Tulsa Law Review

Volume 17 | Issue 1

Fall 1981

Professional Corporations in Oklahoma

Tom Arnold
University of Tulsa, College of Law, mark-arnold@utulsa.edu

TULSA LAW JOURNAL

Volume 17 1981 Number 1

PROFESSIONAL CORPORATIONS IN OKLAHOMA

M. Thomas Arnold*

I. INTRODUCTION

Incorporation of a professional practice is sometimes desirable. The attorney and the professionals involved will face a number of corporate law questions, some similar to those posed by any business corporation, and others unique to the professional corporation. Some of the questions do not yet have definitive answers.[1] This article will examine a number of the corporate law aspects of the professional corporation and suggest answers for some of the open issues. In addition, it will show the need for legislative reconsideration of the Professional Corporation Act.

* Associate Professor of Law, the University of Tulsa College of Law; A.B., *summa cum laude*, Ohio University; M.A., Ohio University; J.D., *cum laude*, University of Michigan.

1. Minimal case law pertaining to professional corporations exists. In Oklahoma, the author has found only two reported cases dealing with the Oklahoma Professional Corporation Act. To a large extent, the existing interpretations of state professional corporation statutes have been made by state attorneys general. *See* [1976] 2 PROF. CORP. GUIDE (P-H) ¶¶ 30,001-35,002. The Oklahoma Business Corporation Act requires the Oklahoma Attorney General to render a written opinion concerning any question of law regarding the construction of the Act upon written request of the Oklahoma Secretary of State. OKLA. STAT. tit. 18, § 1.205 (1971). The Professional Corporation Act makes the Business Corporation Act applicable to professional corporations. *Id.* § 805. The Secretary of State is entitled to regard an opinion of the Attorney General as "binding until such question of law has been ruled upon by a court of competent jurisdiction." *Id.* § 1.205.

II. BENEFITS OF THE CORPORATE FORM

The Oklahoma Professional Corporation Act[2] was passed by the legislature in 1961 for the express purpose of "making available to professional persons the benefits of the corporate form for the business aspects of their practices. . . ."[3] A number of benefits are often cited as flowing from the corporate form of business organization. These include tax benefits and the benefits of limited liability, centralized management, free transferability of ownership interests, and potentially perpetual duration (or continuity of existence).[4]

It is the author's opinion that in most cases the primary consideration in determining whether or not to incorporate relates to the benefits available to the incorporated enterprise under the federal Internal Revenue Code.[5] The benefit of limited liability, at least in the torts context, can usually be obtained as a practical matter by insurance coverage.[6] The benefit of centralized management can generally be obtained through a carefully drafted partnership agreement.[7] The benefit of freely transferable interests is undercut by the lack of a ready market for shares in a closely-held corporation.[8] Finally, legal and practical

---

2. OKLA. STAT. tit. 18, §§ 801-819 (1971).

3. *Id.* § 802.

4. One potential disadvantage to the corporate form of organization is that it is likely to be more costly to form and operate than a sole proprietorship or partnership. Jorrie and Wolf, *Selected Practical Problems with Professional Associations and Professional Corporations*, 10 ST. MARY'S L.J. 247, 249 (1978). In addition, "some people view as a disadvantage the somewhat greater difficulty of dissolving a corporation than a partnership . . . . [A] shareholder cannot dissolve a corporation at will. . . ." 17 B. EATON, PROFESSIONAL CORPORATIONS AND ASSOCIATIONS, BUSINESS ORGANIZATIONS § 3.02[3] (1980).

5. *See* note 10 *infra*.

6. Professor Hamilton writes:

> In practice, however, limited liability is not as important as often thought. Both corporations and partnerships buy liability insurance against claims based on tort. Both buy fire, theft, and extended coverage insurance to protect its property. Employees with access to large amounts of money are bonded whether the business is a partnership or a corporation. Thus the existence of such risks does not materially affect the question whether or not to incorporate, since the great bulk of such risks are in fact borne by others.
>
> So far as contract obligations are concerned, banks and extenders of substantial credit are aware of the limited liability of a corporation, and if in their view the assets of the corporation are insufficient to provide reasonable security, they routinely insist that the persons behind the corporation give their personal guarantees. Such guarantees are often also required on leases and other long term corporate commitments.

R. HAMILTON, THE LAW OF CORPORATIONS IN A NUTSHELL § 2.5, at 22 (1980).

7. "Many of the so-called corporate advantages can be attained by using a partnership . . . . A partnership can delegate the management of its business to one or more partners." G. SEWARD & W. NAUSS, BASIC CORPORATE PRACTICE § 1.02, at 3 (2d ed. 1977).

8. *Cf.* Galler v. Galler, 32 Ill. 2d 16, ___, 203 N.E.2d 577, 583-84 (1964) ("While the shareholder of a public-issue corporation may readily sell his shares on the open market . . . his counterpart of the close corporation has no ready market for his shares should he desire to sell.");

continuity of existence must be distinguished. "A small closely held corporation may be so dependent upon one person that it disintegrates, as a practical matter, upon his death, despite the fact that it continues as a legal entity."[9]

With respect to the professional corporation, similar comments would appertain. Tax considerations usually will be the primary—if not sole—reason for incorporating a professional corporation.[10] The initial reason for the passage of professional corporation statutes was actually to allow professionals to achieve "tax equality" with employees of other corporations.[11]

Donahue v. Rodd Electrotype, 328 N.E.2d 505, 511 (Mass. 1975) ("We deem a close corporation to be typified by . . . no ready market for the corporation stock . . . .").

9. R. DEER, THE LAWYER'S BASIC CORPORATE PRACTICE MANUAL § 1.02(b) (2d ed. 1978). It should also be noted that "[a] partnership agreement can provide for the continuation of the partnership upon a partner's death, an event which absent such a provision would normally dissolve the partnership." G. SEWARD & W. NAUSS, BASIC CORPORATE PRACTICE § 1.02, at 3 (2d ed. 1977).

10. A sole proprietor or partner in a professional practice does not enjoy employee status for federal income tax purposes. Being self-employed, he or she is unable to take advantage of a number of provisions of the Internal Revenue Code which permit an employee to exclude from gross income certain benefits provided by his or her employer. In addition, a sole proprietorship or a partnership is not the employer of the proprietor or of the partners and, thus, may not deduct as compensation the cost of the benefits provided. I.R.C. § 162(a)(1).

The tax advantage of a professional corporation is that the professional(s) involved can attain employee status vis-a-vis the corporation. The significance of this is two-fold. First, the Internal Revenue Code permits the professional *qua* employee of a professional corporation to set aside in a tax-deferred qualified pension plan a larger amount of earned income than would be possible if self-employed. *Compare* I.R.C. § 415(c) *with* § 404(e)(1) *as amended* by the Economic Recovery Tax Act of 1981, Pub. L. No. 97-34, § 312(a). (The self-employed professional is limited to the Keogh plan. In addition, while the shareholder-employee may participate in a qualified profit-sharing plan, the self-employed individual may not.) Second, the professional corporation can provide the professional employee with a number of benefits, the amount or cost of which need not be included in the employee's gross income. These include: group term life insurance up to $50,000 face value, I.R.C. § 79(a); unlimited health and accident insurance coverage, I.R.C. § 106; medical and dental reimbursement pursuant to a non-discriminatory plan, I.R.C. § 105(b) & (d); and disability payments, I.R.C. § 105(d). *See* Hayes, *The Professional Corporation: An Overview*, 12 UNIV. OF RICHMOND L. REV. 323, 324-27 (1978), for a very brief overview of the tax advantages of the professional corporation.

There are potential tax pitfalls in the utilization of a professional corporation. These can generally be avoided through careful planning. *See id.* at 329-32.

While the primary emphasis of this article is the corporate law aspects of the professional corporation, counsel need always be mindful of tax considerations.

11. One commentator on the Oklahoma Professional Corporation Act has stated:

> The goal and effect of this legislation is to make it possible for members of these professions to become stockholder employees of their own corporations in order to achieve tax equality with employees of business corporations whose employees enjoy the benefits of pension and/or profit sharing plans and other benefits described as "fringe benefits."

Fleig, *Professional Corporations*, 33 OKLA. B.J. 357, 357 (1962).

The passage of professional corporation statutes for the purposes of providing professionals with "tax breaks" has not gone uncriticized. Professor Bittker wrote that "the statutes permitting the organization of professional associations and corporations have no apparent purpose other than federal tax reductions . . . and they would have, if successful, a substantial effect on the

As far as limited liability is concerned, the professional corporation statute provides that "[t]his Act does not alter any law applicable to the relationship between a person rendering professional services and a person receiving such services, including liability arising out of such professional services."[12] While this provision has never been judicially interpreted in Oklahoma, one commentator has described it as providing that:

> the physician would continue to be liable for malpractice, as would the corporation. However, the other professionals would not be personally liable except to the extent of their equity in the corporation, whereas as partners, they would be, under certain circumstances, jointly liable.[13]

This interpretation seems entirely reasonable.[14]

In an Indiana case,[15] the court held that a provision like the one in the Oklahoma Act preserving the professional relationship did not impose vicarious liability on a physician for the malpractice of another shareholder of a professional corporation if the physician's sole connection with the tort was his ownership of shares in the corporation. The facts of the case indicate that the non-treating shareholders were not

---

federal revenue." Bittker, *Professional Associations and Federal Income Taxation: Some Questions and Comments*, 17 TAX. L. REV. 1, 29 (1961). He went on to suggest the possibility of "proletarian corporations" asking: "If state action turns the trick for lawyers and doctors, why not state legislation to allow *everyone* to 'incorporate'?" *Id.* at 34.

12. OKLA. STAT. tit. 18, § 812 (1971).

13. Fleig, *supra* note 11, at 358. In commenting on statutes containing provisions like the one in the Oklahoma Act, Cavitch states:

> By implication non-participating shareholders would be insulated from personal liability arising out of the professional relationship . . . since:
>
> (1) the statutes do impose liability on the person rendering the service . . . and
>
> (2) the statutes usually specifically provide that the jurisdiction's general corporation laws are applicable to professional corporations in so far as they are not inconsistent with the provisions of the professional corporation statute.

4A Z. CAVITCH, BUSINESS ORGANIZATIONS § 82.03[a] n.17 (1980).

14. The highest courts of several states have, by court rule, provided that *legal* professional corporations may be formed only upon condition that the shareholders waive limited liability. *See, e.g.*, OHIO S. CT. RULES FOR GOV'T OF THE BAR, RULE III, § 4, providing:

> the participation by an individual as a shareholder of a legal professional association shall be on the ground that such individual shall, and by such participation does, guarantee the financial responsibility of the association for its breach of any duty, whether or not arising from the attorney-client relationship.

See also In re Bar Ass'n of Hawaii, 516 P.2d 1267 (Hawaii 1973), wherein the Hawaii court adopted its Rule 24 pertaining to professional corporations. Rule 24(d) provides that the articles, by-laws and share certificates of a legal professional corporation shall state that liability of shareholders, officers and directors for acts, errors and omissions arising out of performance of professional services by the corporation will be "joint and several to the same extent as if the shareholders, officers or directors were general partners engaged in the practice of law." *Id.* at 1269.

15. Birt v. St. Mary Mercy Hosp. of Gary, Inc., 370 N.E.2d 379 (Ind. App. 1977).

present when the plaintiff was treated, exercised no control over and had no right to control the treating physician, and did not have a physician-patient relationship with the plaintiff.[16] Thus, the holding of the case, confined to its facts, is narrow.

The court went on to state that "[w]ithout deciding, we note that the statute may impose personal liability on contracts to cure and liability for the negligence of assistants acting under the physician's direction."[17] The court seemed to draw a line between duties arising out of the professional relationship and other duties, suggesting that shareholders of a professional corporation may retain personal liability for breaches of duties owed to their clients.[18]

Whether or not a shareholder in an Oklahoma professional corporation obtains full or partial limited liability, the corporation would be subject to general liability.[19]

Concerning the free transferability of interests, the practical limitations in a closely held corporation are compounded by the provision of the Professional Corporation Act which restricts a shareholder from voluntarily transferring his shares to any person other than a duly licensed member of the same profession for which the corporation was

---

16. *Id.* at 380.

17. *Id.* at 383.

18. *Cf.* Boyd v. Badenhausen, 556 S.W.2d 896 (Ky. 1977) (a shareholder in a medical professional corporation may be personally liable for the acts of corporate employees). The *Boyd* court stated:

> [A] physician [is] responsible for the derelictions of persons employed by a corporation to carry out for him the clerical details that are necessary to the successful performance of his duty to render skillful care and attention to whomever he accepts as a patient.
>
> * * *
>
> Placing a layer of other people, by whomsoever they may be employed, between a physician and his patient does not alter the situation, because the physician's professional duties are not susceptible of being delegated or diffused.

Id. at 899.

The court in *Boyd* did not deal with the question of whether a shareholder in a professional corporation is personally liable for breaches of duty not arising from the professional relationship.

19. Although there are no reported Oklahoma cases dealing with the liability of professional corporations, the Professional Corporation Act provides that the Business Corportion Act shall be applicable to professional corporations. OKLA. STAT. tit. 18, § 805 (1971). The Business Corporation Act provides that a corporation may be sued in its corporate name. *Id.* § 1.19(1) (Supp. 1980). The corporation would be liable for contracts made on its behalf by authorized agents. *See id.* § 1.19(5) (providing that corporations have contractual capacity). In addition, the corporation would be liable for the torts of its servants under the doctrine of respondeat superior. See 57 C.J.S. *Master and Servant* §§ 561-62 (1948); RESTATEMENT (SECOND) OF AGENCY § 219(1) (1957).

Cases from other jurisdictions support the proposition that a professional corporation is liable for the malpractice of a shareholder-employee. *See* Birt v. St. Mary Mercy Hosp. of Gary, Inc., 370 N.E.2d 379, 383 (Ind. App. 1977) (dictum); Lenhart v. Toledo Urology Assoc., 48 Ohio App. 2d 249, 356 N.E.2d 749 (1975).

organized.[20]

Finally, although the Oklahoma statute was recently amended to increase the potential existence of an Oklahoma corporation from fifty years to perpetual duration,[21] there is, as mentioned above, a difference between legal and practical continuity of existence.[22]

III. FORMING THE PROFESSIONAL CORPORATION

In Oklahoma, a professional corporation can only be formed for thirteen statutorily enumerated professions.[23] Further, a professional corporation may be formed in Oklahoma only for the practice of a single profession.[24] Thus, an optometrist and a dentist would not be allowed under the Act to form a professional corporation for the joint practice of optometry and dentistry. For some corporations this would not only be illegal under the Act, but would also be a violation of the applicable code of professional responsibility.[25] The professional corporation, in addition to being restricted to rendering only one type of professional service, is not allowed to engage in any other type of busi-

20. OKLA. STAT. tit. 18, § 809 (1971). This proscription is reinforced by a requirement that before a professional corporation may transfer any shares upon its books it must receive a certificate from the relevant regulatory board stating that the transferee is a licensed member of the pertinent profession. *Id.* One author states that "[i]t is advisable for protection against a technical defect in organization to specifically set forth in the articles of incorportion the statutory requirements for transfer of shares . . . ." 4A CAVITCH, *supra* note 13, § 82.02[3].

The statutory requirement that a professional corporation refuse to transfer shares upon its books until receiving the necessary certificate would prevent such a refusal from being wrongful and, thus, a conversion. *See* United States Cities Corp. v. Sautbine, 126 Okla. 172, 259 P. 253 (1927); Annot., 54 A.L.R. 1152 (1927).

21. OKLA. STAT. tit. 18, § 1.14(2) (Supp. 1980). *See generally* Forst, *Accommodations for the Close, Professional and Nonprofit Corporation*, 51 OKLA. B.J. 1817 (1979).

22. *See* note 9 *supra* and accompanying text.

23. OKLA. STAT. tit. 18, § 803 (Supp. 1980). These professions are: (1) medicine, (2) osteopathy, (3) chiropractic, (4) chiropody, (5) optometry, (6) veterinary medicine, (7) architecture, (8) law, (9) dentistry, (10) public accountancy, (11) psychology, (12) physical therapy, and (13) nursing. *Id.* "The articles of incorporation should carefully spell out the nature of the profession to be practiced by the professional corporation, using the exact statutory language to avoid any defect in the organizing instrument." 4A CAVITCH, *supra* note 13, at § 82.02[3]. *See also* Okla. Op. Att'y Gen. (August 9, 1962), *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 33,623 (professional golfer cannot incorporate under the Professional Corporation Act).

24. OKLA. STAT. tit. 18, § 806 (1971). *Compare* PENN. STAT. ANN. tit. 15, § 2907(b) (Purdon Supp. 1980-81), permitting a professional corporation to be formed for the purpose of rendering two or more types of professional services if combined practice is authorized by the applicable licensing rules.

25. *See, e.g.*, OKLA. STAT. ANN. tit. 5, ch. 1, app. 3, Canon 5 and DR 5-107 (West Supp. 1980). The Oklahoma Code of Professional Responsibility provides that a lawyer should exercise independent professional judgment on behalf of a client and that, to this end, a lawyer should not practice in the form of a professional corporation if a non-lawyer owns any interest, is a corporate director or officer thereof, or has the right to direct the professional judgment of the lawyer. *See also id.*, DR 3-102 prohibiting the dividing of legal fees with a non-lawyer.

ness, e.g. selling hamburgers or repairing bicycles.[26] It may, however, own real and personal property necessary or appropriate to the rendering of professional services.[27] Unlike the professional corporation statutes in some jurisdictions, the Oklahoma Act expressly permits a professional corporation to "invest its funds in real estate, mortgages, stocks, bonds, and any other type of investments."[28]

Forming a professional corporation is much like forming a business corporation.[29] For example, the contents of the articles of incorporation are similar,[30] with the exceptions of the scope of the purposes clause, discussed above,[31] the incorporation of the certificate of the regulating board of the profession, discussed below,[32] and the inclusion of the "names and residence addresses of all of the original shareholders, directors, and officers of the professional corporation."[33] The stated capital requirement[34] is applicable, and officers and directors responsible for commencing business prior to satisfaction of the stated capital

26. OKLA. STAT. tit. 18, § 806 (1971).

27. *Id.* Even if the Act did not expressly allow this, it would most likely be allowed under the so-called implied or incidental powers doctrine. A leading case dealing with the implied powers doctrine is Jacksonville M.P. Ry. & Nav. Co. v. Hooper, 160 U.S. 514 (1895). Oklahoma cases have followed this approach. *See* Southwestern Surety Ins. Co. v. Davis, 53 Okla. 332, 156 P. 213 (1916); Okla. Portland Cement Co. v. Anderson, 28 Okla. 650, 115 P. 767 (1911). In addition, the Business Corporation Act provides that "[e]very domestic corporation shall possess the powers and authority incidental to and expedient for the attainment of, the purposes stated in its articles of incorporation." OKLA. STAT. ANN. tit. 18, § 1.27 (West 1971). This seems to be a codification of the incidental powers doctrine.

28. OKLA. STAT. tit. 18, § 806 (1971). The approach of the Act in proscribing a professional corporation from engaging in any business other than rendering professional service while permitting the corporation to invest its funds in stocks raises an interesting question of interpretation. Could a professional corporation be "the sole owner of a subsidiary corporation engaged in any business so long as its interest therein was that of an investor and provided that the separate entity of the subsidiary was carefully observed"? Treadway, *Survey of Kansas Law: Business Associations*, 14 KAN. L. REV. 165, 168 (1965) (analyzing the Kansas Professional Corporation Act).

One notewriter proffers:

> In no state, however, are there specific guidelines as to what constitutes participation in another business as opposed to investment—such as whether it is necessary to participate actively in the decision making of the company or whether a certain percentage of the stock ownership transforms an investment into active engagement.

Note, *Professional Corporations: Analysis Under the Tax Reform Act and Survey of State Statutes*, 58 GEO. L.J. 487, 516-17 (1970).

29. *See generally* Strong & Holdsworth, *Incorporating a Professional Practice—A Comprehensive Checklist*, 16 PRAC. LAW, May, 1970, at 69.

30. The contents of the articles of incorporation of a Business Corporation must conform to OKLA. STAT. tit. 18, § 1.208 (1971). This section is made applicable to professional corporations. *Id.* § 804.

31. See notes 22-28 *supra* and accompanying text.

32. See note 45 *infra* and accompanying text.

33. OKLA. STAT. tit. 18, § 804 (1971).

34. *Id.* § 1.15.

requirement are liable for the unpaid portion.[35] In addition, the lawyer forming the professional corporation should comply with applicable state and federal securities laws.[36]

There are some peculiarities to the formation of a professional corporation in Oklahoma. A business corporation in Oklahoma must have three incorporators.[37] This probably derives from the requirement of three directors under the Business Corporation Act[38] and the managerial authority given to the incorporators by the Oklahoma Act.[39] The Professional Corporation Act requires only one incorporator[40] but does not expressly deal with the question of the number of directors required for the organization of a professional corporation. Early opinion was to the effect that three directors were necessary.[41] In 1963, however, the Oklahoma Supreme Court ruled that a professional corporation could validly organize with only two directors,[42] stating:

> It appears to be reasonable that if it had been the intention of the Legislature to require three or more directors under the Professional Corporation Act, as is required by the Business Corporation Act, it would, no doubt, have stated in the Act that three or more individuals could incorporate.[43]

---

35. *Id.* § 1.174.

36. While complete discussion of this topic is beyond the scope of this article, when forming a closely held corporation, counsel will invariably seek to structure the transaction to fall within available exemptions to the state and federal securities laws. *See* OKLA. STAT. tit. 71, § 401(b)(9)(A) (1971) (limited offering exemption), and Day, *The Impact of the Oklahoma Securities Act on the Formation of Closely Held Corporations*, 50 OKLA. B.J. 1154 (1979). *See also* Securities Act of 1933, § 3(a)(11), 15 U.S.C. § 77c(a)(11) (1971) (intrastate offering exemption). Securities Act of 1933, § 4(2), 15 U.S.C. § 77d(2) (1971) (non-public offering exemption), and Securities Act of 1933 Release No. 4434, 26 Fed. Reg. 11,896 (1961), No. 4552, 27 Fed. Reg. 11,316 (1962), and No. 5450, 39 Fed. Reg. 2353 (1974).

One writer asserts that "[s]ince the participants in a professional corporation are almost invariably residents of a single state, and are usually few in number, it is virtually inconceivable that the formation of a professional corporation could infringe the federal securities laws." 17 B. EATON, *supra* note 4, § 9.04[21]. It is still preferable, however, to comply with the federal securities laws by design rather than by accident.

The Michigan Act exempts professional corporations from the Michigan blue sky law. MICH. COMP. LAWS ANN. § 450.228 (1973). *Accord*, MO. ANN. STAT. § 356.070(2) (Vernon 1966).

37. OKLA. STAT. tit. 18, § 1.208 (1971).

38. *Id.* § 1.35(a).

39. *Id.* § 1.30. The Act confers managerial authority on the incorporators "up to the time that the board of directors has been elected and qualified." *Id.*

40. *Id.* § 804.

41. The Attorney General of Oklahoma rendered an opinion dated August 10, 1961, that the requirement of the Business Corporation Act that a corporation have at least three directors was applicable to professional corporations. Okla. Op. Att'y Gen. (August 10, 1961) *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 33,621. *See* notes 42 and 44 *infra* and accompanying text. This was also the position of any early commentator. Fleig, *supra* note 11, at 358.

42. Christian v. Shideler, 382 P.2d 129 (Okla. 1963).

43. *Id.* at 134.

While the court did not deal with the question of whether a professional corporation with only one director would be permissible, the logic of its decision indicates an affirmative response, and the Oklahoma Attorney General has rendered an opinion to that effect.[44]

In addition, the Professional Corporation Act requires that individuals incorporating a professional corporation file with the Secretary of State, as part of the articles of incorporation, "a certificate by the regulating board of the profession involved that each of the incorporators, directors, and shareholders are [sic] duly licensed to practice such profession."[45] No certificate need be included for officers of the corporation. The Act, however, does require as a continuing obligation that all officers except the secretary, as well as all directors and shareholders, be licensed members of the specific profession.[46]

The restrictions on corporate names also differ with respect to professional corporations. First, the name of a professional corporation must end with "Corporation," "Incorporated," "Corp.," or "Inc."[47] Thus, the words "company" and "limited" and their abbreviations are not permissible endings for the name of a professional corporation

44. Okla. Op. Att'y Gen. 70-321 (1970), *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 33,627. If a professional corporation were formed with only one director, OKLA. STAT. tit. 18, § 1.43 (1971) would require that he or she also be the corporate president.

45. OKLA. STAT. tit. 18, § 804(c) (1971). Cavitch states: "The certificate of the regulatory board is always attached to the articles of incorporation and included at the time of filing. It is also incorporated in the articles by specific reference." 4A CAVITCH," *supra* note 13, at § 82.02[3].

The Act also provides that the regulating boards of the professions permitted to incorporate are "authorized and directed to issue the certificates." OKLA. STAT. tit. 18, § 818 (1971). The Supreme Court of Oklahoma acted swiftly after the passage of the Professional Corporation Act to pronounce that "the canons of ethics . . . do not appear to be offended by the incorporation of the business aspects of a lawyer's practice under the particular provisions of the Oklahoma Professional Corporation Act." *In re* Okla. Prof. Corp. Act, Senate Bill No. 399 of the 28th Session of the Oklahoma Legislature, S.C.B.D. No. 1378 (Dec. 21, 1961), *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 33,622. It designated the Executive Secretary of the Oklahoma Bar Association as the party to issue the certificates necessary for incorporation of a law practice. *Id.*

The Supreme Court of Ohio, in contrast, refused for several years after the passage of the Ohio Professional Association Act to give its imprimatur to legal professional associations. The court stated:

> [U]ntil such time as this court, through its rules for admission to the practice of law, recognizes the right of a corporate entity to practice law, the Secretary of State is under no clear duty to accept for filing and record articles of incorporation which set forth that a purpose of the corporate entity is to "practice law".

State *ex rel.* Green v. Brown, 173 Ohio St. 114, __, 180 N.E.2d 157, 158 (1962). *See also* State *ex rel.* Green v. Brown, 176 Ohio St. 155, 198 N.E.2d 447 (1964).

When the Ohio Supreme Court finally permitted lawyers to incorporate, it conditioned the privilege upon assumption of unlimited liability by the shareholders. *See* note 14 *supra*.

46. OKLA. STAT. tit. 18, § 810 (Supp. 1980). One effect, and perhaps the intent, of excepting the secretary is to allow the attorney who sets up a corporation for his professional client(s) to serve as corporate secretary.

47. OKLA. STAT. tit. 18, § 807 (1971).

even though allowed in the case of other business corporations.[48] In addition, the Professional Corporation Act permits the regulating board of a profession to adopt, by rule, additional requirements regarding the name of corporations rendering services in that profession.[49] Finally, general ethical considerations would place some limitations on the naming of a professional corporation. "[I]t would hardly do, for example, to permit a law corporation named 'Exceptionally Large Judgments Guaranteed, Inc.' "[50]

The need for strict compliance with all requirements for incorporation should be emphasized. One author states that "[i]n Oklahoma, 'de facto' corporations are not recognized under any circumstances."[51] He continues that "if the corporation is not complete in all respects, it will not be recognized under Oklahoma law and consequently will not be recognized as a corporation for tax purposes."[52]

---

48. *Id.* § 1.11(a).

49. *Id.* § 807. The Oklahoma State Board of Public Accountancy Rule VIII(4), Article 505, provides in part:

> A registrant shall not practice under a firm name which includes any fictitious name, indicates specialization, or is misleading as to the type of organization (individual, partnership or corporation). Names of one or more past partners or shareholders may be included in the firm name of a successor partnership or corporation only with the permission of the retiring or withdrawing partner or shareholder.

Reprinted in 17C B. EATON, PROFESSIONAL CORPORATIONS AND ASSOCIATIONS, app. A, at A-75 (1980).

The Oklahoma Code of Professional Responsibility states in part:

> A lawyer in private practice shall not practice under a trade name, a name that is misleading as to the identity of the lawyer or lawyers practicing under such name, or a firm name containing names other than those of one or more of the lawyers in the firm, except that the name of a professional corporation or professional association may contain "P.C." or 'P.A." or similar symbols indicating the nature of the organization, and if otherwise lawful a firm may use as, or continue to include in, its name the name or names of one or more deceased or retired members of the firm or of a predecessor firm in a continuing line of succession.

OKLA. STAT. tit. 5, ch. 1, app. 3, DR2-102(b) (Supp. 1980).

50. R. HAMILTON, CASES AND MATERIALS ON CORPORATIONS 31 (2d ed. 1981). In addition, the name of a professional corporation may not be such as to imply that it was formed for any purpose other than one authorized by the Professional Corporation Act. *See* OKLA. STAT. tit. 18, § 1.11(b) (1971).

51. 4A CAVITCH, *supra* note 13, at § 82.02[3] referring to OKLA. STAT. tit. 18, § 1.14(c) (1971). Cavitch appears to be correct in his interpretation of this subsection. The Draftsman's Note following this subsection of the Oklahoma Business Corporation Act states that it "distinctly changes the former law by abolishing de facto corporations." OKLA. STAT. tit. 18, § 1.14(c) (1971) (Draftsman's Note subsection c). Prior Oklahoma law did in fact recognize the de facto corporation. *See, e.g.*, Indus. Bldg. & Loan Ass'n v. Williams, 131 Okla. 167, 268 P. 228 (1928).

52. 4A CAVITCH, *supra* note 13, § 82.02[3].

IV. Interplay Between the Business and Professional Corporation Acts

A. *In General*

The Oklahoma Professional Corporation Act provides that the Business Corporation Act[53] "shall be applicable to professional corporations and they shall enjoy the powers and privileges and be subject to the duties, restrictions, and liabilities of other corporations, except where inconsistent with [the Professional Corporation Act]."[54] This means, among other things, that a corporation formed pursuant to the Professional Corporation Act may take advantage of the Business Corporation Act provisions which allow greater flexibility in running a closely-held corporation in Oklahoma. Examples include the section permitting shareholders and directors to take action in Oklahoma by written consent in lieu of a meeting[55] and the new provision of the Oklahoma statute permitting telephonic directors' meetings.[56] In addition, the applicability of the Business Corporation Act ensures to shareholders in a professional corporation a number of protections. Among these protections are the right to inspect corporate records,[57] the right to receive a corporate annual report,[58] and the right to bring a shareholder's derivative suit for various types of wrongful behavior by other parties to the corporations.[59]

There are other interesting ramifications to applying the Business Corporation Act to professional corporations. For example, the Business Corporation Act dispenses with the defense of usury for corporations[60] and proscribes loans by a corporation to its officers and directors.[61]

Provisions of the Business Corporation Act which conflict with the letter or purpose of the Professional Corporation Act do not apply to professional corporations. Examples include the provision of the Business Corporation Act permitting a domestic corporation to confer upon

53. Okla. Stat. tit. 18, § 1.1-.250 (1971).
54. *Id.* § 805.
55. *Id.* § 1.55(c) and § 1.38(6) (Supp. 1980), respectively.
56. Okla. Stat. tit. 18, § 1.38(8) (Supp. 1980). *See also* Forst, *supra* note 21, at 1817-18.
57. Okla. Stat. tit. 18, § 1.71 (1971). *See generally* Note, *Shareholder's Inspection Rights*, 30 Okla. L. Rev. 616, 617-21 (1979) (examining Oklahoma law).
58. Okla. Stat. tit. 18, § 1.72 (1971). A corporation's by-laws may dispense with the annual report. *Id.*
59. *Id.* § 1.28(b).
60. *Id.* § 1.26.
61. *Id.* § 1.175.

bondholders or other creditors the right to vote.[62] Providing voting rights to a creditor who is not a licensed member of the profession would be contrary to the purpose of the Professional Corporation Act which requires directors, shareholders, and officers to be duly licensed members of the specific profession.[63] As to certain professions, such as law, it might also be a breach of professional ethics.[64] Similar comments could be made about the provision of the Business Corporation Act which permits a shareholder to vote by proxy.[65] Insofar as the proxy is held by someone other than a duly licensed member of the profession, the proxy, at least if discretionary in nature, would violate the intent of the Professional Corporation Act that only licensed members of the profession participate in management and control[66] and may likewise pose professional ethics problems.

A final example of conflict between the Acts is the section of the Business Corporation Act authorizing the establishment of voting trusts, which also raises similar ethical concerns.[67] An additional con-

62. *Id.* § 1.67.

63. *Id.* § 810 (Supp. 1980).

64. Canon 5 of the Oklahoma Code of Professional Responsibility states: "A Lawyer Should Exercise Independent Professional Judgment on Behalf of a Client." OKLA. STAT. tit. 5, ch. 1, app. 3, Canon 5 (1971). In addition DR 5-107(c) states: "A Lawyer shall not practice with or in the form of a professional corporation or association authorized to practice law for a profit, if . . . [a] non-lawyer has the right to direct or control the professional judgment of a lawyer." *Id.* It seems arguable that giving voting rights to creditors who are non-professionals would violate Canon 5 and DR 5-107(c).

The American Bar Association's proposed Model Rules would permit a lawyer to practice with a firm in which managerial authority would be exercised by a non-lawyer if certain safeguards are respected. DISCUSSION DRAFT OF ABA MODEL RULES OF PROFESSIONAL CONDUCT, Rule 7.5, *reprinted in* 48 U.S.L.W. 1, 27 (Feb. 19, 1980). These would secure against interference with the lawyer's professional judgment or with the attorney-client relationship and against divulgence of client confidences. *Id.* The Comment to the proposed Rule 7.5 states: "In professional corporations it is sometimes essential or convenient that a nonlawyer be an officer or director." *Id.* It is not clear whether the proposed Rule would sanction creditor voting rights.

65. OKLA. STAT. tit. 18, § 1.60 (1971).

66. The professional corporation statutes in a number of states expressly limit the granting of proxies to persons licensed in the same profession as the shareholder, or to a shareholder of the same corporation. *See, e.g.*, MICH. COMP. LAWS ANN. § 450.228 (1973); OR. REV. STAT. § 58.175 (1979). The Florida Act, on the other hand, appears to prohibit all proxies. FLA. STAT. ANN. § 621.09 (West 1977).

67. OKLA. STAT. tit. 18, § 1.66 (1971). Several state professional corporation statutes flatly prohibit transfer of the stock of a professional corporation to a voting trust. *See, e.g.*, OR. REV. STAT. § 58.175 (1979); FLA. STAT. ANN. § 621.09 (West 1977).

Cavitch states: "The reason for such a prohibition is obvious. Voting trust agreements would be violative of professional ethics, for there is the possibility of nonprofessional, unqualified persons controlling professional policies, conduct, and operations of qualified persons." 4A CAVITCH, *supra* note 13, § 82.03[2].

The professional corporation statutes in a few states allow voting trusts only if the trustee is a licensed member of the same specific profession or a shareholder of the same corporation. *See, e.g.*, MICH. COMP. LAWS ANN. § 450.228 (1973); MO. ANN. STAT. § 356.070 (Vernon 1966).

sideration with respect to a voting trust is that the provision of the Business Corporation Act permitting the establishment of a voting trust requires transfer of the stock to the voting trustee.[68] The Professional Corporation Act permits voluntary transfer of shares only to licensed members of the profession for which the corporation was organized and renders all other voluntary transfers null and void.[69] Because of this, it is clear that a valid voting trust could be formed only if the voting trustee were a licensed member of the relevant profession.[70]

B. *Some Specific Questions*

Can foreign professional corporations qualify to do business in Oklahoma? While the Professional Corporation Act is silent on this question, the Business Corporation Act does provide for the domestication of foreign corporations.[71] Is this provision applicable to and available to foreign professional corporations? While there is no case law upon this question in Oklahoma, the Oklahoma Attorney General has rendered an opinion that a Nevada professional corporation could be domesticated under the business corporation law if the Nevada Corporation's sole stockholder was licensed to practice medicine in Oklahoma.[72] Thus, a foreign professional corporation can qualify to do business in Oklahoma if it meets all the requirements of the Oklahoma Professional Corporation Act.

The other side of this question is whether a professional corpora-

68. OKLA. STAT. tit. 18, § 1.66 (1971).

69. *Id.* § 809.

70. It has generally been held that a voting trust which does not comply with the statutory requirements for a voting trust, including transfer of the stock into the name of the voting trustee on the corporation's books, is illegal and, hence, void. Abercrombie v. Davis, 36 Del. Ch. 371, 130 A.2d 338 (1957); Smith v. Biggs Boiler Works Co., 32 Del. Ch. 405, 82 A.2d 372 (1951).

71. OKLA. STAT. tit. 18, §§ 1.199-.200 (1971).

72. Okla. Op. Att'y Gen. 76-184 (1976), *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 33,630. The Attorney General of Ohio has likewise ruled that "[w]here each shareholder of a foreign professional corporation is licensed to render professional service by the State of Ohio and where the foreign professional corporation otherwise meets the requirements of [the Ohio Professional Association Act], it may properly be licensed to do business in Ohio." Ohio Op. Att'y Gen. 77-018 (1977), *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 33, 527. *But see* Dalton, Dalton, Little, Inc. v. Mirandi, 412 F. Supp. 1001 (D.N.J. 1976), in which the court, in dictum, stated that the New Jersey Professional Service Corporation Act "contains no authority for a foreign professional corporation to secure authority to do business in New Jersey." *Id.* at 1004. *See generally* Note, Dalton, Dalton, Little, Inc. v. Mirandi: *A Stumbling Block for Professional Corporations Attempting to Establish a Multi-State Practice*, 30 OKLA. L. REV. 585 (1977).

In a few states the professional corporation acts expressly permit foreign professional corporations to domesticate or qualify to do business. *See, e.g.*, PA. STAT. ANN. tit. 15, § 2906(b) (Purdon Supp. 1980-81). At the other extreme, the Oregon statute expressly prohibits foreign professional corporations from transacting business in the state. OR. REV. STAT. § 58.235 (1979).

tion formed under the Oklahoma Act can qualify to do business in another jurisdiction. Obviously the answer to this question would not depend on Oklahoma law, but rather on the law of the other jurisdiction.[73] One author has stated that the numerous problems involved in using a professional corporation for the conduct of a profession outside of the state of incorporation make the professional corporation "virtually useless for a multistate practice."[74]

Can a professional corporation amend its purpose clause from rendering professional services to all lawful purposes? While the Professional Corporation Act is again silent on this matter, there is no policy reason to prohibit a conversion of a professional corporation to a business corporation. Therefore, conversion should be permitted under the provisions of the Business Corporation Act which allow amendment of a corporation's articles.[75]

The Attorney General of Oklahoma has, on the other hand, rendered an opinion that a corporation formed under the Business Corporation Act cannot file amended articles to become a non-profit corporation and that a non-profit or charitable corporation cannot amend its articles to become a business corporation.[76] The conversion of a professional corporation to a business corporation can be distinguished on the grounds that both are corporations for profit. In addition, the professional corporation in Oklahoma is already permitted to engage in business of an investment nature.[77]

---

73. *See* note 72 *supra*.

74. 17 B. EATON, *supra* note 4, § 9.04[22] (1980).

75. OKLA. STAT. tit. 18, § 1.151 (1971). The procedure for amending the articles is set out in *id.* § 1.153. Under Oklahoma law, a shareholder may dissent to any amendment of the articles which "substantially alters or changes the corporate purpose or purposes." *Id.* § 1.157(a)(2) (Supp. 1980). The procedure for dissenting to such an amendment is set out in *id.* § 1.159 (1971).

The professional corporation acts in some states expressly permit conversion of a professional corporation into a business corporation. *See, e.g.*, FLA. STAT. ANN. § 621.13 (West Supp. 1981); MO. REV. STAT. ANN. § 356.170 (Vernon 1966).

A similar question with which the author will not deal in detail arises with respect to mergers. May an Oklahoma professional corporation merge with another corporation and, if so, under what circumstances? One can speculate that, at a minimum, it could merge with another domestic professional corporation rendering services in the same profession. Some state statutes have provisions dealing with the merger question. *See, e.g.*, FLA. STAT. ANN. § 621.13 (West Supp. 1981) (permitting mergers only with domestic professional corporations organized to render services in the same specific profession and prohibiting mergers with foreign corporations), and MINN. STAT. ANN. § 319A.15 (West Supp. 1981) (permitting mergers or consolidations with any corporation if the surviving or new corporation is a domestic or foreign professional corporation which complies with the Minnesota Professional Corporations Act).

76. 4 Okla. Op. Att'y Gen. 24 (1971).

77. See note 28 *supra* and accompanying text. The reverse of this question is whether a business corporation could convert into a professional corporation by amending its articles appro-

Finally, can shares in a professional corporation be involuntarily transferred to a non-professional? While the Act proscribes a voluntary transfer to anyone other than a licensed member of the profession,[78] the question of involuntary transfers through divorce, creditors', bankruptcy, or incompetency proceedings involving a corporate shareholder is left open. One author has stated, "[w]e might speculate as to the rights of an involuntary transferee, or the consequences of an involuntary transfer through bankruptcy or some creditors' proceeding, to a non-professional. This could conceivably result in dissolution proceedings."[79]

It might be argued that an involuntary transfer of shares should not and would not be permitted by a court. Florida case law is contrary to this proposition in holding that the professional corporation act does not prohibit an involuntary stock transfer via a sale of the stock to satisfy the judgment of a non-professional judgment creditor of a shareholder.[80] The court felt that a contrary rule would be discriminatory in giving "professionals a shelter for their assets, which appears to be inconsistent with the spirit of the Act [and would serve] to carve out a judicial 'no man's land' for shareholders in a professional corporation which is not available to shareholders in non-professional groups."[81]

If a court were to permit an involuntary transfer to a non-professional, the question of possible consequences would still remain. The involuntary transfer of a shareholder's stock in a professional corporation to a non-professional party might be grounds for an action by the Oklahoma Attorney General to cancel the articles of incorporation, although an involuntary transfer does not fit cleanly within any of the enumerated grounds for such action.[82] There is more likelihood that a director or the holder(s) of twenty percent or more of the shares of the

priately. In candor, it is improbable that such a situation will ever arise. If it did, similar logic would seem to apply.

78. OKLA. STAT. tit. 18, § 809 (1971).

79. Fleig, *supra* note 11, at 358.

80. Street v. Sugerman, 202 So. 2d 749 (Fla. 1967).

81. *Id.* at 751.

82. OKLA. STAT. tit. 18, § 1.198 (1971). These grounds are:

(1) The corporate franchise was procured through fraud practiced upon the State;
(2) The corporation could not lawfully have been formed . . . ;
(3) The corporation was formed without a substantial compliance with the conditions prescribed . . . as precedent or essential to incorporation;
(4) The corporation has persistently offended against any provision of the statutes regulating corporations or has persistently abused or usurped corporate privileges or powers;
(5) The corporation has knowingly and persistently violated any provision of the law;
(6) The corporation has done or omitted any act which amounts to a surrender of its

professional corporation could bring an action for involuntary dissolution[83] on the ground that it would be "beneficial to the interest of the shareholders that the corporation . . . be wound up and dissolved."[84]

Arguably, the statutory requirement that a professional corporation repurchase the shares of a disqualified shareholder,[85] discussed below, would apply in consequence of an involuntary transfer to a non-professional. Construing such an involuntary transfer as equivalent to a disqualification would certainly reinforce the statutory policy limiting ownership of a professional corporation to licensed members of the profession. However, the use of book value in the statutory repurchase scheme could result in repurchase from the transferee at an unfair price.[86]

As a practical matter, the problem of the involuntary transfer might be solved by the professional shareholders voluntarily dissolving the corporation[87] or themselves purchasing the shares involved.[88] In addition, the judge in a divorce proceeding, once educated to the problem, could structure his or her order to avoid an involuntary transfer.

V. Death or Disqualification of a Shareholder

The Professional Corporation Act allows the articles, by-laws or a private agreement to provide for the purchase or redemption of shares of a deceased or disqualified shareholder.[89] If this opportunity is not utilized, the Act requires the professional corporation to purchase the shares at book value determined "in accordance with the regular method of accounting used by such corporation."[90] In addition, the restrictions of the Business Corporation Act upon corporate repurchase of shares are inapplicable in the context of death or disqualification of

---

corporate franchise, has failed to exercise or has discontinued its corporate privileges, or has abandoned the corporate enterprise.

These grounds are directed at either problems with the organization of the corporation or wrongdoing attributable to the corporation. An involuntary transfer of the shares to a non-professional would seem to fall within neither category.

83. *Id.* § 1.196(a)(1), (2).

84. *Id.* § 1.195(3).

85. Okla. Stat. tit. 18, § 815 (Supp. 1980).

86. *See* notes 92 and 107-111 *infra* and accompanying text.

87. Okla. Stat. tit. 18, §§ 1.181 (1971) (dissolution by unanimous consent of shareholders) and 1.182 (Supp. 1980) (dissolution by shareholders upon resolution of board of directors).

88. This purchase could occur at the judicial sale or from a non-professional transferee after the judicial sale.

89. Okla. Stat. tit. 18, § 815 (Supp. 1980).

90. *Id.* If the corporation fails to purchase the share within ninety days, an action may be brought to enforce the statutory provision. *Id.*

a shareholder.[91]

This provision raises several questions. First, since disqualification seems to mean only being no longer licensed to render professional services, could a shareholder in a professional corporation force the repurchase of his shares by allowing his or her license to lapse?[92] The Act does not discriminate between voluntary and involuntary disqualifications, so presumably the repurchase requirement would apply. As a practical matter, this seems unlikely to occur. Book value as determined by the corporation's usual accounting method generally would not reflect unrealized appreciation, while depreciation would be reflected. The net result is that book value may not be commensurate with fair value, particularly if the professional corporation owns real estate, has investments or has employed a method of accelerated depreciation.[93]

Second, in the absence of a specific provision in the articles of incorporation, the by-laws, or a private agreement permitting dissolution as an alternative to purchase or redemption, could the remaining shareholders dissolve the corporation in lieu of purchasing the shares of the deceased or disqualified shareholder? One could argue that the word "redemption" would include a distribution upon dissolution. The problem with this approach is that the statutory provision mandates payment of book value at the "end of the month immediately preced-

---

91. *Id.* If the professional corporation has only one shareholder and that shareholder dies or becomes incompetent, the Act permits the personal representative of the shareholder to either sell the shares in the corporation or to dissolve the corporation. *Id.*

Query whether there are ethical limitations on the transfer of shares in a legal professional corporation to even a licensed member of the profession. *See* ABA COMM. ON PROFESSIONAL ETHICS, OPINIONS No. 266 (1945), stating:

> The goodwill of the practice of a lawyer is not, however, of itself an asset, which either he or his estate can sell. As said by the Committee on Professional Ethics of the New York County Lawyers' Association in its *Opinion* 109 (October 6, 1943);
>
> > Clients are not merchandise. Lawyers are not tradesmen. They have nothing to sell but personal service. An attempt, therefore, to barter in clients, would appear inconsistent with the best concepts of our professional status.

Id. at 552.

92. Fleig states: "It appears that the word disqualification, although not defined, is used in a technical sense and has reference to a loss of license to practice . . . ." Fleig, *supra* note 11, at 359. He interprets "disqualification" as *not* including disability, retirement or involuntary transfer. *Id.*

93. *See* Aldrich v. Geahry, 367 Pa. 252, __, 80 A.2d 59, 61 (1951) ("The book value of assets is rarely an accurate representation of the market value. Particularly is this true in a small closed corporation . . . ."). *Cf.* Mahan v. Mahan, 107 Ariz. 517, 489 P.2d 1197 (1971) (holding the book values of a partnership's assets were completely arbitrary). Sellin notes that the " 'book value' of a corporation's stock is not a valid measure of market value . . . ." H. SELLIN, ATTORNEY'S HANDBOOK OF ACCOUNTING 1-22 (1971).

ing the death or disqualification"[94] unless provision to the contrary is made in the articles, by-laws, or a private agreement. The dissolution distribution is unlikely to equal the book value contemplated by the Act.

Since the statutory provision is phrased in absolute terms and the Professional Corporation Act takes precedence over conflicting provisions of the Business Corporation Act,[95] it would appear that the corporation is required to repurchase the shares at book value. Presumably, the corporation could dissolve and distribute to the personal representative of the deceased shareholder or to the disqualified shareholder the book value of the shares prior to any distribution of assets to the remaining qualified shareholders. If the corporation were financially unable to repurchase the shares, dissolution would probably be necessary absent an infusion of new capital. The corporation would then seem to be required to pay the book value of the deceased or disqualified shareholder's shares before distributing any remaining assets to the qualified shareholders.

The statutory provision requires repurchase only in the event of the death or disqualification of a shareholder, and provides that the restrictions of the Business Corporation Act on repurchase of shares[96]

94. OKLA. STAT. tit. 18, § 815 (Supp. 1980).

95. *Id.* § 805 (1971).

96. The Act has two sections dealing with the subject of share repurchase, one entitled "Purchase and redemption of shares" and the other "When shares shall not be purchased." *Id.* §§ 1.136-1.137. Both substantially follow section IX of Hills' Model Corporation Act. Hills, *Model Corporation Act*, 48 HARV. L. REV. 1334, 1370 (1935). A key provision of the first is the requirement that shares be repurchased only out of earned surplus. OKLA. STAT. tit. 18, § 1.136(a)(1) (1971). An important element of the second is a prohibition against repurchase when the corporation is insolvent or would be rendered insolvent by the repurchase. *Id.* § 1.137(a)(1). Does the Professional Corporation Act render both of these provisions inapplicable to the repurchase of the shares of a deceased or disqualified shareholder of a professional corporation? Or is only the first provision, the earned surplus restiction, overridden?

The matter is not free from doubt. The first of the two sections uses the words "limitations" and "restrictions," stating that a "domestic corporation may, subject to the provisions of this Act and any further limitations or restrictions in the articles of incorporation, purchase or otherwise acquire its own shares only as follows . . . ." *Id.* § 1.136(a). The second of the two provisions states that no shares shall be repurchased when certain conditions, e.g. insolvency, exist. *Id.* § 1.137(a). It does not use the words "limit," "limitation," "restrict," or "restriction." Arguably, only the first of the provisions contains *restrictions*, while the second contains *prohibitions*. If this were the case, the second provision, containing the prohibition against repurchase while insolvent, would still apply to the repurchase by a professional corporation of the shares of a deceased or disqualified shareholder. This interpretation, however, depends on rather fine semantical distinctions and might run counter to the common usage of the word "restriction." On the other hand, there is no policy reason supporting the elimination, in this context, of the prohibition against an insolvent corporation repurchasing shares.

My discussion, *infra*, assumes that the Professional Corporation Act renders both of these provisions inapplicable, and will show that, even under this construction of the Act, a corpora-

are inapplicable to a corporate repurchase triggered by a shareholder's death or disqualification. By implication, this would mean that the restrictions *are* applicable to repurchases in any other context, e.g. retirement or disability.[97]

From this arises a third question, namely, what limitations are there upon a professional corporation's ability to repurchase shares upon death or disqualification of a shareholder? The Oklahoma Uniform Fraudulent Conveyances Act[98] makes a conveyance without fair consideration[99] by an insolvent or one who will thereby be rendered insolvent[100] fraudulent without regard to intent.[101] It would appear anomalous to consider a repurchase of shares by an insolvent professional corporation as being for fair consideration since it is nothing but a distribution of the corporation's assets to that shareholder. Thus, if a professional corporation were insolvent at the time of repurchase or would be rendered insolvent thereby, this provision would place a limit upon its ability to repurchase the shares of a deceased or disqualified shareholder.[102]

VI. CONCLUSION

While this article has examined a number of corporation law questions relating to professional corporations, it certainly has not exhausted all possible issues.[103] The reader, however, has been alerted to

---

tion's ability to repurchase its shares upon the death or disqualification of a shareholder is not without limit.

97. "If the redemption or repurchase by the corporation were not made by reason of death or disqualification, then the payment could only be made out of earned surplus . . . ." Fleig, *supra* note 11, at 359.

98. OKLA. STAT. tit. 24, §§ 101-111 (1971).

99. *Id.* § 103 defines "fair consideration":

> Fair consideration is given for property, or obligation
> (a) When in exchange for such property, or obligation, as a fair equivalent therefore, and in good faith, property is conveyed or an antecedent debt is satisfied, or
> (b) When such property, or obligation is received in good faith to secure a present advance or antecedent debt in amount not disproportionately small as compared with the value of the property, or obligation obtained.

100. *Id.* § 102 defines "insolvent": "A person is insolvent when the present fair salable value of his assets is less than the amount that will be required to pay his probable liability on his existing debts as they become absolute and matured." This definition appears to require a hypothetical liquidation of the corporation in order to answer the question of insolvency.

101. *Id.* § 104. In addition, the Bankruptcy Code allows a trustee in bankruptcy to avoid, as fraudulent, transfers which are made for less than a reasonably equivalent value by an insolvent or by one who will be rendered insolvent thereby. 11 U.S.C.A. § 548(a) (West 1979).

102. *Cf.* Powers v. Heggie, 167 N.E. 314 (Mass. 1929) (indicating that a payment of dividends to shareholders which was permissible under the applicable corporation law could still constitute a fraudulent conveyance and be recoverable from such shareholders).

103. For example, could a professional corporation utilize the Business Corporation Act pro-

the existence and nature of several such questions. Additionally, a case for legislative reappraisal of the Oklahoma Professional Corporation Act has been made. Matters which should be clarified by statutory amendment include questions regarding the validity of proxies and voting trusts, admission of foreign corporations, conversions into business corporations and involuntary transfers of shares. As to such questions, the answers given might not be as important as the availability of a clear answer.

In drafting statutory solutions to these problems, one point of reference could be the Professional Corporation Supplement to the Model Business Corporation Act.[104] This Model Act is, in the author's opinion, the result of careful and thoughtful work and could be of substantial aid in states, such as Oklahoma, where professional corporation statutes are "deficient with respect to matters of corporate procedure."[105] The Model Act contains provisions which answer most of the

---

vision permitting indemnification of an officer, employee or agent, OKLA. STAT. tit. 18, § 1.43a (1971), to indemnify one held liable for malpractice? Or would such an action conflict with the intent of the Professional Corporation Act that the professional relationship, including the liability of a person rendering professional services, not be altered by the Act? *Id.* § 812. *Cf.* Fla. Op. Att'y Gen. 062-31 (1962), *reprinted in* [1976] 2 PROF. CORP. GUIDE (P-H) ¶ 30,923 (the articles of a professional service corporation may include a provision indemnifying officers in the event of malpractice).

104. Committee on Corporate Laws, *Report, Professional Corporation Supplement to the Model Business Corporation Act*, 32 BUS. LAW. 289 (1976).

105. *Id.* at 289. In fairness, however, it should be noted that the Oklahoma Professional Corporation Act, even with its shortcomings, is still more comprehensive than the acts in some jurisdictions. For example, the Ohio Act is a woefully inadequate corporation statute. *See* OHIO REV. CODE ANN. § 1785.01-.08 (Baldwin,1979). The Ohio Act, like the Oklahoma Act, leaves unanswered questions about the validity of proxies and voting trusts, conversions of professional associations into business corporations, mergers of professional associations with other corporations, involuntary transfers of shares to non-professionals, and qualification of foreign professional corporations. Unlike the Oklahoma Act, however, the Ohio Act has no statutory solution to the problems of the death and disqualification of shareholders. In addition, the Ohio Act permits organization of a professional association only for the *sole purpose* of rendering professional services. *Id.* § 1785.01-02.

> This of course, raises a number of questions about the manner in which the professional association utilizes its funds. May the three shareholder medical association purchase land and build a one-story office building? May it build a ten-story office building if it only uses one-half of one floor? May it invest its excess funds in raw land or in an apartment project?
>
> The general corporation statute gives the professional association very broad powers in carrying out the purposes stated in its articles. However, since the purpose of a professional association must be limited to rendering a professional service, it is not clear what activities the association may properly undertake outside of those activities which specifically relate to rendering the professional service.

Smith, *Professional Corporations in Ohio: The Time for Statutory Revision*, 30 OHIO ST. L.J. 439, 447-48 (1969) (footnotes omitted).

These questions do not arise under the Oklahoma Act. See notes 27-28 *supra* and accompanying text.

open questions in Oklahoma.[106]

In addition, the concept of "book value" employed in the section of the Oklahoma Professional Corporation Act dealing with the repurchase of the shares of deceased or disqualified shareholders[107] should be discarded.

> If the corporation has engaged in permitted investment activities, such a formula is patently unfair, since generally accepted accounting principles require valuation of securities and other investments at either cost or the lower of cost or market. Book value, therefore, will not reflect unrealized appreciation in the value of investments, resulting in an inadequate return upon redemption.[108]

Perhaps the concept of "fair value" that is utilized in the Business Corporation Act[109] could be adopted. While this concept is not without its problems—such as being less objective than book value[110]—it would allow a court to attempt to do what is fair.[111]

Unless and until the Act is amended, counsel should utilize the opportunity under the current Professional Corporation Act to provide for the repurchase of the shares of a deceased or disqualified shareholder at a price other than the potentially harsh statutory book value standard that would otherwise apply.[112] By providing a reasonable and

106. For example, the Model Professional Corporation Act (hereinafter cited as M.P.C.A.) would prohibit a professional corporation from repurchasing the shares of a disqualified person if it was or would be rendered insolvent. M.P.C.A. § 7, *Report, supra* note 104, at 296. In addition, the M.P.C.A. would resolve the problem of the involuntary transfer of shares to an unqualified individual by treating the transfer in the same manner as the death or disqualification of a shareholder. M.P.C.A. § 10, *id.* at 299-301. Proxies would be valid under the M.P.C.A. only if given to a qualified person, and voting trusts would be valid only if the voting trustee and all beneficiaries were qualified persons. M.P.C.A. § 13, *id.* at 305. The M.P.C.A. would permit conversions of professional corporations into business corporations. M.P.C.A. § 17, *id.* at 307-08. And finally, the M.P.C.A. would allow admission of foreign professional corporations meeting the requirements of the Act. M.P.C.A. § 19, *id.* at 308-09.

107. OKLA. STAT. tit. 18, § 815 (Supp. 1980).

108. Note, *Professional Corporations: Analysis Under the Tax Reform Act and Survey of State Statutes*, 58 GEO. L.J. 487, 527-28 (1970) (footnotes omitted).

109. OKLA. STAT. tit. 18, § 1.159-.160 (1971) (dealing with rights of dissenting shareholders).

110. *See* Foglesong v. Thurston National Life Ins. Co., 555 P.2d 606 (Okla. 1976), and King v. Southwestern Cotton Oil Co., 585 P.2d 385 (Okla. App., 1978), construing the concept of "fair value."

111. The Model Professional Corporation Act uses the concept of "fair value," most likely in recognition of the inherent unfairness of the use of "book value" in the repurchase context. *M.C.P.A.* § 10, *Report, supra* note 104, at 299-301.

112. OKLA. STAT. tit. 18, § 815 (Supp. 1980). Counsel may, in addition, wish to provide for situations other than death or disqualification, such as the retirement or disability of a shareholder. If corporate repurchase is contemplated in contexts other than death or disqualification, then "appropriate provision should be made for creation of earned surplus . . . ." Fleig, *supra* note 11, at 359. *See* OKLA. STAT. tit. 18, § 1.136(a)(1) (1971). This could be done by "setting aside

fair method of valuation, counsel will help his or her clients avoid a Russian roulette situation in which the death or disqualification of a shareholder of the professional corporation may confer a significant portion of the value of his or her investment on the other shareholders.[113]

---

agreed annual sums for earnings . . . ." Fleig, *supra* note 11, at 359. To be on the safe side, counsel might wish to provide for purchase of the shares by shareholders in the event corporate repurchase would be unlawful due to inadequate earned surplus.

The accumulation of earnings raises the spectre of the accumulated earnings tax. I.R.C. §§ 531-537. One author concludes: "A number of courts have held that accumulations to fund entity buy-outs are reasonable needs of the business. The reasonable needs of the business test is usually met by providing for continuity of harmonious management. This would be buttressed by the state restrictions of ownership to licensed professionals . . . ." Brown, *Estate Planning for the Professional Corporation or Association*, 49 OKLA. B.J. 1765, 1766 (1978) (footnotes omitted). The author's discussion, of course, presupposes that the professional corporation is not a personal holding company. "In the case of personal holding companies, no taxable income may be accumulated." Kopple, *An Introduction to Buy-Sell Agreements for Closely-Held Corporations*, 4 ALI-ABA COURSE MATERIALS J. 4, 7 (April, 1980).

113. Query whether a failure to advise the professional client of this possibility could constitute actionable legal malpractice.