

## Major Changes to Pennsylvania Corporate Law Part 4: Fiduciary Duties and Fundamental Changes

PUBLISHED ON

**April 4, 2023**

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*This is Part 4 of a multipart series which will provide a summary of the key changes coming to Pennsylvania as a result of changes to the Pennsylvania Business Corporation Law (Title 15). Part 4 discusses concepts involving fiduciary duties when engaging in business transactions and internal fundamental changes to the processes of a corporation based on the updates to the Business Corporation Law.*

Act 122 went into effect January 2, 2023, implementing significant changes to Pennsylvania's Business Corporation Law, which sets forth the governing laws for all domestic and foreign entities operating under the laws of Pennsylvania. These changes affect how a business may conduct transactional work within the organization. Parts 1-3 of this series addressed the following topics:

- [Part 1](#): The repeal of decennial filings in favor of an annual reporting requirement;
- [Part 2](#): How business executives are losing their ability to maintain anonymity; and
- [Part 3](#): How entities will have more control over significant aspects of corporate governance if their organizational documents are updated accordingly.

Many of the changes to Pennsylvania's Business Corporation Law provide clarity to existing concepts or expand such concepts to additional situations. Namely, several of the recent changes involve the fiduciary duties directors and officers owe to a corporation, as well as altering internal fundamental processes, including:

- Directors and officers are afforded a statutory business judgment standard which affords the duty of care that must be exercised in making business decisions;
- A transaction is not automatically void because the contracting entities share the same directors or officers;
- Shareholders are provided an opportunity for involvement when undertaking fundamental changes of the organization; and
- Alternative methods of valuation are set forth for determining whether an organization has sold all, or substantially all, of its assets.

### **Business Judgment Rule**

In response to a case from the Southern District of New York interpreting Pennsylvania Law, the Business Corporation Law rejected the decision of the Southern District of New York and clarified that a directors' duty to conduct a reasonable inquiry into potential issues only extends so far as is required by Pennsylvania statutory law and those inquiries the director chooses to consider. This is contrary to the open-ended duty of directors to inquire into matters beyond statutory requirements as was contemplated in the decision by the

Court in the Southern District of New York. Further, a director who makes business judgments in good faith fulfills the director's duty if:

- The subject matter does not involve self-dealing;
- The director is informed and reasonably believes the action to be appropriate under the circumstances; and
- The director rationally believes the business judgment is in the best interests of the corporation.

Further, the Business Corporation Law also adopts a similar statutory business judgment rule for officers of an organization. Under this standard, an officer must rationally believe that a business decision is in the best interests of the corporation. Similar to directors, this permits officers to justifiably rely on information received from or prepared by others (i.e., attorneys, accountants, etc.), for their decision making.

The phrase "rationally believes" provides directors and officers with a significantly wider range of discretion than was previously granted by the "reasonably believes" standard. The prior "reasonable" standard turns on what other individuals (i.e., a "reasonable person") would determine is in the best interests of the company under the circumstances, whereas the "rational" standard looks more specifically at whether the directors and officers acted logically, given the circumstances.

## **Interested Directors or Officers**

The recent additions to the Business Corporation Law address the validity of a transaction involving two (2) entities that share the same directors or officers, specifically in the context of wholly owned associations and non-wholly owned associations. For transactions between a business corporation and a wholly owned association, the fact that an officer or director serves in such capacity for both entities alone will not render the entire transaction void (or voidable). The same holds true for non-wholly owned associations *if* one of the following requirements are met:

- The material facts of the relationship or interest as to the transaction are disclosed to the board of directors, and authorized by an affirmative vote of the disinterested directors (even if the disinterested directors are less than a quorum);
- The material facts of the relationship or interest as to the transaction are disclosed to the shareholders entitled to vote on the transaction, and such shareholders approve the transaction in a good faith vote;
- The transaction is fair (to the corporation) when approved/authorized by the directors and shareholders; or
- The directors or officers serving as such for both entities involved in the transaction neither participate in the negotiations of the transaction in a substantial or personal manner for either entity, nor is their vote required at a meeting for either entity to approve the transaction.

These changes provide clarity in situations where there may be a conflict when a transaction or agreement arises with another entity with which the business corporation shares a director(s) or officer(s). In providing these additional details, corporations can proceed with such opportunity (provided such requirements are met), knowing that the fact that interested directors are involved does not void the entire transaction. The Business Corporation Law included a nearly identical provision extending these concepts to nonprofit corporations as well.

## **Fundamental Changes of the Organization**

Other important changes imposed by the Business Corporation Law relate to fundamental changes of the

organization. Such changes expand prior provisions of the Business Corporation Law, providing additional guidance as to how corporations should proceed in the following circumstances:

- The Business Corporation Law changes expand the provision that separate approval by the board of directors is not required when there is unanimous agreement (or consent in record form) by the shareholders to fundamental transactions requiring that a plan of asset transfer be proposed or approved by the board.
- The recent changes provide for a new avenue to amend a corporation's articles of incorporation. Proposals of amendments to the articles of incorporation may be submitted by the board of directors directly to the shareholders without first being adopted by the board of directors.
- The updates explain what information can be utilized when determining whether a corporation has disposed of all or substantially all of its property and assets. The determination may be based on the financial statements of the organization or a balance sheet that reflects certain valuations, such as the book value of the assets, unrealized appreciation and depreciation of the assets, the current value of the corporation's assets, and other reasonable methods.
- Additional clarity was provided with respect to late-filed actions/proceedings initiated after a dissolution. Upon the commencement of a late-filed action or proceeding against a dissolved corporation (an action filed more than two (2) years after the date of dissolution or the period of time otherwise specified by law, whichever is less), any directors, officers or shareholders of the dissolved corporation (when the dissolution became effective), or of a successor entity (or any successor-in-interest to such individuals) may act on behalf of the corporation in connection with the action or proceeding that has been filed.

Please contact attorneys [Charmaine E. Nyman](#) and [Rachael E. Shaw](#) or any member of the [Barley Snyder Business Practice Group](#) if you have any questions about the changes to the Pennsylvania Business Corporation Law, or if you would like assistance in updating your corporate documents to address these changes.

*Stay tuned for additional alerts discussing how these changes could impact your entity and how Barley Snyder can help ensure compliance with the Pennsylvania Business Corporation Law. Also, be on the lookout for a future alert on how the changes will impact internal corporate procedures.*

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