5425

1. CORPORATION FOR PROFIT — ARTICLES OF INCORPORATION — GENERAL CORPORATION ACT OF OHIO—WHERE ONE OF PRINCIPAL OBJECTS IS DISTRIBUTION OF DIVIDENDS OR PROFITS TO MEMBERS, OR TO SECURE MORE FAVORABLE TERMS OR SAVINGS IN PURCHASING OF PROPERTY OR SERVICES, ARTICLES SHOULD BE FILED AS CORPORATION FOR PROFIT.

2. CORPORATION NOT FOR PROFIT — ARTICLES SHOULD STATE PECUNIARY GAIN OR PROFIT NOT PRINCIPAL PURPOSE OF PROPOSED CORPORATION.

SYLLABUS:

Articles of incorporation intended to be filed under authority of the General Corporation Act of Ohio which would permit, as one of the principal objects of incorporation, the distribution of dividends or profits to its members, or one of whose principal objects is to secure more favorable terms or savings for its members in the purchasing of property or services, should be filed as a corporation for profit. If it is desired to incorporate as a corporation not for profit the articles should be set forth, presumptively at least, that pecuniary gain or profit it not to be one of the principal purposes of the proposed corporation.

Columbus, Ohio, September 2, 1942

Hon. John E. Sweeney, Secretary of State,
Columbus, Ohio.

Dear Sir:

I have received from your office the articles of incorporation of a proposed corporation for the purpose of determining whether this document should be accepted by your office for filing as a corporation not for profit. The entire purpose clause reads as follows:

> "The purpose or purposes for which said corporation is formed are: To operate a hospital and nursing home."

While your request might be summarily answered, the frequency with which similar questions have arisen with respect to other proposed articles of incorporation makes it appear appropriate to review at some length the authorities on this question.

The purposes for which corporations for profit may be formed are found in Section 8623-3, General Code, which reads:

> "A corporation for profit may be formed hereunder for any purpose or purposes, other than for carrying on the practice of any profession, for which natural persons lawfully may associate themselves, provided that where the General Code makes special provision for the filing of articles of incorporation of designated classes of corporations, such corporations shall be formed under such provisions and not hereunder. Corporations for the erection, owning and conducting of sanitariums for receiving and caring for patients, their medical and hygienic treatment and the instruction of nurses in the treatment of disease and of hygiene shall not be deemed to be forbidden hereby."

Under authority of this section, it appears evident that a corporation may be formed for the purpose of conducting a hospital or nursing home if it be incorporated as a corporation for profit. Might such an institution also be incorporated as a non-profit corporation and, if so, under what conditions? The purposes for which corporations not for profit may be formed are found in Section 8623-97 of the General Code, which section reads as follows:

> "A corporation not for profit may be formed hereunder for any purpose or purposes not involving pecuniary gain or profit for which natural persons may lawfully associate themselves, provided that where the General Code makes special provision for the filing of articles of incorporation of designated classes of corporations not for profit, such corporation shall be formed under such provisions and not hereunder."

When considering what was intended by the expression "corporations not for profit" as found in the Delaware statutes, the Chancellor said in Read v. Tidewater Coal Exchange, 13 Del. Ch. 195, 209, 116 Atl. 898, 904 (1922):

> "Whether dividends are expected to be paid may, generally speaking, be taken as the test by which we are to determine whether, or not, a given corporation is organized for profit. Perhaps a better way to put it would be to say that a corporation is for profit when its purpose is, whether dividends are intended to be declared or not, to make a profit on the business it does which in reason belongs to it and which if its affairs are administered in good faith would be available for dividends. Subterfuges by which a corporation allowed its profits to be diverted to those owning it, though not in the form of dividends, would manifestly not remove from the corporation its features

> of profit making. Nor would a mere declaration in its certificate of incorporation that it was organized not for profit, be sufficient to stamp upon it a non-profit character. In each case, when the corporation is examined, the true facts must be ascertained and the corporation judged accordingly, no matter what its scheme of operation, or its pretensions may be. Such being true, the state is always protected against schemes to evade franchise taxes, first by the inspection which the corporation must undergo before the Secretary of State, and secondly by the writ of quo warranto which the state may always employ to oust a corporation for abuse of its franchise.
>
> Profit furthermore must be something of a tangible or pecuniary nature. Intangible benefits, not capable of measurement in definite terms, though of value to the recipient, cannot be called profits. When we speak of a corporation for profit, I take it also that we mean profit coming to, or belonging to, the corporation qua such, as distinct from its members or stockholders. Barring cases where profits are improperly diverted directly to the corporate members and not conveyed to them through the channel of the corporate treasury, which cases would rest on a distinct footing, the term 'profit' as employed in the section under discussion means gain or earnings that are expected to come into the possession of the corporation."

Referring to non-profit corporations, Fletcher, in his Cyclopedia Corporations, Permanent Edition, Vol. 1, §68, says:

> "Profit is used in a pecuniary sense, and does not extend to intangible benefits and the existence or nonexistence of stock, or the declaration in the articles of the nature of the corporation, is not necessarily a determinant."

Although the term "profit", as used in Section 8623-97, General Code, appears to be limited to pecuniary gains or savings, the statute does not attempt to limit such profits to corporate dividends. It would appear that any indirect means of subterfuge for the distribution of profits is prohibited.

In State v. Lumberman's Clinic, 58 Pac. (2nd) 812, 816 (Wash.), the court, in discussing such profits, said:

> "Profit does not necessarily mean a direct return by way of dividends, interest, capital account, or salaries. A savings of expense which would otherwise necessarily be incurred is also a profit to the person benefited. If respondent renders to its incorporators or members, or to businesses in which they are interested and in whose profits they share, a service at a cost lower than that which would otherwise be paid for such service, then respondent's operations result in a profit to its members."

This seems to have been the view in Ohio under previous similar statutory provisions. Referring to the 1911 Annual Reports of the Attorney General, page 127, I find that the then Attorney General said:

> "It is not lawful in this state for persons to form an association in the guise of a corporation 'not for profit' when the real object of the incorporators, as disclosed by the articles of incorporations, is the promotion of the welfare of its members by any form of business enterprise or management which will reap a pecuniary profit for them." (Earnings to be disposed of in part to its members and legal representatives.)

A little later, the Attorney General found that his formula for determining what was a corporation not for profit had been too narrow and in the 1912 Annual Reports of the Attorney General, page 39, he said:

> "In this case the corporation itself evidently is not designed to engage in any profitable enterprise unless it should reap interest from an investment of its funds otherwise than in loans to its members. On the other hand, the members of the corporation are not to reap any direct profit, either pecuniary or otherwise. Nevertheless, the object of the corporation is in the full sense of the word a pecuniary one, and it is intended for the pecuniary benefit of its members. * * * While I have in a previous opinion advised you that the test of what constitutes a corporation for profit is the distribution of the increment of its funds among the members of the corporation by way of dividend or otherwise, I am disposed, in view of the question which has now arisen, to enlarge upon the former definition and to state that it should be broad enough to include all corporations the sole purpose of which is the direct or indirect pecuniary benefit of the members."

In the 1913 Annual Reports of the Attorney General, page 93, the same Attorney General said:

> "* * * a corporation, the object of which is to save money for its members by combining their investments and securing more favorable terms therefor, or otherwise, is no less a corporation 'for profit' than one the object of which is to make money for its members, so that its profits may be ratably distributed to them."

A similar conclusion was reached by my predecessor as shown in Opinion No. 2809, Opinions of the Attorney General for 1938, page 1537, in which opinion he considered the present Corporation Act and in the second branch of the syllabus held:

> "A corporation organized for the purpose of purchasing merchandise in large quantities and distributing same to such members, the object being to secure more favorable terms for such members and to save them money in the purchase of such merchandise, is a corporation for profit and should be incorporated under Section 8623-4, General Code."

In State, ex rel. Attorney General v. Home Cooperative Union, 63 O.S. 547, the court indicated that whether a corporation may be incorporated as a non-profit corporation depends upon the objects and acts sought to be performed. It further appeared to reach the conclusion that a statement in the articles of incorporation that the corporation would be operated without profit is not controlling if inconsistent with the other provisions thereof.

In the same manner it appears that while the persons now seeking to organize a corporation have chosen a non-profit corporation form for its articles, yet the objects and purposes as stated therein can not be said to be restricted to profitless operations.

In Cheney v. Ketchum, 5 N.P. 139, the court recognized that a social club might be organized as a corporation not for profit where its controlling purposes were the amusement of its members and the mutual improvement of their social and cultural relationships but having incidental pecuniary benefits for its members in that they were able to procure refreshments at reduced prices.

In Celina Telephone Co. v. Mutual Telephone Co., 102 O.S. 487 (1921), Judge Hough remarked at page 494 of the opinion:

> "How may it be determined whether a corporation or association is one for profit or not for profit? Does the filing of articles of incorporation, in which the declaration is made that it is not for profit, and on which the charter is issued, govern or determine this question? Is the issuance or non-issuance of capital stock controlling, or is it whether a business is to be engaged in, and operated with consideration of the character of that business and the method of conducting it, that is the true test?
>
> We think the latter."

Considering again the proposed articles of incorporation, it will be noted that there are three persons seeking to incorporate. They pro-

pose to act as trustees until an election has been held. No provision is found for other persons becoming members of the organization. No provision is made for the types of patients they expect to receive, as for example, whether they expect to receive charity patients. The articles submitted do not preclude the adoption of a restriction limiting persons entering their institution to pay patients. No provision has been made for the disposition of income. Profits might be distributed as dividends or by subterfuge as salaries, or otherwise. It may be that the incorporators fully intend to operate the corporation without profit. However, it seems that this fact should be shown, at least presumptively, in the purpose clause of the articles.

The Secretary of State, being a public officer, has such duties only as have been enjoined upon him by law and those which are necessarily incidental thereto. Peter v. Parkinson, 83, O.S. 36 and State, ex rel. v. Pierce, 96 O.S. 44. Section 8623-97, et seq., General Code, make it the duty of the Secretary of State to accept for filing, as not for profit corporations, articles of incorporation of corporations to be formed whose purpose or purposes do not involve pecuniary gain or profit for which natural persons might lawfully associate themselves.

The purpose or purposes of a proposed corporation must, of necessity, be ascertained by the Secretary of State from the articles submitted. If the purposes as stated in the articles be expressed in general terms, as in the instant case, the Secretary would be unable to determine therefrom that pecuniary gain or profit was not contemplated. When unable to determine that pecuniary gain or profit is not involved, there is no authority in law for the acceptance for filing of such proposed articles of incorporation. State, ex rel. Harris v. Myers, Secretary of State, 128 O.S. 366.

It is, of course, a matter of common knowledge that most hospitals in Ohio are incorporated not for profit but it is also a matter of common knowledge that such hospitals have been regarded as charitable corporations, even though they receive pay for patients for lodging and care. Taylor, Admr. v. Protestant Hospital Association, 85 O.S. 90. In O'Brien, Treasurer v. Physician's Hospital Association, 96 O.S. 1, it was said on page 9 of the opinion:

> "* * * The first concern of a public charitable hospital must be for those who are unable to pay. If, after taking

> care of these, it still has further accommodations, there can be no objection to making use of the same for pay patients in order to increase the fund which may be at its disposal for the benefit of the poor."

If the purpose clause in the articles of incorporation shows, at least presumptively, that the corporate purpose or purposes do not involve pecuniary gain or profit, it appears that the Secretary of State may properly accept such articles for filing. Should there be no such restrictions or limitations upon the contemplated corporate activities, it appears to be the duty of the Secretary to receive such articles only when tendered for filing as a corporation for profit.

In specific answer to your inquiry, it is my opinion that: Articles of incorporation intended to be filed under authority of the General Corporation Act of Ohio which would permit, as one of the principal objects of incorporation, the distribution of dividends or profits to its members, or one of whose principal objects is to secure more favorable terms or savings for its members in the purchasing of property or services, should be filed as a corporation for profit. If it is desired to incorporate as a corporation not for profit the articles should set forth, presumptively at least, that pecuniary gain or profit is not to be one of the principal purposes of the proposed corporation.

Respectfully,

THOMAS J. HERBERT
Attorney General.