want to take advantage of the federal S corporation tax status. So, this checklist also outlines the steps needed to obtain and maintain the S corporation tax status with the federal IRS. Note that this step is optional. If you do not make the S corporation election, the IRS will treat the entity as a C corporation and the entity itself will have to pay corporate taxes at the federal level. Conversely, with the S corporation tax status, the entity's income is passed through to the shareholders or business owners for federal tax purposes. Each shareholder reports the business income and pays his or her share of taxes when filing the individual tax return. The S corporation also provides tax advantages related to self-employment income. However, the tax benefits of the S corporation come with a cost. The entity must meet certain criteria to be eligible and must abide by certain formalities to maintain the S corporation tax status. If you choose to make the S corporation election, be sure you meet and maintain the S corporation criteria and abide by the formalities.

“This checklist also outlines the steps needed to obtain and maintain the S corporation tax status.”

This checklist is designed to be used with our other resources provided in the C corporation and S corporation chapters of the *Farmer's Guide to Choosing a Business Entity*. It may be helpful to review those chapters first. This checklist and the accompanying explanations are intended to help farmers understand the big picture as they comply with the laws and gear their farm for success.

Summary Checklist

Decide and Prepare for the C Corporation

- Verify that a C corporation is the right entity for your farm business
- Settle on a name for your business and verify that your chosen name is available
- Prepare to allocate assets between business and personal ownership
- Select a registered agent
- Choose directors for the corporation

Form the C Corporation at the State Level

- Draft articles of incorporation
- File articles of incorporation

Organize and Fulfill Corporate Formalities

- Create bylaws
- Hold your first board of directors meeting
- Issue stock, create stock certificate, and create shareholder agreement if necessary
- Get an Employment Identification Number (EIN) with the federal IRS
- Obtain necessary licenses and permits from state and local agencies

Implement Best Practices for the C Corporation

- Follow the bylaws
- Allocate assets between personal and business ownership accounts
- Document relationships for personal assets used for farm purposes
- Update websites, brochures, invoices, order forms and other materials with the “C corporation” (or “S corporation”) designation, if required
- Hold annual shareholder and director meetings
- Keep meeting minutes and maintain records of corporate decisions
- Establish a risk management plan
- Keep accurate and up-to-date accounting records for tax purposes

- Make note of and follow any annual obligations such as when, where, and how to file your annual report or fee with the state

Optional: Elect S Corporation Tax Status

- Verify that electing S corporation tax status is right for the farm operation
- File IRS form 2553
- Distribute and file S corporation tax forms and file and pay state taxes

Checklist with Explanations

Decide and Prepare for the C Corporation

- Verify that a C corporation is the right entity for your farm business

Although C corporations are a popular and wise choice for many farm businesses, each farm should do their homework. Consider your state’s filing fees and annual fees, the level of risk faced by the farm business, whether financing is affected, and how farm partners feel about it before creating a C corporation. The decision is not necessarily complicated, but it should be intentional.

- Settle on a name for the business

Choosing a name is a very significant step. The name helps create an identity for your business, your product, and all that you represent as a farm operation. It’s also a legal consideration. Most states prohibit two businesses from registering the same business name in that state. In addition, if you choose the same name as another business already in operation, that business may demand that you stop using their name. If this problem comes up after your operation has been around a few years, changing your name will likely confuse customers. And, it’s sad to lose the name you’ve grown to love! To keep this from happening, you’ll need to choose a name that isn’t already in use.

First, check state and federal databases of trademarks and trade names. Each state’s business entity registration agency maintains a searchable online database of business names or “trade names.” The United States Patent and Trademark Office (USPTO) has a searchable online database for registered federal trademarks. A basic Internet search will point you in the direction of these databases. Although a farm should not automatically assume that federally registered names are unavailable, consider it a red flag. Be sure you get more information and consult a trademark

“Consider your state’s filing fees and annual fees, the level of risk faced by the farm business, whether financing is affected, and how farm partners feel about it before creating a C corporation.”

attorney before choosing a name already registered in the federal database. You can do a basic Internet search for existing businesses with the same name.

Finally, you may want to check if your preferred website address is available and even register that domain name. You can register your preferred domain name on websites like GoDaddy or DreamHost. Also of note, most state corporation statutes require that the name of a C corporation include the words “Incorporated” or the abbreviation “Inc” and not use the terms of other entities such as non-profit or LLC, as this could confuse the public.

□ Prepare to allocate assets between business and personal

“Owners need to decide which assets are personal and which are business. If assets are used for the farm, they should likely be farm assets.”

The essence of a C corporation is that the business is distinct from its owners.

Accordingly, owners have to follow through with that distinction in practice.

This means that the owners need to decide which assets are personal and which are business. For farms, the ownership of land can be a delicate decision. Many farmers prefer to keep the land under personal ownership and lease their personal land to the farm business. If you decide to go this route, be sure you enter an official lease with the corporation to make this allocation clear and distinct. Also, note that a lease allocation can affect the farm business’ balance sheet. If you work with an accountant, ask that person for advice. If your farm is financed through a bank or the Farm Service Agency, talk with your loan agent about any effect on your qualifications or personal loan guarantees.

Although the decision and process of allocation may seem overwhelming considering the large number of assets many farms have, it shouldn’t be too complicated if you take a common sense approach. If assets are used for the farm, they should likely be farm assets.

□ Select and appoint a registered agent

A registered agent is the person on file for the public and the government to contact the corporation. For example, the registered agent is the individual who is notified if and when the corporation is a party in a legal action. This is called service of process. A registered agent can be an officer or employee of the company, but is more often a third party such as the corporation’s lawyer or a service provider who takes on this role for a small fee. Whomever you pick, the registered agent’s name and address must be listed in the articles of incorporation.

“The directors govern the corporation and make major policy and financial decisions. They have to act primarily in the interest of the company, and not their own interest.”

□ Choose the initial board of directors

The board of directors is a collection of one or more people that governs the corporation and makes major policy and financial decisions for the company. For example, the directors authorize the issuance of stock in the company, appoint officers, and approve loans and other significant financial matters. All states require corporations to have a board of directors. Many states permit just one director, which could be fine for a small farm operation. However, it can be beneficial for the business overall to have others offering advice and different perspectives. Many business experts recommend having an odd number of directors, and some go further to recommend that five, seven, and nine are magic numbers. The odd number prevents deadlock votes, and the five through nine range provides a variety of perspectives, yet not too many opinions. Keep in mind that directors will need to abide by a fiduciary duty to the company (i.e. a duty of care and a duty of loyalty). This basically means that they can't whimsically make decisions and rather have to act with diligence and care. It also means they have to act primarily in the interest of the company, and not their own interest. To help reinforce this, directors should be required to follow a strict conflict of interest policy that specifies that they cannot vote on a matter that affects their personal interests. For example, a director who is also the president or CEO should not be able to vote on the amount of his salary. Be sure to keep this in mind when deciding whom your initial directors will be.

Form the C Corporation at the State Level

□ Draft your articles of incorporation

The corporation must draft and file articles of incorporation with the state agency that handles entity formation, which is usually the secretary of state office. The articles of incorporation can be drafted either by the business owner with the help of an attorney or entirely by an attorney.

The articles of incorporation are publicly available documents and often include only the basic details about the corporation that are required, such as the corporation name, the name and address of a registered agent, a corporate purpose (the general objectives of the business), and the name and addresses of directors and officers. What is required can vary from state to state. A quick Internet search should bring up the website of the state agency that handles this in your state, which will specify

the information you need. Many state's agency's have form articles of incorporation on their websites that the business can use and adapt for their needs.

Many states also require you to designate the number of authorized shares or stock to be issued. Deciding on the exact amount could be tricky, though many say it's actually quite arbitrary. The shares are the ownership interests in the company. Let's say the company authorizes 10,000,000 shares. If there are two owners, each with 50% interest, they each get 5,000,000 shares. It's advisable to consult with an attorney in your state to be sure the number you designate is proper and recommended for your particular farm operation. It could impact how you raise money or get financing in the future.

The articles will also need to include the name of the incorporator. An incorporator is an individual who organizes and arranges for the articles of incorporation to be filed with the Secretary of State. The incorporator must verify that all the included information is true and correct, and sign the articles of incorporation. The incorporator can be a shareholder, director, or officer of the corporation. It is often the lawyer who is handling the formation of the corporation. While the incorporator is distinct from the registered agent, one person may serve as both.

□ File your articles of incorporation

A corporation does not exist until the date its articles of incorporation are filed and then approved by the state agency. Approval can take anywhere between one day and one week from the time of filing. The articles of incorporation form can generally be submitted online, along with the required fee. If there is no form, they will likely need to be mailed in. Each state charges different fees, which vary from \$25 to \$1000. In addition, most states require an annual fee to maintain the corporation, which is generally less than the fee to create the corporation. The initial directors should review the articles together to be sure everything is accurate before filing. However, the articles do not need to be officially approved by the corporation's board of directors. Note that the information on the articles of incorporation may be changed at any time by filing amended articles.

Organize and Fulfill Corporate Formalities

□ Draft bylaws

In addition to the articles of incorporation, state corporation statues also require corporations to have bylaws. The bylaws are a private document, or in effect a

“A corporation does not exist until the date its articles of incorporation are filed and then approved by the state agency.”

contract, that set the ground rules amongst the shareholders, directors, and officers for how the corporation must be governed. They include procedural guidelines for corporate governance (e.g. shareholder meetings, board of director meetings, etc.). There are two overarching principles for bylaws. First, like any legal document, they should be clear and precise to avoid challenges in interpretation down the road. Second, they should be consistent with all applicable state laws. In effect, any provision in the bylaws that runs counter to a state law will be deemed unenforceable. And, any action made pursuant to an unenforceable provision will be deemed invalid. Having unenforceable provisions and invalid actions is not good business practice for obvious reasons!

Like the articles of incorporation, the bylaws can be drafted by the business owner(s) with the help of an attorney or entirely by an attorney. Keep in mind that state corporation statutes often set specific parameters regarding certain corporate governance matters that are typically included in bylaws, such as when and how shareholders must be informed about annual meetings, items that must be voted on at annual meetings, how voting must take place, restrictions on who can decide what, etc. These details can vary from state to state. So, if you decide to draft your own bylaws, be sure to check your state’s corporation statute or consult with an attorney who is familiar with your state’s statute to ensure that your bylaws are fully in compliance with state law. The bylaws don’t not be filed with the state, but they must be officially adopted by the board of directors.

□ Hold your first organizational meeting with the board of directors

Next, the board of directors should hold an organizational meeting. At this meeting, the directors should first officially adopt the bylaws. Then they should elect the initial officers. The officers are responsible for the day-to-day management of the company. Officer positions include a president (or chief executive officer), a vice-president (or chief operations officer), a treasurer (or chief financial officer), and a secretary. A director can serve as an officer, and one person can serve multiple offices. Like directors, the officers owe a fiduciary duty to the company (i.e. a duty of care and a duty of loyalty). Be sure to keep this in mind when deciding who the initial officers will be. After the officers are elected, the directors should also officially approve the issuance of shares or stock in the company. In addition, if the corporation will be an S corporation (i.e. elect S corporation federal tax status), the directors should approve the election at this time. Be sure to follow the voting parameters set forth in your bylaws when voting on these matters. Also, written minutes must be kept for this organizational

For more information on bylaws and guidance on developing your own, review our sample Bylaws for Momma Earth Farms Inc. that follows this checklist.

“The directors elect the officers. The officers are responsible for the day-to-day management of the company.”

meeting and all meetings held by the board of directors and shareholders to provide evidence of what happened should a dispute or issue ever arise.

□ **Issue stock to the founding shareholders**

Before engaging in any business activity as the corporation, you should issue shares of stock to the founding shareholders. This is the formal process of dividing up the ownership in the company. It is also required by law if you are doing business as a corporation. Issuing stock can be complicated. It could involve adherence with complex securities laws at both the state and federal level. Farm Commons strongly recommends that you have an attorney that is familiar with corporate and securities law handle the stock issuance for you. When you're ready to issue the actual shares to your founding shareholders, you'll need to put in writing the following: the initial shareholders names and mailing addresses, the number of shares each shareholder will purchase, and how each shareholder will pay for her shares (i.e. cash, property, or services - also known as "sweat equity"). Keep in mind that most states have a minimum amount of stock that can be issued, so check your state's corporation statute. Some states require that you file a "notice of stock transaction" with your state's business agency or secretary of state. This is typically a simple form, but it's important that you file it if it's required. Otherwise you risk the state saying that the issuance of shares is invalid.

You also have the option of issuing actual stock certificates. This is no longer required in most states, but shareholders have come to expect it and it provides another layer of evidence of who owns how many shares. If you issue a stock certificate, states generally require that you include on the face of the certificate: the name of the corporation, the state where the corporation was formed, the name and number of shares issued to the shareholder, and a signature authenticating the document.

Note also that if you plan on electing S corporation tax status, you can only issue one class of stock, which is generally common stock, meaning one vote per share. This information should be included in your bylaws.

□ **Create shareholder agreement if shareholders want one**

While shareholder agreements are not required, they can be useful to set forth specific terms that all shareholders must abide by and follow amongst each other, particularly with respect to the limitations and process for transferring or selling shares to others. Basically, shareholder agreements could set restrictions to

“Issuing stock is the formal process of dividing up the ownership in the company.”

“Shareholder agreements can be particularly important in closely held corporations, where the shares are held between a small group of people.”

prevent unwanted parties or strangers from acquiring shares in the company. In this way, shareholder agreements can be particularly important in closely held corporations, where the shares are held between a small group of people and are not offered to the general public. In addition, shareholder agreements can be a useful way to protect minority shareholders, who may fear that their voice will be overpowered. For example, the shareholder agreement could require that all shareholders agree on certain decisions. Shareholder agreements also often include procedures for dispute resolution, which can help keep matters out of court.

- [Get an Employment Identification Number \(EIN\) from the IRS](#)

An EIN is the identification number that the IRS uses to identify the tax accounts of employers and certain business entities like corporations. You can get an EIN immediately by applying online through the IRS website. If you prefer, you download the Form SS-4 on the IRS website and fax your completed form to the service center for your state. They will respond with a return fax in about one week. You will also likely need the EIN to get a bank account for the corporation.

- [Obtain necessary licenses and permits from state and local agencies](#)

You’re almost ready to begin to open shop as a corporation. But first, you’ll need to obtain any required licenses and permits for running your farm operation. Depending on your farm operation, this could include a business license with your city (i.e. a tax registration certificate), a seller’s permit from your state, or a zoning permit from the local planning board. It may be helpful to ask other local business owners what they did when starting their business, or contact the relevant state and city offices.

Implement Best Practices for the C Corporation

- [Follow the bylaws](#)

If you go to the work to outline how the business should handle important things like decisions, taxes, and departure of a member, it’s very important to follow the document. This gives the business legitimacy in court.

- [Allocate assets between personal and business ownership accounts](#)

As discussed above, a farm business needs to follow through on creating a corporation by making the division between business and personal. If the farm

“Making your best guess as to the value of the farm’s various assets and placing them on the farm’s balance sheet is a simple way to document the transfer of assets.”

For more information on drafting leases, see Farm Common’s print resource: *Drafting a Lease: Questions for Farmers and Landowners to Ask*, available on our website.

doesn’t already have a separate bank account, set one up. Farm expenses and payments should move through the farm account, only. Of course, if you forget the farm checkbook and use your personal bank card instead, you may pay yourself back.

Next, determine which assets are farm and which are personal. If there are multiple members and each have promised to make an equity investment in the corporation, in exchange for stock, each member needs to follow through with his or her promise by officially making the investment. For example, if one member promised to invest \$35,000 in cash, then that money needs to be deposited into the corporation’s bank account. If a member promised to invest his or her farm property, then the title of the property needs to be transferred to the corporation.

Overall, a common sense allocation is probably the best route. This process can be quite simple—there’s no need to detail every feed scoop, hand weeder, or trash bin. Making your best guess as to the value of the farm’s various assets and placing them on the farm’s balance sheet is a simple way to document the transfer of assets. If a farm tried to keep all assets personal and leave the farm with nothing, a court would likely not respect the corporation. The allocation must be based in reality and the farm must have enough assets to capitalize the operation.

□ Document relationships for personal assets used for farm purposes

If you choose to hold ownership of the land with yourself personally, you should document the new relationship with the corporation. If the farm business uses your property, then the farm business has a lease with you, whether one is written or not. Written documents are generally the better choice, and it can be a very simple one-page outline of basic terms such as rental rate, lease term, and renewal procedures. Many individuals choose to lease the farmland for a rate equal to the value of the annual property taxes, but each farm has unique needs.

Now is a good time to discuss our objectives in allocating assets and writing leases. At any point in time, a court should be able to determine which assets are the farm’s and which are personal. This is because the farm’s creditors can go after business assets. Thus, we need to know what they are. The court should also be able to determine exactly how and why assets are used for both personal and business reasons. Your documentation can go a long way towards creating an efficient process. If records are a mess and there is no documentation, a court

may decide for itself which assets are personal or business and the farm loses an opportunity to influence the process.

- Update websites, brochures, invoices, order forms and other materials with the C corporation designation, if required

State statutes typically require that a corporation use the Inc. designation in the name of the business. This signals to potential creditors that only business assets are available to satisfy potential judgments against the business. If you don't like the look of the words or you've already invested in marketing materials, check with your secretary of state's office about registering a trade name without the letters. In some states, the county register of deeds handles registration of trade names, so you may need to make a few phone calls. For invoices and other official business, it's best to include the letters after your name.

- Hold your annual shareholders and annual board of directors meetings

////////////////////////////////////
 “State corporation statutes explicitly require that shareholder and board of director meetings are each held annually.”
 //////////////////////////////////////

State corporation statutes explicitly require that shareholder and board of director meetings are each held annually. Some states may allow shareholders to approve actions through written consent instead of a meeting in person. This requires that all shareholders sign a document to evidence their agreement. Either way, it's important that you follow these formalities and either hold meetings or obtain written resolutions in their place. This helps establish the corporation's legitimacy and preserves the benefits of having an entity.

The board of directors must also meet annually. Board of directors meetings are often held immediately after the annual shareholder meeting where the board of directors is elected for the year. Like the shareholder meetings, board of director meetings may also be done through consent resolution and written consent, so long as all the relevant details are in writing with signatures of all directors. It may seem silly to follow such formalities, particularly if the farm business has just a few individuals and they are wearing multiple hats. But these formalities are required by law and must be followed to protect the benefits of having an entity.

When holding meetings, be sure to follow the meeting requirements set forth in your bylaws, including having quorum before voting (minimum number of shares or persons represented for a vote to take place), providing proper notice within the specified time (the invitation to the meeting with precise details), and administering

the voting thresholds (e.g. one-vote-per-share for shareholders and one-vote-per-person for and board of directors, or whatever your bylaws specify if different).

- Keep minutes at all meetings and keep records of significant business decisions

For an example meeting minutes, see the *Sample Annual Meeting Minutes with Annotations* included in this section.

Many state corporation statutes require corporations to keep accurate minutes to record key decisions and resolutions of the shareholders and board of directors. While some states do not require this by law, courts in all states will look at the minutes if a dispute or legal mishap arises. The meeting minutes provide evidence that the corporation was acting properly in both how the decision was made and what was or was not decided. The minutes do not have to be elaborate, just enough detail to offer proof of what was decided and why. Not every routine business decision needs to be documented, but any decisions that require formal board or shareholder approval should be recorded. Types of decisions that should be recorded include any decision made at annual meetings, the issuance of new stock, purchases of real property, approval of long term leases, authorizations for credit, and decisions that involve federal or state tax implications.

- Keep your corporate binder and stock register up to date

The corporation should maintain a binder that includes the articles of incorporation and any amendments, the bylaws and any amendments, the minutes for annual meetings and special meetings, and any written resolutions made outside of a meeting (i.e. with unanimous consent), records of big decisions. Keeping all these documents in one place makes it easier to refer back to something if an issue arises. Again, it also records that the corporation is properly managing its affairs should a lawsuit and the court ask for such evidence. The corporation will also need to maintain a stock register. This register must include things like the names of all the shareholders, their addresses, the number of shares held, the date of certificates issued for the shares, any transfers of stock certificates, and any cancellation of stock certificates (i.e. by a shareholder who transfers her stock to another). Generally, it's maintained by the corporation's secretary.

- Establish a risk management strategy

While the corporation entity can provide important liability protection to its owners, it does not act like insurance. The corporation itself is not shielded from liability, and the individual members may lose their protection if the corporation is undercapitalized or not managed properly.

“While the corporation entity can provide important liability protection to its owners, it does not act like insurance.”

In certain situations, your corporation may be required to carry insurance. Corporate insurance requirements are set by the state government, so you'll need to make sure you're complying with your state's business insurance laws. Required coverage for your corporation may include workers' compensation, disability insurance, and unemployment insurance.

For more information on insurance options, see Farm Common's print resource: *Managing the Sustainable Farm's Risks with Insurance: Navigating Common Options*, available on our website.

In addition, you should consider getting a proper insurance policy to cover your farm operation corporation from risks such as crop failure, damage to equipment or property, and injuries or accidents to employees, farm visitors, or customers. The precise policy will depend upon your operation and what is available in your area. It could include a simple farm insurance policy or a more robust commercial policy to cover value-added products or off-farm activities.

You may want to talk to your insurance agent about coverage for defending the directors and officers of your corporation (also called directors and officers or "D & O" insurance), which protects your corporation if a lawsuit is brought against one of your managers accusing them of negligence or wrongdoing.

□ **Keep accurate and up to date accounting records for tax purposes**

This includes maintaining an accurate profit and loss statement. Keeping good accounting records throughout the year will help streamline the process of preparing an annual report (which is required in most states and includes financial information) and filing both state and federal taxes.

□ **Fulfill annual obligations, including filing and paying corporate federal and state taxes, if applicable**

Your state will likely require you to file an annual report and an annual fee to maintain your corporation. If you neglect these duties, the state may dissolve your corporation. You will also need to file and pay your corporate taxes. If you choose to be taxed as C corporation with the federal IRS (which is the default), the corporation will need to file IRS form 1120. The corporation will also need to distribute employment and dividend tax forms to employees and shareholders. Talk with your accountant or tax preparer or your secretary of state's office and the IRS for more information on filing corporate taxes.

“Keeping good accounting records throughout the year will help streamline the process of preparing an annual report and filing taxes.”

Optional: Elect S Corporation Federal Tax Status

- Verify that a S corporation federal tax status is right for your farm operation

Although S corporations are a wise choice for many farm businesses, each farm should do their homework. The S corporation federal tax status provides the pass-through taxation to circumvent the double taxation dilemma of C corporations. Basically, the S corporation does not have to pay corporate taxes on business income. Instead, business income passes through to the individual owners who must report business income and pay their share of taxes on their individual tax returns. In addition, with an S corporation, business owners can take advantage of the potential savings on self-employment taxes, which aren't available with a traditional C corporation. The following chapter in this guide provides more details on the tax benefits, requirements, and formalities that come with an S corporation. Read that section, and then you can decide whether the benefits outweigh the costs for your farm operation.

- Elect S corporation tax status with the federal IRS

Electing S corporation tax status for corporation is quite simple. You will need to fill out and file with the IRS tax Form 2553 "Election by a Small Business Corporation." The form should be completed up to two months and fifteen days after the beginning of the tax year the election is going to take effect, or at any time during the tax year preceding the tax year it is to take effect. This sounds complicated but the IRS provides examples of how the timing works in the instruction sheet for Form 2553. Farm Commons highly recommends that farmers consult with a tax attorney or accountant *before* filing these tax forms to be sure the S corporation tax status is the best option.

- Distribute and file S corporation federal tax forms and file and pay state taxes

As an S corporation, you'll have to file the annual Form 1120S with the IRS. This is not a tax return, as the entity does not itself have to pay income taxes. Rather, this is an informational tax document used to report the corporation's income and losses and any disbursements of profits given to its shareholders (i.e. dividends to shareholders). Again, the entity itself will not have to pay taxes, as the business' income passes through to the individual shareholders.

In addition, you will have to provide each of the shareholders with a schedule K-1. The schedule K-1 is similar to a W-2, the end of the year wage statement

////////////////////////////////////
 "The S corporation federal tax status provides the pass-through taxation to circumvent the double taxation dilemma of C corporations."
 //////////////////////////////////////

////////////////////////////////////
“Farm Commons
recommends
that you seek
expert tax
guidance before
filing any of
the required
S corporation
tax forms.”
////////////////////////////////////

that employees receive from their employers. The schedule K-1 shows the self-employment income each of the shareholders receives from the company. The corporation must also submit a copy of schedule K-1 to the IRS for each shareholder. This allows the IRS to be sure that each shareholder is properly reporting any self-employment income he or she receives from the entity that has S corporation tax status.

Farm Commons recommends that you seek expert tax guidance before filing any of the required S corporation tax forms.

Also of note, be sure to abide by all the state income tax requirements for your corporation in your state. The S corporation tax status is only relevant for federal income taxes filed with the IRS.



C Corporation Sample Bylaws With Annotations

TABLE OF CONTENTS

Article 1: Shareholders	3
Article 2: Stock	9
Article 3: Directors	10
Article 4: Officers	14
Article 5: Indemnification	16
Article 6: Subchapter S Corporation Status	17
Article 7: Amendments	18
Certificate	19

Mother Earth Farms Inc Bylaws¹

An Illinois Corporation

Article 1: Shareholders

Section 1: Place of Meetings

Shareholders' meetings must be held at the principal office or place of business of the Corporation in the State of Illinois, or any location designated in the notice of meeting.²



- 1 Bylaws outline how the corporation is to operate or run its business, including procedural guidelines for corporate governance (e.g. shareholder meetings, board of director meetings, etc.). There are two overarching principles for bylaws. First, like any legal document, they should be clear and precise to avoid interpretation challenges down the road. Second, they should be consistent with all applicable state laws. Any provision in the bylaws that runs counter to a state law will be deemed unenforceable. And, any action made pursuant to an unenforceable provision will be deemed invalid. Having unenforceable provisions and invalid actions is not good business practice for obvious reasons! So it's essential to follow your state laws. Each state has a corporation statute that requires all corporations to adopt bylaws and specifies what must be included. State corporation statutes often set specific parameters, such as when and how shareholders must be informed about annual meetings, items that must be voted on at annual meetings, how voting must take place, and restrictions on who can decide what, etc. These details can vary from state to state. If you decide to draft your own bylaws, be sure to check your state's corporation statute or consult with an attorney who is familiar with your state's statute to ensure that your bylaws are fully in compliance with state law. That way, if you follow your bylaws you can rest assured that you are following the law. These bylaws for Momma Earth Farms Inc. provide a sample of how bylaws look and illustrate the type of issues that are addressed.
- 2 Shareholder meetings don't necessarily have to be held inside the state where the corporation is based. Nor do the meetings have to take place at the farm or central place of business. While you could set a firm place for all meetings in your bylaws, it's often preferred to allow some flexibility in case circumstances change. The important thing is that the shareholders get an invitation to the meeting in advance, or receive "notice" as specified in the bylaws, including precisely when and where the meeting is. Here, Section 5 sets the notice or meeting invite requirements.

Section 3: Special Meetings

Special meetings of the Shareholders may be called at any time by the Board of Directors of the Corporation, or by the President upon written request of one or more Shareholders holding at least ten percent (10%) of the shares of stock of the Corporation.⁴ The Shareholders may discuss any business at a special meeting.



- 4 Special meetings are typically called when urgent matters arise and a major decision needs to be made. This could include a decision to significantly expand or conversely to sell the farm operation, it could also involve a significant shift in ownership, or a decision to amend the bylaws. The same “notice” requirements must be met to properly inform shareholders of the precise time and place of any special meeting as well as the purpose of the calling the urgent meeting.

Section 4: Notice of Meetings

Notice of the time and place of a Shareholders’ meeting and the purpose for the meeting must be provided in writing no fewer than 10 days and no more than 50 days before the meeting to each Shareholder of record at her mailing address, as listed on the books of the Corporation.⁵



- 5 Giving “notice” is the legal speak for sending out an invitation. Basically, the notice or invitation to a meeting must let the shareholders or the board of directors know important details including when, where, and the purpose of the meeting. Properly sending out the invitation to a meeting is essential. For example, if a shareholder doesn’t receive the invitation as specified in the bylaws, she can contest what was discussed and all of the actions taken at the meeting can be deemed invalid. This would be a huge waste of time as it would have to be done all over again. The notice must be in writing. This provides a record of it. It’s also a good idea to set a time range for sending out the invitation in your bylaws to allow some flexibility. Here, notice must be given between 10 to 50 days of the meeting. So the invite can’t be sent before or after this timeframe. The written notice can be mailed, handed out personally, or electronically mailed if all individuals agree. Note that including the purpose in the notice or invitation is very important. Some state statutes say that if the purpose is not included in the invite, the matter can’t be voted or acted on.

Section 5: Waiver of Notice

A Shareholder may waive notice of a meeting by attending the meeting, either in person or by proxy, or by providing a written waiver before or after the meeting. Waiver of notice shall not be deemed if a Shareholder attends a meeting for the express purpose of contesting the notice or contending that the meeting was otherwise not lawfully called or convened.⁶



- 6 This provision basically says that the notice requirements can be waived. This gives the corporation some flexibility in urgent situations (i.e. if a meeting needs to be called in fewer than 10 days) or if the shareholders don't really care if they receive such an official invitation. Say all the shareholders are friends, and they say, "Hey, I don't need an official notice mailed to me, just tell me when the meeting is and I'll be there." As long as they put this in writing, which can be a simple email, before or after the meeting, you can rest assured that there will be no issue. Also, if an individual shows up to a meeting and doesn't raise issue about whether or how he got the invitation, then that will be deemed a waiver. This makes sense, as the notice provision ensures that shareholders will learn when and where a meeting is to take place so they can attend. The person that shows up obviously found out about it, so the issue is waived. However, if the shareholder shows up to raise issue about improper notice, it is not waived. This gives shareholders the opportunity to lash out in person if they think their interests are being subverted or intentionally sabotaged, which does happen!

Section 6: Quorum

In order to transact business at a Shareholder meeting, there must be a quorum consisting of a majority of the issued and outstanding shares of stock of the Corporation either in person or by proxy.⁷



- 7 A quorum is the amount of represented shares that must be present for the meeting to happen. Note that a quorum is not based on a majority of the number of shareholders, but a majority of the shares of the company. Not all shareholders will necessarily hold the same amount of shares. Many state statutes specify a minimum for a quorum, such as a majority of the shares in the company. If this is the case, your bylaws can set the quorum higher (i.e. two-thirds of the shares) but not lower (i.e. one-third of the shares). Without a quorum, any decision made at the meeting is considered invalid as it could reflect the interest of just a small percentage of ownership interest in the company. Say only 10% of the company's shares are represented at a meeting. Allowing this 10% to take actions on behalf of the company wouldn't be in the best interest of the company.



Here, because Mother Earth Farms has just two shareholders that each have 50% of the shares, both Mom and Daughter need to be present for a quorum (i.e. majority of 51%).

Section 7: Number of Votes for Each Shareholder

Each Shareholder is entitled to one vote for each share of stock belonging in her name on the books of the Corporation.⁸



- 8 Most state statutes require a one-vote-per-share voting rule, so this restates the law. However, some states allow shareholders to receive fractional shares (e.g. 2.5 shares), which can then be matched with fractional voting power (2.5 votes). Small businesses do not usually deal in fractional shares, so the one-vote-per-share rule will work well for most small farm operations.

Section 8: Proxies

At all Shareholder's meetings, every person entitled to vote may authorize another person or persons to act by proxy with respect to her shares by filing a written proxy with the Secretary of the Corporation. A proxy may be revoked at any time before a vote, either by written notice to the Secretary or by oral notice given by the Shareholder at the meeting. The presence of a Shareholder at a meeting who filed a proxy does not constitute a revocation of the proxy. A proxy appointment is valid for 12 months from the filing, unless otherwise indicated in the written proxy form.⁹



- 9 A proxy is a written authorization signed by a shareholder (or a shareholder's power of attorney) giving someone else the power to represent and vote on behalf of the shareholder's shares. It basically allows someone to stand in for a shareholder at the meeting. The shareholder can either specify parameters for how the other person, or proxy holder, should vote. Or, she could simply trust and allow the proxy holder to vote based on his or her own conscience. The proxy counts towards a quorum and represents the shareholder's votes.



In our example of Mother Earth Farms, if Daughter gets sick and signs a written proxy allowing Cousin to vote on behalf of her shares, Cousin and Mom can still make decisions and take a vote because Cousin is standing in for Daughter's 50% share.

Section 9: Voting

If a quorum is present, a majority vote of the shares entitled to vote and represented at the meeting shall be the act of the corporation.¹⁰



10 This basically says that a majority of the shares present at the meeting will have the final say on any matter that's taken to vote. This can be a bit tricky. Again, the quorum requires that at least a majority of the shares are present at the meeting.



Let's say for a moment that there are three shareholders: Mom has 40%, Daughter has 35%, and Aunt has 15% of the shares. Daughter and Aunt attend the meeting as shareholders, but Mom doesn't. There's a quorum, because Daughter and Aunt together have 60% of the shares. Now, let's say that Daughter and Aunt take up the matter of voting on next year's board of directors. Daughter now represents the majority of shares present at the meeting, as Mom's shares don't count because Mom's not present. So basically whatever Daughter decides is the act of the company. This scenario shows how important it is to attend the meetings, or to get a proxy (i.e. someone else to stand in for you).

Section 10: Order of business

The following order of business shall be observed at all Annual and Special Meetings:

1. Roll call
2. Proof of notice of meeting

If a quorum is present, the meeting continues with the following order of business:

3. Approval of the minutes of previous meetings, unless waived by unanimous consent
4. Reports of Board of Directors, if any
5. Reports of Officers, if any
6. Reports of Committee, if any
7. Election of Director, if necessary
8. Unfinished business, if any
9. New business, if any¹¹



- 11 This provision isn't really necessary, but it can be helpful to have a sort of working agenda of items that must be handled and in what order at every meeting. It can help ensure all important matters are covered in an efficient manner.

Section 11: List of Shareholders

A complete alphabetical list of the Shareholders of the Corporation entitled to vote at the meeting, including address of and number of shares owned by each Shareholder, must be prepared by the Secretary, or other Officer of the Corporation in charge of the Stock Transfer Books. This list shall be kept on file for a period of at least sixty (60) days prior to the meeting at the registered office of the Corporation and must be subject to inspection during usual business hours by any Shareholder. This list shall also be available at all Shareholders' meetings and must be open to inspection by any Shareholder at any time during a meeting. Failure to comply with the requirements of this Section will not affect the validity of any action taken at any Shareholders' meetings.¹²



- 12 Most states statutes require the corporation to maintain an alphabetical list of shareholders and to have it readily available for inspection at shareholder meetings. This provides a level of accountability and transparency, which can help ensure that none of the shareholders are wrongly left out or being subverted.

Section 12: Adjournment of Annual Meeting

If a quorum is not present at the Annual Meeting, the Shareholders present, in person or by proxy, may adjourn for a future time agreed upon by a majority of the Shareholders present. Notice of such adjournment must be given to the Shareholders who are not present or represented at the meeting. If a quorum is present, they may adjourn when they see fit and return at time and day that is agreed upon; no notice of such adjournment must be given.¹³



- 13 Adjournment means to suspend the meeting to another time or place. If the quorum is not met, there's really no point of meeting as no official action can be taken. This adjournment provision allows the shareholders present to postpone the meeting to a time they agree will be more suitable for all. If this happens, they must send out an invitation to the shareholders that aren't present in accordance with the notice requirements in Section 5. This provision also allows the shareholders to end a meeting even if matters are not completed so long as they agree to a time and day to return. This is helpful if things run late, which often happens!

Article 2: Stock

Section 1: Certificates of Stock

The Corporation will issue certificates of stock when shares are fully paid.¹⁴ Certificates of stock represent shares in the corporation, and must include the following: (1) the name of the corporation and that it is organized under the laws of Illinois; (2) the name of the person who owns the shares (the Shareholder); and (3) the number of shares that the certificate represents. The certificates of stock must be signed by the president and by the secretary and must be attested by the corporate seal. All certificates must be consecutively numbered and the name of the person owning the shares, the number of shares, and the date of issue must be entered into the Corporation's books.



14 Most states no longer require corporations to issue certificates of stock. However, it is a custom that many corporations still observe. Many shareholders have come to expect paper stock certificates. Issuing them also provides another layer of proof of who has stock or equity ownership in the company. If your state requires certificates of stock, be sure to look up the section on share issuance in your state's corporation's statute and follow the exact requirements.

Section 2: Transfer of Shares

Shareholders may transfer their stock in person or by their attorney upon surrender of the properly endorsed certificate of stock. It is the duty of the Secretary to issue a new certificate to the person entitled to it, to cancel the old certificates, and to record the transaction on the share register of the corporation.¹⁵



15 If the corporation issues stock certificates, this provision should be included to specify what happens when the stock is transferred to another person. Basically, the transferring shareholder needs to fill out the endorsement section (usually found on the back of the certificate of stock) and then give the certificate to the secretary of the corporation. It is the secretary's job to record the transfer in the corporation's Stock Transfer Books and issue a new certificate to the new shareholder. Most farm operations will have a closely held corporation, which means that the shareholders can't just transfer the shares to a stranger. The shareholders of a closely held corporation typically enter a separate shareholder agreement that specifies some additional restrictions on how shares may be transferred. In addition, if the corporation elects the S corporation tax status, the transfer of shares is restricted in certain circumstances. If either is the case for your farm operation, be sure to follow the shareholder agreement and the S corporation restrictions. See Article VII in these bylaws for an example of the type of provisions that should be included if you elect S corporation tax status.

Section 3: Lost, Destroyed, or Stolen Shares¹⁶

If a Shareholder claims that her certificates of stock have been lost, destroyed, or stolen, a new certificate will be issued in the place of the original if the owner: (1) requests a replacement certificate before the corporation has notice that the missing shares have been acquired by a bona fide purchaser; (2) files with the corporation an indemnity bond (no more than twice the value of the shares represented by the certificate) if required by the Board of Directors; and (3) satisfies other reasonable requirements provided under the authority of the Board of Directors.



- 16 This section discusses how lost, destroyed, or stole certificates of stock can be replaced. Following these procedures helps assure that there will be no double selling of the stock if the lost or stolen stock finds its way into the hands of an innocent purchaser who purchases the stock without any knowledge of its lost or stolen status. Basically, the original shareholder must give the corporation notice before the innocent purchaser records their stock with the secretary, otherwise the shareholder may have to cover any damages incurred to the corporation if stock ownership is contested. This is very unlikely to become an issue in a closely held corporation with only a few shareholders such as Mother Earth Farms. But is important to include in case something happens to the certificates of stock.

Article 3: Directors¹⁷**Section 1: Number, Election and Term of Office**

The Corporation is managed by a Board of Directors consisting of two (2) persons.¹⁸ The number of Directors may be increased or decreased by an amendment to the Bylaws. However, the number of Directors shall never be less than two (2) individuals. The Directors shall be elected at the annual Shareholders' meeting and hold office until the next annual meeting and until their successors have been elected and trained.



- 17 Most state statutes require a corporation to have a board of directors. The board plays the role of making major management decisions for the company. The shareholders elect the members of the board to play this role. The shareholders can always remove directors if they're not happy with how decisions are being made.
- 18 Some states require a minimum of three board members while others require just one. Additionally, most states require that directors have a one-year term and require elections at the annual shareholder meeting. The same directors may be reelected each year, but the election formality needs to take place. Be sure to check your state statute to see what is specifically required here.

Section 2: Vacancies

Vacancies in the Board of Directors may be filled by a vote of the remaining Directors.¹⁹ The Director fulfilling the vacancy shall serve until the next annual Shareholders’ meeting.



19 Allowing the remaining directors to fill a vacancy is consistent with the law in most states. However, some states require director vacancies to be filled by a shareholder vote. Again, be sure to check your state statute.

Section 3: Director Meetings and Quorum

An annual meeting of the Board of Directors shall be held immediately after and at the same location as the annual Shareholder meeting. Additionally, special meetings may be called by any Director by giving five (5) days written notice of such meeting to each Director. Notice is not required for any Director who attends the meeting in person or who waives such notice in a writing filed with the Secretary of the Corporation. At all meetings of the Board a majority of the Directors shall constitute a quorum for the transaction of business.²⁰ The act of a majority of the Directors present at any meeting at which there is a quorum shall be the act of the Board of Directors, except as may be otherwise specifically provided by these Bylaws. If all Directors are present, a meeting may be held at any time without notice. In the event that the Corporation has only one Director at any time, a single Director shall constitute a quorum.



20 Most state statutes also require the board of directors to have an annual meeting. This provision sets the parameters for notice and a quorum, which is similar to the requirements for shareholder meetings. Note that the quorum for directors is a majority of the number of directors and has nothing to do with the share or stock percentage. This section also allows the board to meet as many times as necessary to deal with corporation issues.



For Mother Earth Farms, it is unlikely that Mom and Daughter will need to call a formal meeting whenever they want to meet, but to maintain corporate formalities and to ensure liability protection, Mom and Daughter should be sure to have a formal annual directors meeting.

Section 4: Powers

The business and affairs of the Corporation must be managed by the Directors who may exercise all the powers necessary to run the business.²¹



21 Again, the board plays the role of making major management decisions for the company. If the shareholders aren't happy, they can go through the process of removing directors.

Section 6: Removal

At any Shareholders' meeting, any Director (or Directors) may be removed from office, without reason or cause,²² by a majority vote of the present Shareholders. Vacancies will be filled according to Section 2.



22 Most state statutes specify that a director cannot be removed unless there's a cause, such as illegal activity, unless the bylaws specify otherwise. So if you want to give shareholders the right to remove directors without cause, you need to include this in your bylaws. This gives the shareholders absolute control if they feel things aren't going well. After all, the shareholders are the ones that have financial stake in the company.

Section 7: Compensation²³

Directors and members of any committee of the Board of Directors are entitled to a reasonable compensation for their services as determined by resolution of the Board of Directors. A Director may also serve the corporation in any other capacity and receive compensation for that position. Directors must also be provided with reasonable pensions, disability, or death benefits, and other benefits or payments to Directors and to their estates, families, dependents, or beneficiaries for services rendered to the Corporation by the Directors.²⁴



23 This section includes the generally accepted practice of not paying salaries to directors, but instead paying them for their services (such as attendance of meetings and/or travel expenses and the costs associated with attending a meeting). Since Mom and Daughter will likely be compensated for their roles as officers and meetings will be held on the farm, they may decide by resolution that the reasonable compensation for directors is nothing (\$0).

24 Including compensation and benefits for directors is optional. If you include it, it needs to be customized to the benefits that are being offered to the board.

Section 8: Committees²⁵

The Board of Directors may designate one or more committees to report to the Board on any area of corporate operation and performance. Each committee shall consist of at least one member of the Board of Directors. Each committee may exercise any and all powers that are conferred or authorized by the Board of Directors. Matters will be decided by a majority vote of the committee members. The Board of Directors shall have the power to fill vacancies, to change the size of membership, and to discharge any

committee. Each committee must keep a written record of its acts and proceedings and must submit that record to the Board of Directors at each regular meeting and at any other times as requested by the Board of Directors.



“”

25 Committees are a way for the board to delegate decision making to smaller groups rather than requiring all members of the board to vote on a matter. This is particularly useful for larger boards that want to divvy up the tasks base on interest or expertise (such as a committee for finances or personnel). State statutes specify that some issues may not be delegated to a committee such as amendments to the bylaws. For a small corporation like Mother Earth Farms, it is unlikely any committees will be set up. However, including this clause sets up the infrastructure in case more directors come on or if there's a particular issue that the board decides only one board member needs to be present to make decisions on.

Section 9: Dividends

The Board of Directors has full power to determine whether any, and, if so, what part, of the funds legally available for the payment of dividends will be declared and paid to the Shareholders of the Corporation.²⁶



“”

26 A dividend is when the company hands out or distributes the company's earnings to shareholders. Dividends are not required, and can only be made if the company turns a profit. It's often preferred to keep the money in the farm operation to spur growth. In these bylaws, it's up to the directors to decide whether, when, and how much of the earnings should be given to the shareholders in the form of dividends. All state corporation statutes require that dividends be distributed based on shares stock in the corporation.



Here, Mom and Daughter each have 50% stock, so they would split any dividends. If Mom had 60% stock, she would get 60% of the dividend amount.

Article 4: Officers

Section 1: Titles, Election, and Duties

The Board of Directors shall appoint a President, a Vice-President, a Treasurer, and a Secretary.²⁷ The Directors may also appoint other Officers with titles and duties as determined by the Board of Directors. The duties of the Officers are described in the following sections of this article, by these Bylaws, and from time to time as prescribed by the Board of Directors.



27 Most state statutes require corporations to have at least a president and a secretary. This section creates positions for a president, vice-president, treasurer, and secretary. It is good business practice to divvy up the roles. If your corporation prefers to call the president the chief executive officer (CEO) you can replace the term in the section. The same goes with chief financial officer (CFO) in place of treasurer. This section also gives the board of directors the flexibility to create other officer positions should the need arise.

Section 2: President

The President shall preside at all meetings of the Directors and Shareholders and shall have general supervision, direction, and control of the day-to-day business of the Corporation subject to the control of the Board of Directors.²⁸



28 This clause describes the president's duties, which include presiding over all meetings of both shareholders and directors, as well as running the day-to-day business of the corporation. There is no state-required definition of what a president does, and wording the clause generally gives the corporation flexibility with regards to what the president can and can't do. As it's laid out here, Mom (the corporation's president) has flexibility to do what needs to be done for the company to succeed day to day. This makes sense for a small farm operation like Mother Earth Farms. It's important to craft the roles and responsibilities of the officers in a way that's most suitable for your farm operation.

Section 3: Vice-President

The Vice-President shall exercise the functions of the President during the President's absence or disability to fulfil her actions. In addition, the Vice-President will have any other duties that are assigned to her by the Board of Directors.²⁹



29 This clause also is designed to allow the vice-president's role to be as flexible as possible.

Section 4: Treasurer

The Treasurer will keep and maintain the financial accounts of the Corporation, including an account of all monies received or disbursed. She will keep adequate and correct books and records of accounts of the properties and business transactions of the corporation. The Treasurer may endorse on behalf of the Corporation for collection only, checks, notes, and other obligations. She must deposit the same and all monies and valuables in the name of, and to the credit of, the Corporation in such banks and depositories as the Board of Directors shall designate.³⁰



- 30 Generally, the treasurer, or chief financial officer if you prefer, is in charge of all the money flowing in and out of the corporate accounts. This provision provides a level of accountability by requiring that whatever the treasurer receives must be put into the proper corporate account. In addition, the treasurer must keep accurate books and records of all the corporate accounts.

Section 5: Secretary

The Secretary shall keep the minutes of the meetings of Shareholders and Directors and shall give notice of all such meetings as required in these Bylaws. If the Secretary is not present at a meeting, the Shareholders at the Shareholders' meetings or Directors at a Directors' meeting shall appoint someone to take the meeting's minutes. The Secretary shall have custody of the seal of the Corporation and all books, records, and papers of the Corporation, except those in the custody of the Treasurer or some other person authorized to have custody and possession thereof by a resolution of the Board of Directors. The Secretary shall also perform any duties that are incidental to her office or are properly required by the Board of Directors.³¹



- 31 The secretary is generally in charge of making sure that the notice or invitation to meetings is proper, that the meetings are held in accordance with the bylaws and state law, and that minutes are taken and kept in the corporate binder along with the articles, bylaws, and any amendments. Here, the secretary is also in charge of keeping non-financial books include the stock register. This register must include things like the names of all the shareholders, their addresses, the number of shares held, the date of certificates issued for the shares, any transfers of stock certificates, and any cancellation of stock certificates (i.e. by a shareholder who transfers her stock to another). The secretary's job can be very detail oriented, including being sure that deadlines for sending meeting invitations are not missed. Some of the secretary's responsibilities can be delegated to other directors or employees by resolution of the board of directors.

Section 6: Compensation

The salaries of all Officers shall be fixed by the Board of Directors. If an individual serves as a Director and an Officer, she may receive compensation for both positions. No director or officer may vote on his or her own salary.³²



- 32 Both directors and officers may receive a compensation for their service in the role. Here, the board of directors has the authority to determine whether and how much compensation to pay the officers and directors. Note that all states require directors and officers to abide

by a “fiduciary duty.” This is a legal term that says that the director or officer must act solely in another party’s interest, which here is the corporation’s interest. A director has a “conflict of interest” if she can vote on her own salary. She may personally have an interest in a huge bonus, but that would not be in the interest of the corporation. It’s good practice to have a clear conflict of interest policy that all directors and officers abide by. Adding a voting restriction in the compensation provision of the bylaws serves as a reminder of the director’s fiduciary duty to act first and foremost in the interest of the corporation.

Section 7: Appointment, Removal, and Vacancies

Each Officer must serve for the term of one year³³ and until her successor is appointed and trained. However, an Officer may be removed by the Board of Directors at any time with or without cause and with or without hearing or notice of hearing.³⁴ Vacancies of an Officer by reason of death, resignation or other cause shall be filled by the Board of Directors.



33 It’s up to you to decide how long you want officers to serve in their role. Here, it’s one year.

34 The bylaws should specify who has the authority to appoint and dismiss officers and how this process takes place. Here, the authority is in the hands of the board of directors. Of note, even though dismissal can be “without cause,” the board of directors must still be careful to abide by state and federal employment law. For example, dismissal of an officer cannot be based on discriminatory reasons.

Article 5: Indemnification

Section 1: Indemnification and Reimbursement

The Corporation must indemnify each of its Directors, Officers, and employees (and any executor, administrator, and heir of a Directors, Officer, or employee) whether or not currently in service against all reasonable expenses incurred by her in connection with the defense of any litigation she is a party to because she is or was a Director, Officer, or employee of the Corporation. The individual will not have a right to reimbursement if the matter involves negligence or misconduct in the performance of her duties, or was faulty in the performance of her duty as Director, Officer or employee by reason of willful misconduct, bad faith, gross negligence or reckless disregard for the duties of her position. The right to indemnity also applies to court approved settlements and compromises.³⁵



35 An indemnification provision is simply a promise by the other party to cover your losses if he or she does something that causes you harm or causes a third party to sue you.

Indemnification provisions can vary quite a bit. Here, this indemnification clause means

that if someone sues a director, officer, or employee of the company for something they did on behalf of the corporation, the corporation has to pay to defend that lawsuit. The caveat is that if the action is attributed to the negligence or intentional bad acts of the director, officer, or employee, the corporation does not have to pay to defend the lawsuit. In general, if the individual was acting in good faith and with the corporation's best interests in mind, the corporation will need to indemnify or pay her for any legal costs incurred. A corporation should consider carrying insurance for this – without insurance, the business probably can't afford to follow through on this provision. Farm liability insurance may or may not provide this coverage. A commercial policy might be necessary.

Article 6: Subchapter S Corporation Status

Section 1: Election

The Corporation shall be an “S corporation” as the term is defined in the Internal Revenue Code of 1986, as amended (the “Code”), and shall take all actions necessary to elect S corporation tax status and continue to keep the status in effect. The Corporation must not take any actions that would disqualify the Corporation as an S corporation as the term is defined in the Code.³⁶



³⁶ This section should only be included if the corporation elects S corporation tax status through the IRS. The S corporation is simply a federal tax status, as it provides certain tax benefits for small businesses (i.e. the “S” stands for small business). S corporation has no meaning at the state level. Read the chapter on S corporations in this guide for more information on the benefits and requirements of S corporations. The following section within this article have to do with making sure the IRS requirements for S corporation tax status are not violated.

Section 2: Restrictions on Transfer

No Shareholder may transfer, either directly or indirectly, any shares of the corporation to any person or entity if the holding of the Corporation's shares or stock by such a person or entity would disqualify the corporation as an S corporation as the term is defined in the Code. Any attempt to transfer an interest in the corporation to such a person or entity shall be void and ineffective.³⁷



³⁷ An S corporation has certain requirements for who can be a shareholder. For example, all shareholders must be U.S. citizens and a shareholder can't be another business entity. So if a shareholder inadvertently transfers her stock to a Canadian, it would disqualify the corporation from the S corporation tax status. This provision ensures this does not happen, as it deems any such transfer invalid.

Section 3: Subchapter S Stock

The Corporation may have no more than one class of stock, and within that class, the rights, designations, and preferences of shares may differ only with respect to voting rights.³⁸



38 Having only one class of stock is another requirement for S corporation tax status eligibility. This simply reinforces the IRS requirement.

Article 7: Amendments³⁹

Section 1: By Shareholders

New Bylaws may be adopted and any Bylaws may be amended, altered or repealed by the Shareholders at any Shareholders’ meeting, provided written notice of such proposed action shall have been given in the call for such meeting.

Section 2: By Directors

Except as otherwise provided by law, the Directors may adopt, amend or repeal these Bylaws.



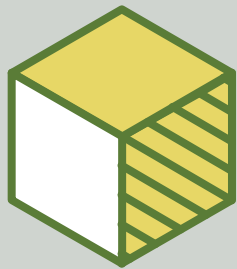
39 It’s important to include explicit provisions for how the bylaws can be amended. Many state statutes speak to these as well, so be sure to check any specific requirements in your states statute. In these bylaws, either the shareholders or the directors can amend the bylaws by a majority vote at a meeting (i.e. one share one vote for shareholders and one person one vote for directors). You could require a different voting threshold such as a super-majority (three-quarter approval) or unanimous consent to amend the bylaws, or any other “big” decision that needs to be made such as selling the company or closing the business. It’s up to you. Just be sure to check your states statute to ensure whatever you decide is in line with the laws of your state.

Certificate

This certifies that the foregoing is a true and correct copy of the Bylaws of Mother Earth Farms, Inc., and that these Bylaws were duly adopted by the Board of Directors of the Corporation on the date set forth below.

Dated _____

Signature _____



Sample Annual Shareholder Meeting Minutes with Annotations

ANNUAL SHAREHOLDER MEETING MINUTES FOR MOTHER EARTH FARM INC.

An annual shareholders' meeting was held on February 11, 2015 at 2:00 P.M. at the Mother Earth Farm Inc. office, in Illini, Illinois, for the purpose of electing directors of the corporation for next year's term, to discuss the company's financial performance, address any amendments to the Bylaws, and for any other relevant business matter that may arise.



¹ *The place, time, and date information needs to be in line with whatever is specified in the company's bylaws. For Mother Earth Farm Inc., the bylaws explicitly say that the meeting will be held on the second Tuesday of February at 2:00 P.M. Your bylaws don't necessarily have to be as precise. Most state statutes require that the annual meeting be held at a date, time, and place set forth in the bylaws, or be determined in accordance with the bylaws. For example, the bylaws could simply specify a month and a place, and require that the precise time be determined within 30 days before the meeting date. Whatever the case, be sure that you follow what your bylaws say and report the actual date, time, place, and purpose of the actual meeting in your minutes.*

² *Most states require that director elections are held at the annual meeting. Any other matter that is discussed is up to you. It's helpful to state the purpose at the beginning of the minutes as it makes it easier to recall what was covered if you're searching for something in particular.*

Mom Farmer acted as chairperson and Daughter Farmer acted as secretary of the meeting.³



³ *Mom is the president and the bylaws say that the president presides over shareholder meetings. Daughter is the secretary of the corporation, so she's the one that handles administrative aspects, including the minutes.*

The secretary announced that all the attendees were given proper notification of the meeting's time, place, and purpose as required by the bylaws, or that such notice had been waived. Copies of the written notice and any written waivers are attached to these minutes.⁴



⁴ State statutes require that shareholders are told in advance the date, time, and place of the annual meeting as well as the purpose, or what will be covered, so that they can plan and prepare. This invitation to the meeting—or “notice” in legal speak—must be in writing and follow the timing protocol that is set forth in your bylaws. For example, if your bylaws say that you must notify shareholders of the annual meeting 30 days prior to the meeting date, be sure to do so. Your bylaws can also specify how such notice can be waived. For example, some bylaws say that if a shareholder shows up and didn’t actually receive a written announcement about the meeting, the notice requirement is waived (unless they specifically came to raise issue about improper notice). This makes sense, as the point of requiring written notice is to be sure shareholders know about the meeting. If they show up, they obviously know about. As for providing shareholders advanced notice about the purpose of the meeting, it’s generally sufficient to attach an agenda or to simply provide some bullet points on topics to be covered along with the written notice announcing the meeting time and place. You may also want to include a catch all statement like “any other relevant business matter that may arise.” This allows other matters to be discussed if they spontaneously arise. So basically, this section in the minutes states the notice and waiver requirements in the bylaws were followed. It is also good practice to include copies of the written notice or waivers as this provides a safeguard if a shareholder later down the road contests that they weren’t given proper written notice.

The secretary announced that an alphabetical list of the names and number of shares held by all shareholders was available at the meeting for any of the present parties to inspect.⁵

The secretary announced that the following shareholders, proxy holders, and shares were present and constituted a quorum of the shareholders:⁶

Name	Number of Shares
Mom Farmer	50
Daughter Farmer	50



⁵ Most state statutes require that an alphabetical list of the shareholders is available for inspection at the annual meeting. This is also required in the Mother Earth Farm bylaws. Including a statement about it in the minutes is good practice.

⁶ This is where you list each shareholder and the amount of shares they have. The bylaws



will specify what a quorum is, or how many shareholders need to be present for a vote to take place. The Mother Earth Farm, Inc. bylaws say that a quorum is a majority of the voting shares. Since Mom and Daughter both own 50% of the 100 shares of Mother Earth Farm Inc, both need to be present to meet the quorum. If a proxy had been used (i.e. someone standing in for either mom or daughter), be sure to include a sentence after this list that announces that a copy of the written proxy is attached to the meeting minutes.

The secretary announced that the following non-shareholder individuals were also present at the meeting:

Name	Title
Joan Smith	Accountant



⁷ This is where you list non-shareholders who were present at the meeting. This could include employees of the company who have something to report, or experts such as lawyers or accountants to advise on legal or financial matters.

The secretary announced that the minutes of the annual shareholders' meeting held on February 12, 2014 were distributed at the meeting. The previous meeting's minutes were approved by all of the shareholders in attendance.



⁸ It is customary to approve the previous meeting's minutes as the first matter of business at a meeting. While it is not legally necessary, it's a good way to remind shareholders of the issues that came up the year before.

The president announced that the next item of business was the election of the board of directors for another one-year term. The shareholders nominated Mom and Daughter. Mom made a motion to vote on the nominations and daughter seconded the motion.⁹ After a majority vote, the secretary declared that both Mom and Daughter were elected to serve on the board of directors for an additional year.¹⁰



⁹ Making a "motion" and "seconding the motion" is a custom formality in corporate meetings. Basically, any official action or vote that is to be taken at a meeting requires at least two people to agree. The first "moves" or "makes a motion" for the vote and the second person "seconds" the motion. Then the vote can take place. This helps assure that



only relevant and significant matters go to a vote. Here, it seems silly given there are only two shareholders. However, it's good business practice to follow these custom formalities.

¹⁰ Since Mother Earth Farm Inc. only has two shareholders who are also the only board members, officially voting on this matter each year may seem like a waste of time. However, it's important to follow the formality and to report it in the minutes since most states require director elections to be held at annual meetings.

The president announced that the next item of business was the financial performance of the company. The president presented the annual report and a printed version of the report was attached to the end of the minutes.¹¹ Joan Smith, the accountant, reported that based on the findings in annual report and her review of the company's financial statements, the company was doing well financially.



¹¹ If any reports are presented at the meeting, be sure to attach them to the minutes. Again, this serves to track what information was presented in case a dispute arises. Of note, most states require that a corporation prepares and files an annual report, which reports on the corporation's activities throughout the preceding year and provides a summary of the financial performance. Here, the accountant attended the annual meeting to report on the financial performance. This is not at all necessary. However, reviewing your financial performance annually with an accountant can be a helpful exercise. Doing this at an annual meeting ensures that all shareholders have the opportunity to directly hear the expert advice and any tips for financial improvement.

Mom then requested that the annual meeting be held in January instead of February. She presented an amendment to the bylaws to make this change and made a motion to vote on the matter. Daughter seconded the motion. After a majority vote of the shareholders in attendance, an amendment to the bylaws was adopted stating that annual meetings will now be held on the second Tuesday of January.¹²



¹² Electing the board of directors may be the only and final order of business, as it's really the only matter that is legally required to be handled at an annual meeting. However, consider the annual meeting as an opportunity to discuss and handle any new or unfinished business matters. One example is an amendment to the bylaws. The Mother Earth Farms, Inc. bylaws require unanimous consent for an amendment. The bylaws also require that a proposed amendment to the bylaws must be announced before the meeting, or included in the official written notice. Be sure to follow your bylaws in such



situations. Here, both Mom and Daughter agree to changing the meeting time. Be sure to attach the amendment to the meetings, and follow up by formally amending the bylaws accordingly and including a new copy of your amended bylaws in your corporate binder together with all your meeting minutes.

Since there was no further business to come before the meeting, on motion duly made by Mom and seconded by Daughter, the meeting was adjourned.¹³

Daughter Earth, Secretary



¹³ *If there is no further business discussed, the meeting can be adjourned. Again, customarily, this official action requires two people to agree by making a motion and seconding the motion.*

Do you have questions or thoughts on how to improve this document? We want to hear from you. Please email us!

info@farmcommons.org

CONNECT WITH US!



www.twitter.com/farmcommons



www.facebook.com/farmcommons



info@farmcommons.org



RACHEL
REPONDS

Was this resource not quite what you were looking for? Do you still have more questions? Send your questions to Farm Commons and we will do our best to feature an answer in our blog. Read the most recent questions and