



BUSINESS LAW SECTION

THE STATE BAR OF CALIFORNIA

LEGISLATIVE PROPOSAL (BLS-2006-01): CALIFORNIA GENERAL CORPORATION LAW: TECHNICAL CORRECTIONS

TO: Larry Doyle, Office of Governmental Affairs, California State Bar

FROM: Jeffrey C. Selman, Vice-Chair,
Legislation of the Executive Committee of the State Bar

DATE: June 6, 2005

RE: Proposal to amend §§114, 600, 603, 1301, 1501, 8321, 12591, 15634, 17106 and
28501 of the Corporations Code of the State of California

SECTION ACTION:

(Approved by BLS Executive Committee May 20, 2005)
(Approved by Corporations Committee May 6, 2005)

SECTION CONTACTS:

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HISTORY, DIGEST AND PURPOSE

The mission statement of the Corporations Committee (the “Committee”) provides that it shall study, consider, take a position and advocate that position with respect to, among other things,

“statutory changes that would promote efficiency or effectiveness in practice.” The Committee has concluded that amending Sections 114, 600, 603, 1301, 1501, 8321, 12591, 15634, 17106 and 28501 of the Corporations Code (the “Code”) will promote such efficiency and effectiveness by providing consistency to applicable accounting principles and Section 307 of the Code. The Committee recommends that Section 114 be amended to include statements of cash flows and comparable statements, that Sections 1501, 8321, 12591, 15634, 17106 and 28501 be amended to add “cash flows or” before “changes in financial position”, that Section 600 be amended to correct a typographical error, that Section 603 be amended to change the reference to “signed” to “provided” and that Section 1301 be amended to correct a typographical error.

1. Background.

(a) Sections 114, 1501(a), 8321(a)(1), 12591(a)(1), 15634(c)(1), 17106(c)(1) and 28501(a) of the Code refer to financial statement requirements for various entities. Those sections refer to “statements of changes in financial position,” a term that has been replaced in most cases under applicable accounting principles^a with “statements of cash flows.” Thus, the Sections should provide for statements of cash flows. These changes would be consistent with the requirements of Sections 5012 and 12217 of the Code.

(b) The reference in Section 600(b) to “regulated management companies,” as defined in Section 23701m of the Revenue and Taxation Code, was added to the Code in 1987. At that time, Section 23701m read, “Sections 851 to 855, inclusive, of the Internal Revenue Code, relating to regulated investment companies, shall be applicable for purposes of this chapter, except Section 852(b)(1) of the Internal Revenue Code shall not apply.” Internal Revenue Code Section 851 provides the definition of a “regulation investment company.” When Section 23701m was repealed by the California legislature in 1988, no corresponding reference was provided in either the Corporations Code or the Revenue and Taxation Code that would provide a definition of “regulated management companies” under Section 600(b).

(c) Section 603(a) of the Code refers to consents “signed” by shareholders. On January 1, 2005, SB 1306 became effective and expressly authorized the use of electronic transmission for deliveries of notices and written consents, among others. In various parts of the Code, e.g., Section 307(a), the word “signs” was replaced with “provides”. As a result of an error, that change was not made to Section 603 governing the delivery of written consents by shareholders. As a result the correct term should be “provided” to make it consistent with the changes adopted pursuant to SB 1306.

(d) Section 1301(b) of the Code contains a typographical error. It refers to clauses “(i) or (ii) of paragraph (1) of subdivision (b) of Section 1300”. However, Section 1300(b)(1) contains clauses numbered (A) and (B); it does not contain clauses numbered (i) or (ii). The reference to clauses “(i)” and “(ii)” in Section 1301(b) should be replaced with “(A)” and “(B)”.

Therefore, the Committee unanimously recommends making the technical corrections described in this proposal to clarify the Code.

^a See Statement of Financial Accounting Standards No. 95 (1987).

2. Amendments. Section 114 would be amended to include statements of cash flows and comparable statements, Sections 1501(a), 8321(a)(1), 12591(a)(1), 15634(c)(1), 17106(c)(1) and 28501(a) would be amended to add “cash flows or” before “changes in financial position”, Section 600(b) would be amended to correct a typographical error, Section 603(a) would be amended to replace “signed” with “provided” and Section 1301(b) would be amended to correct a typographical error.

APPLICATION

If adopted, the proposed amendment would be effective January 1, 2007.

PENDING LITIGATION

None to our knowledge.

LIKELY SUPPORT AND OPPOSITION

Support from corporations and professionals providing services to such companies. No opposition expected.

FISCAL IMPACT

None expected.

GERMANENESS

The subject matter of this proposal is one in which the members of the Business Law Section have special experience, and which requires their special knowledge, training and technical expertise. In addition, the proposed statute will promote clarity, consistency and comprehensiveness in the law.

TEXT OF PROPOSAL

SECTION 1. Section 114 of the Corporations Code is amended, to read:

§ 114. All references in this division to financial statements, balance sheets, income statements, statements of cash flows and statements of changes in financial position of a corporation and all references to assets, liabilities, earnings, retained earnings, and similar accounting items of a corporation mean such financial statements, ~~or~~ such items or comparable statements or items prepared or determined in conformity with generally accepted accounting principles then applicable, fairly presenting in conformity with generally accepted accounting principles the matters which they purport to present, subject to any specific accounting treatment required by a particular section of this division. Unless otherwise expressly stated, all references in this division to such financial statements mean, in the case of a corporation which has subsidiaries, consolidated statements of the corporation and such of its subsidiaries as are required to be included in such consolidated statements under generally accepted accounting principles then applicable and all references to such accounting items mean such items determined on a consolidated basis in accordance with such consolidated financial statements. Financial statements other than annual statements may be condensed or otherwise presented as permitted by authoritative accounting pronouncements.

SECTION 2. Section 600 of the Corporations Code is amended to read:

§ 600. (a) Meetings of shareholders may be held at such place within or without this state as may be stated in or fixed in accordance with the bylaws. If no other place is stated or so fixed, shareholder meetings shall be held at the principal executive office of the corporation.

(b) An annual meeting of shareholders shall be held for the election of directors on a date and at a time stated in or fixed in accordance with the bylaws. However, if the corporation is a regulated management company, as defined in Section ~~23704~~ **851** of the **United States Internal Revenue and Taxation Code relating to regulated investment companies**, a meeting of shareholders shall be held as required by the Federal Investment Company Act of 1940 (15 U.S.C. Sec. 80a-1, *et seq.*) Any other proper business may be transacted at the annual meeting.

(c) If there is a failure to hold the annual meeting for a period of 60 days after the date designated therefore, or, if no date has been designated, for a period of 15 months after the organization of the corporation or after its last annual meeting, the superior court of the proper county may summarily order a meeting to be held upon the application of any shareholder after notice to the corporation giving it an opportunity to be heard. The shares represented at such meeting, either in person or by proxy, and entitled to vote thereat shall constitute a quorum for the purposes of such meeting, notwithstanding any provision of the articles or bylaws or in this division to the contrary. The court may issue such orders as may be appropriate, including, without limitation, orders designating the time and place of such meeting, the record date for determination of shareholders entitled to vote and the form of notice of such meeting.

(d) Special meetings of the shareholders may be called by the board, the chairman of the board, the president or holders of shares entitled to cast not less than 10 percent of the votes at the meeting or such additional persons as may be provided in the articles or bylaws.

SECTION 3. Section 603 of the Corporations Code is amended to read:

§ 603. (a) Unless otherwise provided in the articles, any action that may be taken at any annual or special meeting of shareholders may be taken without a meeting and without prior notice, if a consent in writing, setting forth the action so taken, shall be **provided** signed by the holders of outstanding shares having not less than the minimum number of votes that would be necessary to authorize or take that action at a meeting at which all shares entitled to vote thereon were present and voted.

(b) Unless the consents of all shareholders entitled to vote have been solicited in writing, both of the following shall apply:

(1) Notice of any shareholder approval pursuant to Section 310, 317, 1152, 1202 or 2007 without a meeting by less than unanimous written consent shall be given at least 10 days before the consummation of the action authorized by that approval. Notice shall be given as provided in subdivision (b) of Section 601.

(2) Prompt notice shall be given of the taking of any other corporate action approved by shareholders without a meeting by less than unanimous written consent, to those shareholders entitled to vote who have not consented in writing. Notice shall be given as provided in subdivision (b) of Section 601.

(c) Any shareholder giving a written consent, or the shareholder's proxyholders, or a transferee of the shares or a personal representatives of the shareholder or their respective proxyholders, may revoke the consent personally or by proxy by a writing received by the corporation prior to the time that written consents of the number of shares required to authorize

the proposed action have been filed with the secretary of the corporation, but may not do so thereafter. The revocation is effective upon its receipt by the secretary of the corporation.

(d) Notwithstanding subdivision (a), directors may not be elected by written consent except by unanimous written consent of all shares entitled to vote for the election of directors; provided that the shareholders may elect a director to fill a vacancy, other than a vacancy created by removal, by the written consent of a majority of the outstanding shares entitled to vote.

SECTION 4. Section 1301 of the Corporations Code is amended to read:

§ 1301. (a) If, in the case of a reorganization, any shareholders of a corporation have a right under Section 1300, subject to compliance with paragraphs (3) and (4) of subdivision (b) thereof, to require the corporation to purchase their shares for cash, such corporation shall mail to each such shareholder a notice of the approval of the reorganization by its outstanding shares (Section 152) within 10 days after the date of such approval, accompanied by a copy of Sections 1300, 1302, 1303, 1304 and this section, a statement of the price determined by the corporation to represent the fair market value of the dissenting shares, and a brief description of the procedure to be followed if the shareholder desires to exercise the shareholder's right under subsection sections. The statement of price constitutes an offer by the corporation to purchase at the price stated any dissenting shares as defined in subdivision (b) of Section 1300, unless they lose their status as dissenting shares under Section 1309.

(b) Any shareholder who has a right to require the corporation to purchase the shareholder's shares for cash under Section 1300, subject to compliance with paragraphs (3) and (4) of subdivision (b) thereof, and who desires the corporation to purchase such shares shall make written demand upon the corporation for the purchase of such shares and payment to the shareholder in cash of their fair market value. The demand is not effective for any purpose unless it is received by the corporation or any transfer agent thereof (1) in the case of shares described in clause **(A) or (B)** ~~(i) or (ii)~~ of paragraph (1) of subdivision (b) of Section 1300 (without regard to the provisos in that paragraph), not later than the date of the shareholders' meeting to vote upon the reorganization, or (2) in any other case within 30 days after the date on which the notice of the approval by the outstanding shares pursuant to subdivision (a) or the notice pursuant to subdivision (i) of Section 1110 was mailed to the shareholder.

(c) The demand shall state the number and class of the shares held of record by the shareholder which the shareholder demands that the corporation purchase and shall contain a statement of what such shareholder claims to be the fair market value of those shares as of the date before the announcement of the proposed reorganization or short-form merger. The statement of fair market value constitutes an offer by the shareholder to sell the shares at such price.

SECTION 5. Section 1501 of the Corporations Code is amended to read:

§ 1501. (a) The board shall cause an annual report to be sent to the shareholders not later than 120 days after the close of the fiscal year, unless in the case of a corporation with less than 100 holders of record of its shares (determined as provided in Section 605) this requirement is expressly waived in the bylaws. Unless otherwise provided by the articles or bylaws and if approved by the board of directors, that report and any accompanying material sent pursuant to this section may be sent by electronic transmission by the corporation (Section 20). This report shall contain a balance sheet as of the end of that fiscal year and an income statement and a statement of **cash flows or** changes in financial position for that fiscal year, accompanied by any

report thereon of independent accountants or, if there is no such report, the certificate of an authorized officer of the corporation that the statements were prepared without audit from the books and records of the corporation.

Unless so waived, the report shall be sent to the shareholders of at least 15 (or, if sent by third-class mail, 35) days prior to the annual meeting of shareholders to be held during the next fiscal year, but this requirement shall not limit the requirement for holding an annual meeting as required by Section 600.

Notwithstanding Section 114, the financial statements of any corporation with fewer than 100 holders of record of its shares (determined as provided in Section 605) required to be furnished by this subdivision and subdivision (c) are not required to be prepared in conformity with generally accepted accounting principles if they reasonably set forth the assets and liabilities and the income and expense of the corporation and disclose the accounting basis used in their preparation.

(b) In addition to the financial statements required by subdivision (a), the annual report of any corporation having 100 or more holders of record of its shares (determined as provided in Section 605) either not subject to the reporting requirements of Section 13 of the Securities Exchange Act of 1934,^b or exempted from those reporting requirements by Section 12(g)(2)^c of that act, shall also describe briefly both of the following:

(1) Any transaction (excluding compensation of officers and directors) during the previous fiscal year involving an amount in excess of forty thousand dollars (\$40,000) (other than contracts let at competitive bid or services rendered at prices regulated by law) to which the corporation or its parent or subsidiary was a party and in which any director or officer of the corporation or of a subsidiary or (if known to the corporation or its parent or subsidiary) any holder of more than 10 percent of the outstanding voting shares of the corporation had a direct or indirect material interest, naming the person and stating the person's relationship to the corporation, the nature of the person's interest in the transaction and, where practicable, the amount of the interest; provided that in the case of a transaction with a partnership of which the person is a partner, only the interest of the partnership need be stated; and provided further that no such report need be made in the case of any transaction approved by the shareholders (Section 153).

(2) The amount and circumstances of any indemnification or advances aggregating more than ten thousand dollars (\$10,000) paid during the fiscal year to any officer or director of the corporation pursuant to Section 317; provided that no such report need be made in the case of indemnification approved by the shareholders (Section 153) under paragraph (2) of subdivision (e) of Section 317.

(c) If no annual report for the last fiscal year has been sent to shareholders, the corporation shall, upon the written request of any shareholder made more than 120 days after the close of that fiscal year, deliver or mail to the person making the request within 30 days thereafter the financial statements required by subdivision (a) for that year. A shareholder or shareholders holding at least 5 percent of the outstanding shares of any class of a corporation may make a written request to the corporation for an income statement of the corporation for the three-month, six-month or nine-month period of the current fiscal year ended more than 30 days prior to the date of the request and a balance sheet of the corporation as of the end of the period

^b 15 U.S.C.A. § 7002(a)(2)(B).

^c 15 U.S.C.A. § 7001.

and, in addition, if no annual report for the last fiscal year has been sent to shareholders, the statements referred to in subdivision (a) for the last fiscal year. The statements shall be delivered or mailed to the person making the request within 30 days thereafter. A copy of the statements shall be kept on file in the principal office of the corporation for 12 months and it shall be exhibited at all reasonable times to any shareholder demanding an examination of the statements or a copy shall be mailed to the shareholder.

(d) The quarterly income statements and balance sheets referred to in this section shall be accompanied by the report thereon, if any, of any independent accountants engaged by the corporation or the certificate of an authorized officer of the corporation that the financial statements were prepared without audit from the books and records of the corporation.

(e) In addition to the penalties provided for in Section 2200, the superior court of the proper county shall enforce the duty of making and mailing or delivering the information and financial statements required by this section and, for good cause shown, may extend the time therefore.

(f) In any action or proceeding under this section, if the court finds the failure of the corporation to comply with the requirements of this section to have been without justification, the court may award an amount sufficient to reimburse the shareholder for the reasonable expenses incurred by the shareholder, including attorneys' fees, in connection with the action or proceeding.

(g) This section applies to any domestic corporation and also to a foreign corporation having its principal executive office in this state or customarily holding meetings of its board in this state.

SECTION 6. Section 8321 of the Corporations Code is amended to read:

§ 8321. (a) A corporation shall notify each member yearly of the member's right to receive a financial report pursuant to this subdivision. Except as provided in subdivision (c), upon written request of a member the board shall promptly cause the most recent annual report to be sent to the requesting member. An annual report shall be prepared not later than 120 days after the close of the corporation's fiscal year. Unless otherwise provided by the articles or bylaws and if approved by the board of directors, that report and any accompanying material may be sent by electronic transmission by the corporation (Section 20), That report shall contain in appropriate detail the following.

(1) A balance sheet as of the end of such fiscal year and an income statement and statement of **cash flows or** changes in financial position for such fiscal year.

(2) A statement of the place where the names and addresses of the current members are located.

(3) Any information required by Section 8322.

(b) The report required by subdivision (a) shall be accompanied by any report thereon of independent accountants, or, if there is no such report, the certificate of an authorized officer of the corporation that such statements were prepared without audit from the books and records of the corporation.

(c) Subdivision (a) does not apply to any corporation which receives less than ten thousand dollars (\$10,000) in gross revenues or receipts during the fiscal year.

SECTION 7. Section 12591 of the Corporations Code is amended to read:

§ 12591. (a) A corporation shall notify each member yearly of the member's right to receive a financial report pursuant to this subdivision. Except as provided in subdivision (c), upon written request of a member the board shall promptly cause the most recent annual report to be sent to the requesting member. An annual report shall be prepared not later than 120 days after the close of the corporation's fiscal year. Unless otherwise provided by the articles or bylaws and if approved by the board of directors, that report and any accompanying material sent pursuant to this section may be sent by electronic transmission by the corporation (Section 20). That report shall contain in appropriate detail the following.

(1) A balance sheet as of the end of such fiscal year and an income statement and statement of **cash flows or** changes in financial position for such fiscal year.

(2) A statement of the place where the names and addresses of the current members are located.

(3) Any information required by Section 12592.

(b) The report required by subdivision (a) shall be accompanied by any report thereon of independent accountants, or, there is no such report, the certificate of an authorized officer of the corporation that such statements were prepared without audit from the books and records of the corporation.

(c) This section does not apply to corporations which do not have more than 25 members at any time during the fiscal year.

SECTION 8. Section 15634 of the Corporations Code is amended to read:

§ 15634. (a) Upon the request of a limited partner, the general partners shall promptly deliver to the limited partner, at the expense of the partnership, a copy of the information required to be maintained by subdivision (a) (b), or (d) of Section 15615.

(b) Each limited partner has the right upon reasonable request to each of the following:

(1) Inspect and copy during normal business hours any of the partnership records required to be maintained by Section 15615.

(2) Obtain from the general partners, promptly after becoming available, a copy of the limited partnership's federal, state and local income tax or information returns for each year.

(c) In the case of any limited partnership with more than 35 limited partners:

(1) The general partners shall cause an annual report to be sent to each of the partners not later than 120 days after the close of the fiscal year. That report shall contain a balance sheet as of the end of the fiscal year and an income statement and statement of **cash flows or** changes in financial position for the fiscal year.

(2) Limited partners representing at least 5 percent of the interests of limited partners may make a written request to a general partner for an income statement of the limited partnership for the initial three-month, six-month, or nine-month period of the current fiscal year ended more than 30 days prior to the date of the request and a balance sheet of the partnership as of the end of that period. The statement shall be delivered or mailed to the limited partners within 30 days thereafter.

(3) The financial statements referred to in this section shall be accompanied by the report thereon, if any, of the independent accountants engaged by the partnership or, if there is no such report, the certificate of a general partner of the partnership that such financial statements were prepared without audit from the books and records of the limited partnership.

(d) The general partners shall promptly furnish to a limited partner a copy of any amendment to the partnership agreement executed by a general partner pursuant to a power of attorney from the limited partner.

(e) The general partners shall send to each of the partners within 90 days after the end of each taxable year such information as is necessary to complete federal and state income tax or information returns, and, in the case of a limited partnership with 35 or fewer limited partners, a copy of the limited partnership's federal, state, and local income tax or information returns for the year.

(f) In addition to any other remedies, a court of competent jurisdiction may enforce the duty of making and mailing or delivering the information and financial statements required by this section and, for good cause shown, may extend the time therefore.

(g) In any action under this section, if the court finds the failure of the partnership to comply with the requirements of this section to have been without justification, the court may award an amount sufficient to reimburse the partners bringing the action for the reasonable expenses incurred by the partners, including attorneys' fees, in connection with the action or proceeding.

(h) Any waiver by a partner of the rights provided in this section shall be unenforceable.

(i) Any request, inspection, or copying by a limited partner may be made by the limited partner or by the limited partner's agent or attorney.

SECTION 9. Section 17106 of the Corporations Code is amended to read:

§ 17106. (a) Upon the request of a member or a holder of an economic interest, for purposes reasonably related to the interest of that person as a member or a holder of an economic interest, a manager shall promptly deliver, in writing, to the member or holder of an economic interest, at the expense of the limited liability company, a copy of the information required to be maintained by paragraphs (1) (2), and (4) of subdivision (a) of Section 17058, and any written operating agreement of the limited liability company.

(b) Each member, manager, and holder of an economic interest has the right upon reasonable request, for purposes reasonably related to the interest of that person as a member, manager, or holder of an economic interest, to each of the following:

(1) To inspect and copy during normal business hours any of the records required to be maintained by Section 17058.

(2) To obtain in writing from the limited liability company promptly after becoming available, a copy of the limited liability company's federal, state, and local income tax or information returns for each year.

(c) In the case of any limited liability company with more than 35 members:

(1) A manager shall cause an annual report to be sent to each of the members not later than 120 days after the close of the fiscal year. That report, which may be sent by electronic transmission by the limited liability company (paragraph (1) of subdivision (o) of Section 17001), shall contain a balance sheet as of the end of the fiscal year and an income statement and statement of **cash flows or** changes in financial position for the fiscal year.

(2) Members representing at least 5 percent of the voting interests of members, or three or more members, may make a written request to a manager for an income statement of the limited liability company for the initial three-month, six-month, or nine-month period of the current fiscal year ended more than 30 days prior to the date of the request, and a balance sheet of the limited

liability company as of the end of that period. The statement shall be delivered or mailed to the members within 30 days thereafter.

(3) The financial statements referred to in this section shall be accompanied by the report thereon, if any, of the independent accountants engaged by the limited liability company, or, if there is no report, the certificate of a manager of the limited liability company that the financial statements were prepared without audit from the books and records of the limited liability company.

(d) A manager shall promptly furnish to a member a copy of any amendment to the articles of organization or operating agreement executed by a manager pursuant to a power of attorney from the member. The articles of organization or operating agreement may be sent by electronic transmission by the limited liability company.

(e) The limited liability company shall send or cause information to be sent in writing to each member or holder of an economic interest within 90 days after the end of each taxable year such information as is necessary to complete federal and state income tax or information returns, and, in the case of a limited liability company with 35 or fewer members, a copy of the limited liability company's federal, state, and local income tax or information returns for the year.

(f) In addition to any other remedies, a court of competent jurisdiction may enforce the duty of making and mailing or delivering the information and financial statements required by this section and, for good cause shown, may extend the time therefor.

(g) In any action under this section, if the court finds the failure of the limited liability company to comply with the requirements of this section is without justification, the court may award an amount sufficient to reimburse the person bringing the action for the reasonable expenses incurred by that person, including attorneys' fees, in connection with the action or proceeding.

(h) Any waiver of the rights provided in this section shall be unenforceable.

(i) Any request, inspection, or copying by a member or holder of an economic interest may be made by that person or by that person's agent or attorney.

SECTION 10. Section 28501 of the Corporations Code is amended to read:

§ 28501. Each licensee shall, not more than 90 days after the close of each of its fiscal years or within a longer period that the commissioner may by regulation or order specify, file with the commissioner an audit report containing all of the following:

(a) Financial statements (including balance sheets, statements of income or loss, statements of changes in capital accounts, and statements of **cash flows or** changes in financial position or, in the case of a licensee that is a California nonprofit corporation, comparable financial statements) for, or as of, the end of the fiscal year, prepared, with audit, by an independent verified public accountant in accordance with generally accepted accounting principles.

(b) A report, certificate, or opinion of the independent certified public accountant or independent public accountant, stating that the financial statements were prepared in accordance with generally accepted accounting principles.

(c) Any other information that the commissioner may by regulation or order require.