

**RESOLUTION 05-01-08**

**DIGEST**

Revenue and Tax Code: Tax Credits for Use of Public Transportation and Ridesharing  
Adds Revenue and Tax Code section 22000 to provide a 35% tax credit to employers and employees for the cost of using public transportation and ridesharing.

**RESOLUTIONS COMMITTEE RECOMMENDATION**

APPROVE IN PRINCIPLE

History:

No similar resolutions found.

Reasons:

This resolution adds Revenue and Tax Code section 22000 to provide a 35% tax credit to employers and employees for the cost of using public transportation and ridesharing. This resolution should be approved in principle because it encourages the use of public transportation , and is better for the environment.

This resolution also allows employees a 35% tax credit for the amount employees receive as reimbursements from their employers. It also allows the credits, if unused, to carry over to subsequent tax years. The purpose of the credits is to provide incentives to employers and employees to establish and utilize employer-sponsored “qualified transportation commuting” expense reimbursement programs, which encourages the use of public transportation, ridesharing, use of electric, fuel cell, or other zero carbon emission vehicles, including bicycles.

**TEXT OF RESOLUTION**

RESOLVED, that the Conference of Delegates of California Bar Associations recommends that legislation be sponsored to add Revenue & Tax Code section 22000 to read as follows:

- 1    §22000
- 2           (a) For each taxable year beginning on or after the effective date of this legislation,
- 3    there shall be allowed as a credit against the amount of "net tax" (as defined in Section
- 4    17039 of the Revenue & Tax Code) an amount equal to the amount determined in
- 5    subdivisions (b) and (c).
- 6           (b) The amount of the credit allowed to the employer by this division shall be as
- 7    follows:
- 8           (1) The credit shall be thirty-five percent of the cost paid or incurred by an
- 9    employer in reimbursing employees for qualified transportation commuting expenses, as
- 10   defined in this division, as part of an employer-sponsored qualified transportation
- 11   commuting incentive program for employees.
- 12           (2) The credit provided in this subdivision shall be claimed in the state income tax
- 13   return for the taxable year in which those qualified transportation commuting expenses are
- 14   reimbursed to the employees.

15 (c) The amount of the credit allowed to the employee by this division shall be as  
16 follows:

17 (1) The credit shall be thirty-five percent of the amount received by the employee  
18 from their employer as a reimbursement for qualified transportation commuting expenses,  
19 as defined in this division, as part of an employer-sponsored qualified transportation  
20 commuting incentive program for employees.

21 (2) The credit provided in this subdivision shall be claimed in the state income tax  
22 return for the taxable year in which those qualified transportation commuting expenses are  
23 received.

24 (d) If an employer and employee elect to receive the credits allowed in subdivisions  
25 (b) and (c), they shall do all of the following:

26 (1) The employee shall keep a contemporaneous log of qualifying transportation  
27 commuting information. The log information shall include, but not be limited to, dates and  
28 times qualified transportation was used in commuting, the type of transportation used, the  
29 miles traveled while ridesharing if ridesharing, as defined in this division, and any  
30 expenses incurred by the employee in using such qualified transportation.

31 (2) The employee shall turn over the information required by paragraph (d)(1) to  
32 their employer at some time before the state income tax return for the taxable year in which  
33 the qualified transportation commuting expenses were incurred is due. The date of receipt  
34 of the employee's log shall be decided by the employer, and the employer shall give notice  
35 to the employee of such date of receipt.

36 (3) The employer shall review the information required by paragraph (d)(1) and  
37 reimburse the employee for all qualified transportation commuting expenses, as defined in  
38 this division. The employer shall keep a record of all such reimbursements.

39 (4) Both the employer and the employee shall retain a copy of the information  
40 required by paragraph (d)(1) and shall provide such information upon the request of the  
41 Franchise Tax Board.

42 (e) In the case where the credit allowed by this section exceeds the "net tax," the  
43 excess may be carried over to reduce the "net tax" in the following years and succeeding  
44 years if necessary, until the credit has been exhausted.

45 (f) For purposes of this section:

46 (1) "Employer" means a taxpayer for whom services are performed by an  
47 employee.

48 (2) "Employee" means an individual who performs services for an employer for  
49 more than 10 hours per week for remuneration, and who commutes to and from work using  
50 Qualified Transportation at least three days a week or 15 days per month during any one or  
51 more months of the year.

52 (3) "Employer-sponsored qualified transportation commuting incentive program for  
53 employees" is a program an employer can elect to provide for employees as an incentive to  
54 conserve energy, prevent pollution and reduce carbon emissions by using Qualified  
55 Transportation while commuting to the employer's place of business to provide services as  
56 an employee.

57 (4) "Qualified transportation commuting expenses" mean any expenses incurred by  
58 an employee commuting to or from the employer's place of business to provide services as  
59 an employee while using qualified transportation, as defined in this division. The allowed  
60 expense for transportation by ridesharing and zero carbon emission vehicles, including

61 bicycle, shall be the per mile allowed business expense deduction for business travel miles  
62 by automobile for the applicable tax year as determined by the Federal Internal Revenue  
63 Code.

64 (5) "Qualified Transportation" includes public transportation and ridesharing, as  
65 both are defined in this division, use of an electric, fuel cell or other zero carbon emission  
66 vehicle, or use of a bicycle.

67 (6) "Public transportation" means a public bus system, train, tram, trolley, or any  
68 other public transportation the Franchise Tax Board deems acceptable.

69 (7) "Ridesharing" means 2 or more employees sharing a trip in a motor vehicle.

70 (g) This section shall remain in effect until the Federal Internal Revenue Code is amended  
71 to provide a business expense deduction to employers and an exclusion from taxable  
72 income for employees for reimbursement of qualified transportation commuting expenses  
73 by an employer, or a credit substantially comparable to the credit under this section to  
74 employers and employees, and as of that date this division shall be reviewed and phased  
75 out, or repealed, as is deemed necessary by the legislature. However, any unused credit  
76 may continue to be carried forward, as provided in subdivision (e), until the credit has been  
77 exhausted.

(Proposed new language underlined; language to be deleted stricken.)

**PROPONENT:** San Diego County Bar Association

**STATEMENT OF REASONS:**

Existing Law: Provides no incentive for the use of public transportation and/or ridesharing.

This Resolution: Adds a tax credit to promote the use of public transportation and/or ridesharing.

The Problem: The reduction of carbon emissions is a worldwide issue. Employers need a direct and tangible incentive to encourage workers to use public transportation and/or ridesharing.

**IMPACT STATEMENT:**

This resolution does not affect any other law, statute or rule.

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**RESPONSIBLE FLOOR DELEGATE:** Bob Blanchard

## RESOLUTION 05-02-2008

### DIGEST:

#### Corporations: Definition of "Conforms to Law"

Amends Corporations Code sections 109, 202, 401, 1103, 1110, and 1113, and adds sections 912 and 1161, to eliminate substantial review of corporate filings by the Secretary of State.

### RESOLUTIONS COMMITTEE RECOMMENDATION:

DISAPPROVE

#### History:

Similar to 08-01-2007, which was disapproved.

#### Reasons:

This resolution amends Corporations Code sections 109, 202, 401, 1103, 1110, and 1113, and adds sections 912 and 1161, to eliminate substantial review of corporate filings by the Secretary of State. This resolution should be disapproved because current law assures that procedural and substantive conformance in corporate filings is achieved.

Currently, employees in the office of the Secretary of State are responsible for providing an initial review of all corporate filings for California. Review for conformance of statutes setting forth what is to be included in each filing does not generally require legal analysis. However, when there are questions, employees within the Secretary of State's office can rely on the guidance and expertise provided by Staff Counsel to address substantive questions that exceed the purview of procedural conformance.

Proponents argue that review should be limited to procedural conformance only. This could effectively eliminate a more detailed review of filings, which may be necessary to identify shell or unlawful corporations. Thus, this resolution would have unintended consequences. By enabling Staff Counsel to work with employees to assure procedural and substantive compliance with the law, the interests of the public, fairness and equity are best protected.

### TEXT OF RESOLUTION

RESOLVED, that the Conference of Delegates of California Bar Associations recommends that legislation be sponsored to amend Corporations Code sections 109, 202, 401, 1103, 1110, and 1113, and to add sections 912 and 1161, to read as follows:

- 1    § 109
- 2       (a) Any agreement, certificate or other instrument relating to a domestic or
- 3   foreign corporation filed pursuant to this division may be corrected with respect to any
- 4   misstatement of fact contained therein, any defect in the execution thereof or any other
- 5   error or defect contained therein, by filing a certificate of correction entitled "Certificate
- 6   of Correction of \_\_\_\_ (insert here the title of the agreement, certificate or other
- 7   instrument to be corrected and name(s) of corporation or corporations)"; provided,
- 8   however, that no such certificate of correction shall alter the wording of any resolution or

9 written consent which was in fact adopted by the board or the shareholders or effect a  
10 corrected amendment of articles which amendment as so corrected would not in all  
11 respects have complied with the requirements of this division at the time of filing of the  
12 agreement, certificate, or other instrument being corrected.

13 (b) If the certificate of correction corrects original articles, the certificate of  
14 correction shall be either an officers' certificate or a certificate signed and verified by the  
15 incorporators, or a majority of them. If the certificate of correction corrects an agreement  
16 of merger or an officers' certificate accompanying an agreement of merger, the certificate  
17 of correction shall be an officers' certificate of the surviving corporation only. In all other  
18 instances, the certificate of correction shall be either an officer's certificate or a certificate  
19 signed and verified as provided in this division with respect to the agreement, certificate  
20 or other instrument being corrected.

21 (c) A certificate of correction shall set forth the following:

22 (1) The name or names of the corporation or corporations.

23 (2) The date the agreement, certificate or other instrument being corrected was  
24 filed.

25 (3) The provision in the agreement, certificate or other instrument as corrected  
26 and, if the execution was defective, wherein it was defective.

27 (4) If applicable, that the certificate does not alter the wording of any resolution or  
28 written consent which was in fact adopted by the board or the shareholders.

29 (d) A provision of the articles, amended articles, restated articles, or certificate of  
30 determination being corrected by a certificate of correction shall be identified in the  
31 certificate of correction in accordance with subdivision (a) of Section 907.

32 (e) The filing of the certificate of correction shall not alter the effective time of  
33 the agreement, certificate or instrument being corrected, which shall remain as its original  
34 effective time, and such filing shall not affect any right or liability accrued or incurred  
35 before such filing, except that any right or liability accrued or incurred by reason of the  
36 error or defect being corrected shall be extinguished by such filing if the person having  
37 that right has not detrimentally relied on the original instrument.

38 (f) A certificate of correction that conforms to the requirements of this Section  
39 conforms to law for the purposes of Section 110.

40

41 § 110

42 (a) Upon receipt of any instrument by the Secretary of State for filing pursuant to  
43 this division, if it conforms to law, it shall be filed by, and in the office of, the Secretary  
44 of State and the date of filing endorsed thereon. Except for instruments filed pursuant to  
45 Section 1502, the date of filing shall be the date the instrument is received by the  
46 Secretary of State unless withheld from filing for a period of time pursuant to a request  
47 by the party submitting it for filing or unless in the judgment of the Secretary of State the  
48 filing is intended to be coordinated with the filing of some other corporate document  
49 which cannot be filed. The Secretary of State shall file a document as of any requested  
50 future date not more than 90 days after its receipt, including a Saturday, Sunday, or legal  
51 holiday, if the document is received in the Secretary of State's office at least one business  
52 day prior to the requested date of filing. An instrument does not fail to conform to law  
53 because it is not accompanied by the full filing fee if the unpaid portion of the fee does

54 not exceed the limits established by the policy of the Secretary of State for extending  
55 credit in these cases.

56 (b) If the Secretary of State determines that an instrument submitted for filing or  
57 otherwise submitted does not conform to law and returns it to the person submitting it,  
58 the instrument may be resubmitted accompanied by a written opinion of the member of  
59 the State Bar of California submitting the instrument, or representing the person  
60 submitting it, to the effect that the specific provision of the instrument objected to by the  
61 Secretary of State does conform to law and stating the points and authorities upon which  
62 the opinion is based. The Secretary of State shall rely, with respect to any disputed point  
63 of law (other than the application of Sections 201, 2101, and 2106), upon that written  
64 opinion in determining whether the instrument conforms to law. The date of filing in that  
65 case shall be the date the instrument is received on resubmission.

66 (c) Any instrument filed with respect to a corporation (other than original articles)  
67 may provide that it is to become effective not more than 90 days subsequent to its filing  
68 date. In case such a delayed effective date is specified, the instrument may be prevented  
69 from becoming effective by a certificate stating that by appropriate corporate action it has  
70 been revoked and is null and void, executed in the same manner as the original  
71 instrument and filed before the specified effective date. In the case of a merger  
72 agreement, the certificate revoking the earlier filing need only be executed on behalf of  
73 one of the constituent corporations. If no revocation certificate is filed, the instrument  
74 becomes effective on the date specified.

75

76 § 202

77 The articles of incorporation shall set forth:

78 (a) The name of the corporation; provided, however, that in order for the  
79 corporation to be subject to the provisions of this division applicable to a close  
80 corporation (Section 158), the name of the corporation must contain the word  
81 "corporation", "incorporated" or "limited" or an abbreviation of one of such words.

82 (b) (1) The applicable one of the following statements:

83 (i) The purpose of the corporation is to engage in any lawful act or activity for  
84 which a corporation may be organized under the General Corporation Law of California  
85 other than the banking business, the trust company business or the practice of a  
86 profession permitted to be incorporated by the California Corporations Code; or

87 (ii) The purpose of the corporation is to engage in the profession of \_\_\_\_ (with the  
88 insertion of a profession permitted to be incorporated by the California Corporations  
89 Code) and any other lawful activities (other than the banking or trust company business)  
90 not prohibited to a corporation engaging in such profession by applicable laws and  
91 regulations.

92 (2) In case the corporation is a corporation subject to the Banking Law, the  
93 articles shall set forth a statement of purpose which is prescribed in the applicable  
94 provision of the Banking Law.

95 (3) In case the corporation is a corporation subject to the Insurance Code as an  
96 insurer, the articles shall additionally state that the business of the corporation is to be an  
97 insurer.

98 (4) If the corporation is intended to be a "professional corporation" within the  
99 meaning of the Moscone-Knox Professional Corporation Act (Part 4 (commencing with

100 Section 13400) of Division 3), the articles shall additionally contain the statement  
101 required by Section 13404.

102 The articles shall not set forth any further or additional statement with respect to the  
103 purposes or powers of the corporation, except by way of limitation or except as expressly  
104 required by any law of this state other than this division or any federal or other statute or  
105 regulation (including the Internal Revenue Code and regulations thereunder as a  
106 condition of acquiring or maintaining a particular status for tax purposes).

107 (c) The name and address in this state of the corporation's initial agent for service  
108 of process in accordance with subdivision (b) of Section 1502.

109 (d) If the corporation is authorized to issue only one class of shares, the total  
110 number of shares which the corporation is authorized to issue.

111 (e) If the corporation is authorized to issue more than one class of shares, or if any  
112 class of shares is to have two or more series:

113 (1) The total number of shares of each class the corporation is authorized to issue,  
114 and the total number of shares of each series which the corporation is authorized to issue  
115 or that the board is authorized to fix the number of shares of any such series;

116 (2) The designation of each class, and the designation of each series or that the  
117 board may determine the designation of any such series; and

118 (3) The rights, preferences, privileges and restrictions granted to or imposed upon  
119 the respective classes or series of shares or the holders thereof, or that the board, within  
120 any limits and restrictions stated, may determine or alter the rights, preferences,  
121 privileges and restrictions granted to or imposed upon any wholly unissued class of  
122 shares or any wholly unissued series of any class of shares. As to any series the number  
123 of shares of which is authorized to be fixed by the board, the articles may also authorize  
124 the board, within the limits and restrictions stated therein or stated in any resolution or  
125 resolutions of the board originally fixing the number of shares constituting any series, to  
126 increase or decrease (but not below the number of shares of such series then outstanding)  
127 the number of shares of any such series subsequent to the issue of shares of that series. In  
128 case the number of shares of any series shall be so decreased, the shares constituting such  
129 decrease shall resume the status which they had prior to the adoption of the resolution  
130 originally fixing the number of shares of such series.

131 (f) Articles that conform to the requirements of subdivisions (a) through (d) and  
132 paragraphs (1) and (2) of subdivision (e) of this Section conform to law for the purposes  
133 of Section 110.

134  
135 § 401

136 (a) Before any corporation issues any shares of any class or series of which the  
137 rights, preferences, privileges, and restrictions, or any of them, or the number of shares  
138 constituting any series or the designation of the series, are not set forth in its articles but  
139 are fixed in a resolution adopted by the board pursuant to authority given by its articles,  
140 an officers' certificate shall be executed and filed, setting forth: (1) a copy of the  
141 resolution; (2) the number of shares of the class or series; and (3) that none of the shares  
142 of the class or series has been issued.

143 (b) After any certificate of determination has been filed, but before the  
144 corporation issues any shares of the class or series covered thereby, the board may alter  
145 or revoke any right, preference, privilege, or restriction fixed or determined by the

146 resolution set forth therein by the adoption of another resolution appropriate for that  
147 purpose and the execution and filing of an officers' certificate setting forth a copy of the  
148 resolution, and stating that none of the shares of the class or the series affected has been  
149 issued.

150 (c) After any certificate of determination has been filed, the board may, if  
151 authorized in the articles pursuant to subdivision (e) of Section 202, increase or decrease  
152 the number of shares constituting any series, by the adoption of another resolution  
153 appropriate for that purpose and the execution and filing of an officers' certificate setting  
154 forth a copy of the resolution, the number of shares of the series then outstanding and the  
155 increase or decrease in the number of shares constituting the series. If any certificate of  
156 determination has been incorporated in restated articles filed pursuant to Section 910, the  
157 action authorized by this subdivision may, notwithstanding Section 902, be accomplished  
158 by an amendment of the articles approved by the board alone.

159 (d) After shares of a class or series have been issued, the provisions of the  
160 resolution set forth in a certificate of determination may be amended only by the adoption  
161 and approval of an amendment in accordance with Section 902, 903, or 904 and the filing  
162 of a certificate of amendment in accordance with Sections 905 and 908. Notwithstanding  
163 the preceding sentence, a certificate to increase or decrease the number of shares of a  
164 series also may be filed as permitted by subdivision (c).

165 (e) A provision in a certificate of determination being amended pursuant to  
166 subdivision (b), (c), or (d) shall be identified in the amendment in accordance with  
167 subdivision (a) of Section 907.

168 (f) If a certificate is filed pursuant to subdivision (c) to decrease the number of  
169 shares of a series to zero, the certificate of determination whereby the series was  
170 established is thereupon no longer in force and the series is no longer an authorized series  
171 of the corporation.

172 (g) If the rights, preferences, privileges, and restrictions of the class or series  
173 contain a supermajority vote provision, as defined in subdivision (b) of Section 710,  
174 subject to Section 710, the officers' certificate shall also state that the provision has been  
175 approved by the shareholders in accordance with subdivision (c) of Section 710.

176 (h) A certificate that conforms to the requirements of this Section conforms to law  
177 for the purposes of Section 110.

178  
179 § 912

180 A certificate that conforms to the requirements of this Chapter conforms to law  
181 for the purposes of Section 110.

182  
183 § 1103

184 After approval of a merger by the board and any approval of the outstanding  
185 shares (Section 152) required by Chapter 12 (commencing with Section 1200), the  
186 surviving corporation shall file a copy of the agreement of merger with an officers'  
187 certificate of each constituent corporation attached stating the total number of outstanding  
188 shares of each class entitled to vote on the merger, that the principal terms of the  
189 agreement in the form attached were approved by that corporation by a vote of a number  
190 of shares of each class which equaled or exceeded the vote required, specifying each  
191 class entitled to vote and the percentage vote required of each class, or that the merger

192 agreement was entitled to be and was approved by the board alone under the provisions  
193 of Section 1201. If equity securities of a parent of a constituent corporation are to be  
194 issued in the merger, the officers' certificate of that constituent corporation shall state  
195 either that no vote of the shareholders of the parent was required or that the required vote  
196 was obtained. A certificate that conforms to the requirements of this Section conforms to  
197 law for the purposes of Section 110. The merger and any amendment of the articles of  
198 the surviving corporation contained in the merger agreement shall thereupon be effective  
199 (subject to subdivision (c) of Section 110 and subject to the provisions of Section 1108)  
200 and the several parties thereto shall be one corporation. The Secretary of State may  
201 certify a copy of the merger agreement separate from the officers' certificates attached  
202 thereto.

203

204 § 1110

205 (a) If a domestic corporation owns all the outstanding shares, or owns less than all  
206 the outstanding shares but at least 90 percent of the outstanding shares of each class, of a  
207 corporation or corporations, domestic or foreign, the merger of the subsidiary corporation  
208 or corporations into the parent corporation or the merger into the subsidiary corporation  
209 of the parent corporation and any other subsidiary corporation or corporations, may be  
210 effected by a resolution or plan of merger adopted and approved by the board of the  
211 parent corporation and the filing of a certificate of ownership as provided in subdivision  
212 (e). The resolution or plan of merger shall provide for the merger and shall provide that  
213 the surviving corporation assumes all the liabilities of each disappearing corporation and  
214 shall include any other provisions required by this section.

215 (b) If the parent corporation owns less than all the outstanding shares but at least  
216 90 percent of the outstanding shares of each class of the subsidiary corporation that is a  
217 party to the merger, the resolution or plan of merger also shall set forth the securities,  
218 cash, property, or rights to be issued, paid, delivered, or granted upon surrender of each  
219 outstanding share of the subsidiary corporation not owned by the parent corporation and  
220 the entire resolution or plan of merger as well as the consideration to be received for each  
221 share of the subsidiary corporation not owned by the parent corporation, shall be  
222 approved by the board of that subsidiary corporation.

223 (c) If the parent corporation is to be merged into one of its subsidiary  
224 corporations, the resolution or plan of merger also shall provide for the pro rata  
225 conversion of the outstanding shares of the parent corporation into shares of the surviving  
226 subsidiary corporation. In this case, the entire resolution or plan of merger shall be  
227 approved by the board of the surviving subsidiary corporation and, if the merger, but for  
228 the operation of this section, would be a merger reorganization (Section 181) the  
229 principal terms of which would be required to be approved by the outstanding shares  
230 (Section 152) of any class of the parent corporation pursuant to subdivision (d) of Section  
231 1201, the principal terms of the resolution or plan of merger shall be approved by the  
232 outstanding shares (Section 152) of that same class of the parent corporation.

233 (d) In any merger pursuant to this section, the resolution or plan of merger may  
234 provide for the amendment of the articles of the surviving corporation to change its name,  
235 subject to Section 201, regardless of whether the name so adopted is the same as or  
236 similar to that of one of the disappearing corporations. The provision shall establish the  
237 wording of the amendment pursuant to paragraph (2) of subdivision (a) of Section 907

238 and the resolution or plan of merger shall not provide for the amendment of the articles of  
239 the surviving corporation other than to change its name.

240 (e) After the required approval or approvals of the resolution or plan of merger, a  
241 certificate of ownership consisting of an officers' certificate of the parent corporation  
242 shall be filed, and a copy thereof for each domestic subsidiary corporation and qualified  
243 foreign disappearing subsidiary corporation which is a party to the merger shall also be  
244 filed. The certificate of ownership shall:

245 (1) Identify the parent and subsidiary corporation or corporations.

246 (2) Set forth the share ownership by the parent corporation of each subsidiary  
247 corporation as 100 percent of the outstanding shares or as at least 90 percent of the  
248 outstanding shares of each class, as the case may be.

249 (3) Set forth the resolution or plan of merger.

250 (4) Set forth approval of the resolution or plan of merger by the board of the  
251 parent corporation.

252 (5) Set forth other approvals of the resolution or plan of merger as required under  
253 subdivision (b) or (c), if applicable. A certificate that conforms to the requirements of  
254 this subdivision conforms to law for the purposes of Section 110.

255 (f) Upon the filing of the certificate of ownership, the merger shall be effective  
256 and any amendment of the articles of the surviving corporation set forth in the certificate  
257 shall be effective.

258 (g) A merger pursuant to this section may be effected if the parent corporation is a  
259 foreign corporation and if at least one subsidiary corporation is a domestic corporation  
260 but in such a case the certificate of ownership prepared as in subdivision (e) or the  
261 document required by subdivision (d) of Section 1108 shall be filed as to each domestic  
262 and qualified foreign subsidiary corporation, but no filing shall be made as to the foreign  
263 parent corporation. No merger into or with a foreign corporation may be effected as  
264 provided by this section unless the laws of the state or place of its incorporation permit  
265 that action.

266 (h) In the event all of the outstanding shares of a subsidiary domestic corporation  
267 party to a merger effected under this section are not owned by the parent corporation  
268 immediately prior to the merger, the parent corporation shall, at least 20 days before the  
269 effective date of the merger, give notice to each shareholder of such subsidiary  
270 corporation that the merger will become effective on or after a specified date. The notice  
271 shall contain a copy of the resolution or plan of merger and the information required by  
272 subdivision (a) of Section 1301. The notice shall be sent by mail addressed to the  
273 shareholder at the address of the shareholder as it appears on the records of the  
274 corporation. The shareholder shall have the right to demand payment of cash for the  
275 shares of the shareholder pursuant to Chapter 13 (commencing with Section 1300).

276 (i) If an agreement of merger is entered into between a parent corporation and one  
277 or more of its subsidiary corporations and the share ownership requirements of  
278 subdivision (a) are met, the agreement of merger may be filed as a plan of merger with a  
279 certificate of ownership in accordance with the requirements of this section, in which  
280 case Sections 1101, 1102, 1103, 1200, 1201, and 1202 shall not apply; or the agreement  
281 of merger may be filed pursuant to Section 1103, in which case this section shall not  
282 apply.

283

284 § 1113.

285 (a) Any one or more corporations may merge with one or more other business  
286 entities (Section 174.5). One or more domestic corporations (Section 167) not organized  
287 under this division and one or more foreign corporations (Section 171) may be parties to  
288 the merger. Notwithstanding the provisions of this section, the merger of any number of  
289 corporations with any number of other business entities may be effected only if:

290 (1) In a merger in which a domestic corporation not organized under this division  
291 or a domestic other business entity is a party, it is authorized by the laws under which it is  
292 organized to effect the merger.

293 (2) In a merger in which a foreign corporation is a party, it is authorized by the  
294 laws under which it is organized to effect the merger.

295 (3) In a merger in which a foreign other business entity is a party, it is authorized  
296 by the laws under which it is organized to effect the merger.

297 (b) Each corporation and each other party which desires to merge shall approve,  
298 and shall be a party to, an agreement of merger. Other persons, including a parent party  
299 (Section 1200), may be parties to the agreement of merger. The board of each  
300 corporation which desires to merge, and, if required the shareholders, shall approve the  
301 agreement of merger. The agreement of merger shall be approved on behalf of each party  
302 by those persons required to approve the merger by the laws under which it is organized.  
303 The agreement of merger shall state:

304 (1) The terms and conditions of the merger.

305 (2) The name and place of incorporation or organization of each party to the  
306 merger and the identity of the surviving party.

307 (3) The amendments, if any, subject to Sections 900 and 907, to the articles of the  
308 surviving corporation, if applicable, to be effected by the merger. If any amendment  
309 changes the name of the surviving corporation, if applicable, the new name may be,  
310 subject to subdivision (b) of Section 201, the same as or similar to the name of a  
311 disappearing party to the merger.

312 (4) The manner of converting the shares of each constituent corporation into  
313 shares, interests, or other securities of the surviving party. If any shares of any constituent  
314 corporation are not to be converted solely into shares, interests or other securities of the  
315 surviving party, the agreement of merger shall state (i) the cash, rights, securities, or other  
316 property which the holders of those shares are to receive in exchange for the shares,  
317 which cash, rights, securities, or other property may be in addition to or in lieu of shares,  
318 interests or other securities of the surviving party, or (ii) that the shares are canceled  
319 without consideration.

320 (5) Any other details or provisions required by the laws under which any party to  
321 the merger is organized, including, if a public benefit corporation or a religious  
322 corporation is a party to the merger, Section 6019.1, or, if a mutual benefit corporation is  
323 a party to the merger, Section 8019.1, or, if a consumer cooperative corporation is a party  
324 to the merger, Section 12540.1, or, if a domestic limited partnership is a party to the  
325 merger, Section 15678.2 or 15911.12, or, if a domestic partnership is a party to the  
326 merger, Section 16911, or, if a domestic limited liability company is a party to the  
327 merger, Section 17551.

328 (6) Any other details or provisions as are desired, including, without limitation, a  
329 provision for the payment of cash in lieu of fractional shares or for any other arrangement  
330 with respect thereto consistent with the provisions of Section 407.

331 (c) Each share of the same class or series of any constituent corporation (other  
332 than the cancellation of shares held by a party to the merger or its parent, or a wholly  
333 owned subsidiary of either, in another constituent corporation) shall, unless all  
334 shareholders of the class or series consent and except as provided in Section 407, be  
335 treated equally with respect to any distribution of cash, rights, securities, or other  
336 property. Notwithstanding paragraph (4) of subdivision (b), the unredeemable common  
337 shares of a constituent corporation may be converted only into unredeemable common  
338 shares of a surviving corporation or a parent party (Section 1200) or unredeemable equity  
339 securities of a surviving party other than a corporation if another party to the merger or its  
340 parent owns, directly or indirectly, prior to the merger shares of that corporation  
341 representing more than 50 percent of the voting power of that corporation, unless all of  
342 the shareholders of the class consent and except as provided in Section 407.

343 (d) Notwithstanding its prior approval, an agreement of merger may be amended  
344 prior to the filing of the agreement of merger or the certificate of merger, as is applicable,  
345 if the amendment is approved by the board of each constituent corporation and, if the  
346 amendment changes any of the principal terms of the agreement, by the outstanding  
347 shares (Section 152), if required by Chapter 12 (commencing with Section 1200), in the  
348 same manner as the original agreement of merger. If the agreement of merger as so  
349 amended and approved is also approved by each of the other parties to the agreement of  
350 merger, the agreement of merger as so amended shall then constitute the agreement of  
351 merger.

352 (e) The board of a constituent corporation may, in its discretion, abandon a  
353 merger, subject to the contractual rights, if any, of third parties, including other parties to  
354 the agreement of merger, without further approval by the outstanding shares (Section  
355 152), at any time before the merger is effective.

356 (f) Each constituent corporation shall sign the agreement of merger by its  
357 chairperson of the board, president or a vice president and also by its secretary or an  
358 assistant secretary acting on behalf of their respective corporations.

359 (g) (1) If the surviving party is a corporation or a foreign corporation, or if a  
360 public benefit corporation (Section 5060), a mutual benefit corporation (Section 5059), a  
361 religious corporation (Section 5061), or a corporation organized under the Consumer  
362 Cooperative Corporation Law (Section 12200) is a party to the merger, after required  
363 approvals of the merger by each constituent corporation through approval of the board  
364 (Section 151) and any approval of the outstanding shares (Section 152) required by  
365 Chapter 12 (commencing with Section 1200) and by the other parties to the merger, the  
366 surviving party shall file a copy of the agreement of merger with an officers' certificate of  
367 each constituent domestic and foreign corporation attached stating the total number of  
368 outstanding shares or membership interests of each class entitled to vote on the merger  
369 (and identifying any other person or persons whose approval is required), that the  
370 agreement of merger in the form attached or its principal terms, as required, were  
371 approved by that corporation by a vote of a number of shares or membership interests of  
372 each class that equaled or exceeded the vote required, specifying each class entitled to  
373 vote and the percentage vote required of each class and, if applicable, by that other

374 person or persons whose approval is required, or that the merger agreement was entitled  
375 to be and was approved by the board alone (as provided in Section 1201, in the case of  
376 corporations subject to that section). If equity securities of a parent party (Section 1200)  
377 are to be issued in the merger, the officers' certificate of that controlled party shall state  
378 either that no vote of the shareholders of the parent party was required or that the required  
379 vote was obtained. In lieu of an officers' certificate, a certificate of merger, on a form  
380 prescribed by the Secretary of State, shall be filed for each constituent other business  
381 entity. The certificate of merger shall be executed and acknowledged by each domestic  
382 constituent limited liability company by all managers of the limited liability company  
383 (unless a lesser number is specified in its articles of organization or operating agreement)  
384 and by each domestic constituent limited partnership by all general partners (unless a  
385 lesser number is provided in its certificate of limited partnership or partnership  
386 agreement) and by each domestic constituent general partnership by two partners (unless  
387 a lesser number is provided in its partnership agreement) and by each foreign constituent  
388 limited liability company by one or more managers and by each foreign constituent  
389 general partnership or foreign constituent limited partnership by one or more general  
390 partners, and by each constituent reciprocal insurer by the chairperson of the board,  
391 president, or vice president, and by the secretary or assistant secretary, or, if a constituent  
392 reciprocal insurer has not appointed those officers, by the chairperson of the board,  
393 president, or vice president, and by the secretary or assistant secretary of the constituent  
394 reciprocal insurer's attorney-in-fact, and by each other party to the merger by those  
395 persons required or authorized to execute the certificate of merger by the laws under  
396 which that party is organized, specifying for that party the provision of law or other basis  
397 for the authority of the signing persons. The certificate of merger shall set forth, if a vote  
398 of the shareholders, members, partners, or other holders of interests of the constituent  
399 other business entity was required, a statement setting forth the total number of  
400 outstanding interests of each class entitled to vote on the merger and that the agreement  
401 of merger in the form attached or its principal terms, as required, were approved by a vote  
402 of the number of interests of each class that equaled or exceeded the vote required,  
403 specifying each class entitled to vote and the percentage vote required of each class, and  
404 any other information required to be set forth under the laws under which the constituent  
405 other business entity is organized, including, if a domestic limited partnership is a party  
406 to the merger, subdivision (a) of Section 15678.4 or subdivision (a) of Section 15911.14,  
407 if a domestic partnership is a party to the merger, subdivision (b) of Section 16915, and,  
408 if a domestic limited liability company is a party to the merger, subdivision (a) of Section  
409 17552. The certificate of merger for each constituent foreign other business entity, if  
410 any, shall also set forth the statutory or other basis under which that foreign other  
411 business entity is authorized by the laws under which it is organized to effect the merger.  
412 The merger and any amendment of the articles of the surviving corporation, if applicable,  
413 contained in the agreement of merger shall be effective upon filing of the agreement of  
414 merger with an officer's certificate of each constituent domestic and foreign corporation  
415 and a certificate of merger for each constituent other business entity, subject to  
416 subdivision (c) of Section 110 and subject to the provisions of subdivision (j), and the  
417 several parties thereto shall be one entity. If a domestic reciprocal insurer organized after  
418 1974 to provide medical malpractice insurance is a party to the merger, the agreement of  
419 merger or certificate of merger shall not be filed until there has been filed the certificate

420 issued by the Insurance Commissioner approving the merger pursuant to Section 1555 of  
421 the Insurance Code. The Secretary of State may certify a copy of the agreement of merger  
422 separate from the officers' certificates and certificates of merger attached thereto.

423 (2) If the surviving entity is an other business entity, and no public benefit  
424 corporation (Section 5060), mutual benefit corporation (Section 5059), religious  
425 corporation (Section 5061), or corporation organized under the Consumer Cooperative  
426 Corporation Law (Section 12200) is a party to the merger, after required approvals of the  
427 merger by each constituent corporation through approval of the board (Section 151) and  
428 any approval of the outstanding shares (Section 152) required by Chapter 12  
429 (commencing with Section 1200) and by the other parties to the merger, the parties to the  
430 merger shall file a certificate of merger in the office of, and on a form prescribed by, the  
431 Secretary of State. The certificate of merger shall be executed and acknowledged by each  
432 constituent domestic and foreign corporation by its chairperson of the board, president or  
433 a vice president and also by its secretary or an assistant secretary and by each domestic  
434 constituent limited liability company by all managers of the limited liability company  
435 (unless a lesser number is specified in its articles of organization or operating agreement)  
436 and by each domestic constituent limited partnership by all general partners (unless a  
437 lesser number is provided in its certificate of limited partnership or partnership  
438 agreement) and by each domestic constituent general partnership by two partners (unless  
439 a lesser number is provided in its partnership agreement) and by each foreign constituent  
440 limited liability company by one or more managers and by each foreign constituent  
441 general partnership or foreign constituent limited partnership by one or more general  
442 partners, and by each constituent reciprocal insurer by the chairperson of the board,  
443 president, or vice president, and by the secretary or assistant secretary, or, if a constituent  
444 reciprocal insurer has not appointed those officers, by the chairperson of the board,  
445 president, or vice president, and by the secretary or assistant secretary of the constituent  
446 reciprocal insurer's attorney-in-fact. The certificate of merger shall be signed by each  
447 other party to the merger by those persons required or authorized to execute the  
448 certificate of merger by the laws under which that party is organized, specifying for that  
449 party the provision of law or other basis for the authority of the signing persons. The  
450 certificate of merger shall set forth all of the following:

451 (A) The name, place of incorporation or organization, and the Secretary of State's  
452 file number, if any, of each party to the merger, separately identifying the disappearing  
453 parties and the surviving party.

454 (B) If the approval of the outstanding shares of a constituent corporation was  
455 required by Chapter 12 (commencing with Section 1200), a statement setting forth the  
456 total number of outstanding shares of each class entitled to vote on the merger and that  
457 the principal terms of the agreement of merger were approved by a vote of the number of  
458 shares of each class entitled to vote and the percentage vote required of each class.

459 (C) The future effective date or time, not more than 90 days subsequent to the  
460 date of filing of the merger, if the merger is not to be effective upon the filing of the  
461 certificate of merger with the office of the Secretary of State.

462 (D) A statement, by each party to the merger which is a domestic corporation not  
463 organized under this division, a foreign corporation, or an other business entity, of the  
464 statutory or other basis under which that party is authorized by the laws under which it is  
465 organized to effect the merger.

466 (E) Any other information required to be stated in the certificate of merger by the  
467 laws under which each party to the merger is organized, including, if a domestic limited  
468 liability company is a party to the merger, subdivision (a) of Section 17552, if a domestic  
469 partnership is a party to the merger, subdivision (b) of Section 16915, and, if a domestic  
470 limited partnership is a party to the merger, subdivision (a) of Section 15678.4 or  
471 subdivision (a) of Section 15911.14.

472 (F) Any other details or provisions that may be desired.

473 Unless a future effective date or time is provided in a certificate of merger, in  
474 which event the merger shall be effective at that future effective date or time, a merger  
475 shall be effective upon the filing of the certificate of merger in the office of the Secretary  
476 of State and the several parties thereto shall be one entity. The surviving other business  
477 entity shall keep a copy of the agreement of merger at its principal place of business  
478 which, for purposes of this subdivision, shall be the office referred to in Section 17057 if  
479 a domestic limited liability company, at the business address specified in paragraph (5) of  
480 subdivision (a) of Section 17552 if a foreign limited liability company, at the office  
481 referred to in subdivision (a) of Section 16403 if a domestic general partnership, at the  
482 business address specified in subdivision (f) of Section 16911 if a foreign partnership, at  
483 the office referred to in subdivision (a) of Section 15614 or in subdivision (a) of Section  
484 15901.14 if a domestic limited partnership, or at the business address specified in  
485 paragraph (5) of subdivision (a) of Section 15678.4 or paragraph (3) of subdivision (a) of  
486 Section 15909.02 if a foreign limited partnership. Upon the request of a holder of equity  
487 securities of a party to the merger, a person with authority to do so on behalf of the  
488 surviving other business entity shall promptly deliver to that holder, a copy of the  
489 agreement of merger. A waiver by that holder of the rights provided in the foregoing  
490 sentence shall be unenforceable. If a domestic reciprocal insurer organized after 1974 to  
491 provide medical malpractice insurance is a party to the merger the agreement of merger  
492 or certificate of merger shall not be filed until there has been filed the certificate issued  
493 by the Insurance Commissioner approving the merger in accordance with Section 1555 of  
494 the Insurance Code.

495 (h) (1) A copy of an agreement of merger certified on or after the effective date by  
496 an official having custody thereof has the same force in evidence as the original and,  
497 except as against the state, is conclusive evidence of the performance of all conditions  
498 precedent to the merger, the existence on the effective date of the surviving party to the  
499 merger and the performance of the conditions necessary to the adoption of any  
500 amendment to the articles, if applicable, contained in the agreement of merger.

501 (2) For all purposes for a merger in which the surviving entity is a domestic other  
502 business entity and the filing of a certificate of merger is required by paragraph (2) of  
503 subdivision (g), a copy of the certificate of merger duly certified by the Secretary of State  
504 is conclusive evidence of the merger of the constituent corporations, either by themselves  
505 or together with the other parties to the merger, into the surviving other business entity.

506 (i) (1) Upon a merger pursuant to this section, the separate existences of the  
507 disappearing parties to the merger cease and the surviving party to the merger shall  
508 succeed, without other transfer, to all the rights and property of each of the disappearing  
509 parties to the merger and shall be subject to all the debts and liabilities of each in the  
510 same manner as if the surviving party to the merger had itself incurred them.

511 (2) All rights of creditors and all liens upon the property of each of the constituent  
512 corporations and other parties to the merger shall be preserved unimpaired, provided that  
513 those liens upon property of a disappearing party shall be limited to the property affected  
514 thereby immediately prior to the time the merger is effective.

515 (3) Any action or proceeding pending by or against any disappearing corporation  
516 or disappearing party to the merger may be prosecuted to judgment, which shall bind the  
517 surviving party, or the surviving party may be proceeded against or substituted in its  
518 place.

519 (4) If a limited partnership or a general partnership is a party to the merger,  
520 nothing in this section is intended to affect the liability a general partner of a disappearing  
521 limited partnership or general partnership may have in connection with the debts and  
522 liabilities of the disappearing limited partnership or general partnership existing prior to  
523 the time the merger is effective.

524 (j) (1) The merger of domestic corporations with foreign corporations or foreign  
525 other business entities in a merger in which one or more other business entities is a party  
526 shall comply with subdivision (a) and this subdivision.

527 (2) If the surviving party is a domestic corporation or domestic other business  
528 entity, the merger proceedings with respect to that party and any domestic disappearing  
529 corporation shall conform to the provisions of this section. If the surviving party is a  
530 foreign corporation or foreign other business entity, then, subject to the requirements of  
531 subdivision (c), and of Section 407 and Chapter 12 (commencing with Section 1200) and  
532 Chapter 13 (commencing with Section 1300), and, if applicable, corresponding  
533 provisions of the Nonprofit Corporation Law or the Consumer Cooperative Corporation  
534 Law, with respect to any domestic constituent corporations, Chapter 13 (commencing  
535 with Section 17600) of Title 2.5 with respect to any domestic constituent limited liability  
536 companies, Article 6 (commencing with Section 16601) of Chapter 5 of Title 2 with  
537 respect to any domestic constituent general partnerships, and Article 7.6 (commencing  
538 with Section 15679.1) of Chapter 3, and Article 11.5 (commencing with Section  
539 15911.20) of Chapter 5.5 of Title 2 with respect to any domestic constituent limited  
540 partnerships, the merger proceedings may be in accordance with the laws of the state or  
541 place of incorporation or organization of the surviving party.

542 (3) If the surviving party is a domestic corporation or domestic other business  
543 entity, the certificate of merger or the agreement of merger with attachments shall be  
544 filed as provided in subdivision (g) and thereupon, subject to subdivision (c) of Section  
545 110 or paragraph (2) of subdivision (g), as is applicable, the merger shall be effective as  
546 to each domestic constituent corporation and domestic constituent other business entity.

547 (4) If the surviving party is a foreign corporation or foreign other business entity,  
548 the merger shall become effective in accordance with the law of the jurisdiction in which  
549 the surviving party is organized, but, except as provided in paragraph (5), the merger  
550 shall be effective as to any domestic disappearing corporation as of the time of  
551 effectiveness in the foreign jurisdiction upon the filing in this state of a copy of the  
552 agreement of merger with an officers' certificate of each constituent foreign and domestic  
553 corporation and a certificate of merger of each constituent other business entity attached,  
554 which officers' certificates and certificates of merger shall conform to the requirements of  
555 paragraph (1) of subdivision (g). If one or more domestic other business entities is a  
556 disappearing party in a merger pursuant to this subdivision in which a foreign other

557 business entity is the surviving entity, a certificate of merger required by the laws under  
558 which that domestic other business entity is organized, including subdivision (a) of  
559 Section 15678.4, subdivision (a) of Section 15911.14, subdivision (b) of Section 16915,  
560 or subdivision (a) of Section 17552, as is applicable, shall also be filed at the same time  
561 as the filing of the agreement of merger.

562 (5) If the date of the filing in this state pursuant to this subdivision is more than  
563 six months after the time of the effectiveness in the foreign jurisdiction, or if the powers  
564 of a domestic disappearing corporation are suspended at the time of effectiveness in the  
565 foreign jurisdiction, the merger shall be effective as to the domestic disappearing  
566 corporation as of the date of filing in this state.

567 (6) In a merger described in paragraph (3) or (4), each foreign disappearing  
568 corporation that is qualified for the transaction of intrastate business shall by virtue of the  
569 filing pursuant to this subdivision, subject to subdivision (c) of Section 110,  
570 automatically surrender its right to transact intrastate business in this state. The filing of  
571 the agreement of merger or certificate of merger, as is applicable, pursuant to this  
572 subdivision, by a disappearing foreign other business entity registered for the transaction  
573 of intrastate business in this state shall, by virtue of that filing, subject to subdivision (c)  
574 of Section 110, automatically cancels the registration for that foreign other business  
575 entity, without the necessity of the filing of a certificate of cancellation.

576 (k) A certificate that conforms to the requirements of this Section conforms to  
577 law for the purposes of Section 110.

578

579 § 1161

580 A certificate of conversion that conforms to the requirements of this Chapter  
581 conforms to law for the purposes of Section 110.

(Proposed new language underlined; language to be deleted stricken.)

**PROPONENT:** Santa Clara County Bar Association

**STATEMENT OF REASONS:**

Existing Law: Section 110(a) of the General Corporation Law (GCL) requires the Secretary of State (SoS) to file an instrument submitted for filing only if the instrument “conforms to law.” The GCL does not define the phrase “conforms to law.”

This Resolution: The proposed amendments provide that a given instrument “conforms to law” if the instrument satisfies the requirements for the form of the instrument.

The Problem: Reviewing the substance of corporate instruments (substantive review) is expensive for the State of California, expensive for California businesses, fails to promote public policy, undermines the California General Corporation Law, and does not protect California shareholders.

Expensive for California. In 2005, thirty-four SoS staff members (9 attorneys, 16 document examiners, and 8 additional filers) were trained to review corporate filings.

Expensive for California Businesses. A corporation with complex articles is likely to have to submit amendments to its articles of incorporation multiple times to address SoS staff objections. SoS staff objections are often trivial, regularly increase the filer’s legal expenses, and delay closing of funding transactions and mergers.

Does Not Promote Public Policy. No legislator, academician, or commentator claims (a) that incorrectly drafted corporate instruments represent a serious social problem; (b) that a corporate instrument can prevail in a conflict with the GCL; or (c) that the courts are not an adequate remedy when conflicts arise. The leading treatise on the GCL, Marsh’s California Corporation Law, includes extensive discussions of the public policies underlying different provisions of the GCL, but contains no discussion of substantive review.

Undermines the California GCL. Substantive review undermines the California GCL by encouraging California businesses to incorporate in other states (most notably Delaware). Many if not most California corporate attorneys for corporations with multiple classes of stock would rather incorporate their clients in Delaware than risk the expense and embarrassment of delay associated with substantive review.

Does Not Protect Shareholders. The SoS routinely files corporate instruments that strip preferred shareholders of their liquidation preferences and dilute the holdings of common shareholders to a pittance. The SoS makes no inquiry as to whether these actions are appropriate, or as to whether the corporation’s Board of Directors has satisfied its fiduciary obligations in approving the changes.

Not a Service. Substantive review is not a government service. The fact that the SoS has agreed to file a corporate document does not mean that the document does not violate the GCL. The SoS's findings are not binding on any court and have no value as precedent, even with respect to the SoS itself. The SoS staff routinely objects to language it previously approved for filing.

No Unintended Consequences. No jurisdiction other than California reviews corporate instruments for substantive conformity to law. There are no reports of problems arising in these other jurisdictions that substantive review solves at a reasonable cost. There are no movements in other jurisdictions to implement substantive review.

#### **IMPACT STATEMENT:**

This resolution does not affect any other law, statute or rule.

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**RESPONSIBLE FLOOR DELEGATE:** Nelson D. Crandall

#### **COUNTERARGUMENT**

##### **SACRAMENTO COUNTY BAR ASSOCIATION**

First, the resolution is unnecessary because the General Corporation Law, (and the Nonprofit Corporation Law, the Consumer Cooperative Corporation Law and the Limited Liability Company Law for that matter) has statutory procedures for filing documents when the submitter disagrees with the Secretary of State's determination that a document does not comply with law. Any document returned by the Secretary of State for non-compliance with law may be resubmitted to the Secretary of State accompanied by a written opinion of a member of The State Bar of California setting forth the reasons the document does comply with law and the Secretary of State is required to rely on the points and authorities in that opinion in its legal review.

This issue is not new. The express statutory duty of legal review by the Secretary of State was added to the law in 1929. In 1977, the business corporation law was significantly revised and the legislative drafting committee considered removing statutory substantive review for many of the same reasons noted by the Proponent. However, the drafting committee decided to retain the express duty of legal review and established the procedure described above. Contrary to the Proponent's contention, the leading treatise on the General Corporation Law, Marsh's California Corporations, contains several pages of discussion on this issue and the history of legal review by the Secretary of State.

Second, substantive legal review of business entity documents submitted to the Secretary of State actually saves money for business and the state. As the Proponent points out, the Courts are the remedy when conflicts arise. Consider the increased cost of litigation to corporations,

shareholders and even the courts in litigating disputes that could have been avoided by substantive review by the Secretary of State. Having a handful of Secretary of State attorneys and document reviewers review the documents and provide detailed comments on problems prior to filing is far more cost-effective. It is important to note that a *very* large percentage of the business entity documents received at the Secretary of State are drafted by laypersons and they benefit significantly from the legal review and comments included when a document is returned unfiled. To a lesser degree, attorneys benefit from the substantive review and comment as well. Many future problems are averted by substantive legal review.

Lastly, Proponent's argument that substantive review of business entity documents undermines the General Corporation Law by encouraging businesses to incorporate in other states does not make sense. The General Corporation is undermined, however, when we don't require or expect documents submitted to the Secretary of State to comply with that law. By effectively eliminating substantive review of documents submitted under California law, this resolution itself would undermine California laws governing business entities.

## **RESOLUTION 05-03-08**

### **DIGEST**

#### Professional Corporations: Employee Stock Option Plan Trustees as Share Owners

Amends Corporations Code sections 13406 and 13407 to allow professionally licensed trustees of Employee Stock Option Plans to own shares in professional corporations.

### **RESOLUTIONS COMMITTEE RECOMMENDATION**

APPROVE IN PRINCIPLE

#### History:

Similar to Resolution 02-07-02, which was approved.

#### Reasons:

This resolution amends Corporations Code sections 13406 and 13407 to allow professionally licensed trustees of Employee Stock Option Plans to own shares in professional corporations. This resolution should be approved in principle because it would permit professional corporations to utilize Employee Stock Ownership Plans to obtain the same tax benefits in connection with the purchase of shares of deceased or retiring shareholders, as afforded other corporations.

This resolution would add subdivision (d) to Corporations Code section 13406 and reference the same in section 13407, to allow for the issuance and transfer of shares in Professional Corporations to licensed professional persons serving as trustees of qualified Employee Stock Option Plan trusts, created to hold shares of the professional corporation. The beneficiaries of the trusts, in order to qualify for the federal tax benefits, would all be employees of the professional corporation, including non-licensed and non-professional employees. Under Internal Revenue Code section 409, subdivision (e)(3), the voting power of such beneficiaries are limited to corporate mergers, consolidations, sales of all or substantially all of the corporation's assets, recapitalizations, reclassifications, liquidations, and dissolutions. The day-to-day operations and activities of the professional corporations would still be conducted and governed only by licensed professionals.

This resolution would allow non-licensed and non-professional persons to be owners of shares in licensed professional corporations, but would limit their stockholder voting rights to matters that do not interfere with or lessen the protections afforded the public by the current professional licensing statutes, rules, and regulations.

### **TEXT OF RESOLUTION**

RESOLVED, that the Conference of Delegates of California Bar Associations recommends that legislation be sponsored to amend Corporations Code sections 13406 and 13407 to read as follows:

1    § 13406

2 (a) Subject to the provisions of subdivision (b) and (d), shares of capital stock in  
3 a professional corporation may be issued only to a licensed person or to a person who is  
4 licensed to render the same professional services in the jurisdiction or jurisdictions in  
5 which the person practices, and any shares issued in violation of this restriction shall be  
6 void. Unless there is a public offering of securities by a professional corporation or by a  
7 foreign professional corporation in this state, its financial statements shall be treated by the  
8 Commissioner of Corporations as confidential, except to the extent that such statements  
9 shall be subject to subpoena in connection with any judicial or administrative proceeding,  
10 and may be admissible in evidence therein. No shareholder of a professional corporation  
11 or of a foreign professional corporation qualified to render professional services in this  
12 state shall enter into a voting trust, proxy, or any other arrangement vesting another person  
13 (other than another person who is a shareholder of the same corporation) with the authority  
14 to exercise the voting power of any or all of his or her shares, and any such purported  
15 voting trust, proxy or other arrangement shall be void.

16 (b) A professional law corporation may be incorporated as a nonprofit public  
17 benefit corporation under the Nonprofit Public Benefit Corporation Law under either of the  
18 following circumstances:

19 (1) The corporation is a qualified legal services project or a qualified support  
20 center within the meaning of subdivisions (a) and (b) of Section 6213 of the Business and  
21 Professions Code.

22 (2) The professional law corporation otherwise meets all of the requirements and  
23 complies with all of the provisions of the Nonprofit Public Benefit Corporation Law, as  
24 well as all of the following requirements:

25 (A) All of the members of the corporation, if it is a membership organization as  
26 described in the Nonprofit Corporation Law, are persons licensed to practice law in  
27 California.

28 (B) All of the members of the professional law corporation's board of directors  
29 are persons licensed to practice law in California.

30 (C) Seventy percent of the clients to whom the corporation provides legal  
31 services are lower income persons as defined in Section 50079.5 of the Health and Safety  
32 Code, and to other persons who would not otherwise have access to legal services.

33 (D) The corporation shall not enter into contingency fee contracts with clients.

34 (c) A professional law corporation incorporated as a nonprofit public benefit  
35 corporation that is a recipient in good standing as defined in subdivision (c) of  
36 Section 6213 of the Business and Professions Code shall be deemed to have satisfied all of  
37 the filing requirements of a professional law corporation under Sections 6161.1, 6162, and  
38 6163 of the Business and Professions Code.

39 (d) Shares of capital stock in a professional corporation may be issued to a  
40 trustee, who is a licensed person or a person who is licensed to render the same  
41 professional services in the jurisdiction or jurisdictions in which the person practices, of a  
42 trust created to hold share of the professional corporation pursuant to an employee stock  
43 ownership plan meeting the requirements of Sections 401 and 409 of the Internal Revenue  
44 Code, as amended; provided all voting rights with respect to such shares, subject to the  
45 limitation set forth in Section 409(e)(3) of the Internal Revenue Code, as amended, shall be  
46 exercised in the sole discretion of a licensed person or a person who is licensed to render  
47 the same professional services in the jurisdiction or jurisdictions in which the person

48 practices and no person who is not a licensed person or a person who is licensed to render  
49 the same professional services in the jurisdiction or jurisdictions in which the person  
50 practices shall be entitled to any distribution of shares of capital stock of the professional  
51 corporation from any such trust.

52

53 § 13407

54 Shares in a professional corporation or a foreign professional corporation  
55 qualified to render professional services in this state may be transferred only to a licensed  
56 person, to a shareholder of the same corporation, to a person licensed to practice the same  
57 profession in the jurisdiction or jurisdictions in which the person practices, to a trustee  
58 permitted under subdivision (d) of section 13406 of the Corporations Code, or to a  
59 professional corporation, and any transfer in violation of this restriction shall be void,  
60 except as provided herein.

61 A professional corporation may purchase its own shares without regard to any  
62 restrictions provided by law upon the repurchase of shares, if at least one share remains  
63 issued and outstanding.

64 If a professional corporation or a foreign professional corporation qualified to  
65 render professional services in this state shall fail to acquire all of the shares of a  
66 shareholder who is disqualified from rendering professional services in this state or of a  
67 deceased shareholder who was, on his or her date of death, licensed to render professional  
68 services in this state, or if such a disqualified shareholder or the representative of such a  
69 deceased shareholder shall fail to transfer said shares to the corporation, to another  
70 shareholder of the corporation, to a person licensed to practice the same profession in the  
71 jurisdiction or jurisdictions in which the person practices, or to a licensed person, within 90  
72 days following the date of disqualification, or within six months following the date of  
73 death of the shareholder, as the case may be, then the certificate of registration of the  
74 corporation may be suspended or revoked by the governmental agency regulating the  
75 profession in which the corporation is engaged. In the event of such a suspension or  
76 revocation, the corporation shall cease to render professional services in this state.

77 Notwithstanding any provision in this part, upon the death or incapacity of a  
78 dentist, any individual named in subdivision (a) of Section 1625.3 of the Business and  
79 Professions Code may employ licensed dentists and dental assistants and charge for their  
80 professional services for a period not to exceed 12 months from the date of death or  
81 incapacity of the dentist. The employment of licensed dentists and dental assistants shall  
82 not be deemed the practice of dentistry within the meaning of Section 1625 of the Business  
83 and Professions Code, provided that all of the requirements of Section 1625.4 of the  
84 Business and Professions Code are met. If an individual listed in Section 1625.3 of the  
85 Business and Professions Code is employing licensed persons and dental assistants, then  
86 the shares of a deceased or incapacitated dentist shall be transferred as provided in this  
87 section no later than 12 months from the date of death or incapacity of the dentist.

(Proposed new language underlined; language to be deleted stricken.)

**PROPONENT:** San Diego County Bar Association

**STATEMENT OF REASONS:**

Existing Law: Restricts ownership of shares of a professional corporation to licensed persons in the profession for which the corporation was formed.

This Resolution: Authorizes share ownership by an employee stock ownership plan (ESOP) trust where the trustees are licensed persons and distributions to non-licensed person are required to be in cash.

The Problem: Current state law makes the considerable benefits of an ESOP authorized under Federal tax law unavailable to owners and employees of professional corporations. These benefits include providing tax deferred retirement income to all employees and facilitating ownership succession by providing a tax advantaged mechanism to purchase shares of the corporation from retiring owners. This resolution would extend to professionals the same benefits currently available to owners of other types of businesses. Professional corporations would continue to only be under the control of licensed persons and only licensed persons would be entitled to receive distributions in the form of stock. All distributions to non-licensed persons would be made solely in cash.

Under current law, funds used by a professional corporation to repurchase shares of a retiring shareholder are not deductible as a business expense. As a consequence, monies earned to repurchase shares from a retiring shareholder are first taxed at the corporate level and then subject to tax again upon receipt by the retiring shareholder. Amounts contributed to an ESOP to purchase shares from a retiring shareholder are tax deductible to the corporation. Under Federal Internal Revenue Code section 409(e)(3), a plan may limit the right of participants to direct the voting of plan shares to only corporate mergers, consolidations, sales of all or substantially all of the corporation's assets, recapitalizations, reclassifications, liquidations, and dissolutions. Thus, trustees who would be limited to licensed persons, would exercise sole and absolute control over the election of directors and all aspects of running the professional business.

## **IMPACT STATEMENT**

This resolution does not affect any other law, statute or rule.

**AUTHOR AND/OR PERMANENT CONTACT:** Robert W. Blanchard, Blanchard, Krasner & French, 800 Silverado Street, 2<sup>nd</sup> Floor, La Jolla, California 92037; voice: (858) 551-2440; fax: (858) 551-2434; email: bblanchard@bkflaw.com.

**RESPONSIBLE FLOOR DELEGATE:** Bob Blanchard

**RESOLUTION 05-04-2008**

**DIGEST:**

Business & Professions Code: Funeral Services Interest Charges

Amends Business & Professions Code section 7685 to require written disclosure of the terms of interest charges where funerals are paid for in installments.

**RESOLUTIONS COMMITTEE RECOMMENDATION:**

APPROVE IN PRINCIPLE

History:

No similar resolutions found.

Reasons:

This resolution amends Business & Professions Code section 7685 to require written disclosure of the terms of interest charges where funerals are paid for in installments. This resolution should be approved in principle because state consumer protection interests favor disclosure of credit and financing terms.

Federal Truth in Lending Laws require the disclosure of credit terms according to a standard formula so that consumers can compare different credit sources directly. Regulation Z, the regulation promulgated pursuant to the Truth in Lending Act (TILA), requires disclosure of “any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or condition of the extension of credit.” If a funeral home charges for the extension of credit over a period of installments, TILA disclosures must be made under federal law. However, proponents argue that funeral establishments do not comply with federal disclosure laws and state laws regulating the funeral industry fail to specifically require disclosure of funeral financing interest charges to consumers.

Because adoption of the proposed resolution would protect consumers from confusion as to what charges are involved in financing funerals, Section 7685 should be amended to require disclosure. For all these reasons, this resolution should be approved in principle.

This resolution is related to 05-05-2008.

**TEXT OF RESOLUTION**

RESOLVED that the Conference of Delegates recommend that legislation be sponsored to amend the California Business and Professions Code § 7685 to read as follows:

- 1 § 7685
- 2 (a) Every funeral director shall provide to any person, upon beginning discussion
- 3 of prices or of the funeral goods and services offered, a written or printed list containing,
- 4 but not necessarily limited to, the price for professional services offered, which may
- 5 include the funeral director's services, the preparation of the body, the use of facilities,
- 6 and the use of automotive equipment. All services included in this price or prices shall

7 be enumerated. A written notice shall be provided to the person that interest may be added  
8 to the funeral services contract for the services offered if the funeral services contract if  
9 paid in installment payments. The interest rate shall be enumerated over the course of the  
10 installment contract.

11 (b) The list shall also include a statement indicating that the survivor of the  
12 deceased who is handling the funeral arrangements, or the responsible party, is entitled to  
13 receive, prior to the drafting of any contract, a copy of any preneed agreement that has  
14 been signed and paid for, in full or in part, by or on behalf of the deceased, and that is in  
15 the possession of the funeral establishment.

16 (c) The funeral director shall also provide a statement on that list that gives the  
17 price range for all caskets offered for sale.

18 The funeral director shall also provide a written statement or list that, at a  
19 minimum, specifically identifies a particular casket or caskets by price and by thickness of  
20 metal, or type of wood, or other construction, interior and color, in addition to other casket  
21 identification requirements under Title 16, Code of Federal Regulations, Part 453 and any  
22 subsequent version of this regulation, when a request for specific information on a casket  
23 or caskets is made in person by any individual. Prices of caskets and other identifying  
24 features such as thickness of metal, or type of wood, or other construction, interior and  
25 color, in addition to other casket identification requirements required to be given over the  
26 telephone by Title 16, Code of Federal Regulations, Part 453 and any subsequent version  
27 of this regulation, shall be provided over the telephone, if requested.

(Proposed new language underlined; language to be deleted stricken)

**PROPONENT:** San Fernando Valley Bar Association

**STATEMENT OF REASONS:**

Existing Law: There is no notice that interest charges may be added to a pre-need funeral services contract or to a funeral services contract if paid in installment payments.

This Resolution: This resolution would provide for a structure wherein the consumer would be notified, in writing, that interest charges would be added to a funeral services contract if the funeral services contract is paid in installment payments. This resolution would educate the consumer as to the interest rate over the course of the funeral services contract.

The Problem: Currently, funeral services contracts itemize the costs for: funeral director's funeral director's time and services, the use of the facilities, the preparation of the body and other professional services, the use of automotive and other necessary equipment to move and transport the body, the casket, the outside receptacle, clothing if necessary, or to dress the body, flowers, cemetery or crematory charges, newspaper notices, clergy honorarium, transcripts, telegrams, long distance telephone calls, and music. However, there is no requirement that interest charges, if applicable, be made aware to the consumer. Often, funeral services contracts have a listing of the items purchased and then a grand total with a payment plan for those who cannot afford to pay the entire balance in full. However, there is no indication as to any interest charged or the interest rate charged, nor is it required to indicate so on the funeral services

contract. Consumers may not even be aware that they are paying interest over the course of the funeral services contract. This resolution would require that a notice be provided to the consumer to advise that interest may be added to the funeral services contract and what rate may be charged for the interest.

**IMPACT STATEMENT:**

This resolution does not affect any other law, statute or rule.

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**RESPONSIBLE FLOOR DELEGATE:**

**RESOLUTION 05-05-2008**

**DIGEST**

Business & Professions Code: Funeral Services Interest Charges

Amends Business & Professions Code section 7685.2 to require written disclosure of the terms of interest charges where a funeral services contract is paid in installments.

**RESOLUTIONS COMMITTEE RECOMMENDATION**

APPROVE IN PRINCIPLE

History

No similar resolution found.

Reasons

This resolution amends Business & Professions Code section 7685.2 to require written disclosure of the terms of interest charges where a funeral services contract is paid in installments. This resolution should be approved in principle because truth in lending and consumer protection laws favor disclosure of credit and financing terms.

Truth in Lending Laws require the disclosure of credit terms according to a standard formula so that consumers can compare different credit sources directly. Regulation Z, the regulation promulgated pursuant to the Truth in Lending Act (TILA), requires disclosure of “any charge payable directly or indirectly by the consumer and imposed directly or indirectly by the creditor as an incident to or condition of the extension of credit.” If a funeral home charges for the extension of credit over a period of installments, under TILA disclosures must be made under federal law. However, proponents argue that laws regulating the funeral industry fail to specifically require disclosure of interest and charges connected with financing funeral services.

Adoption of this proposed resolution would protect consumers from confusion as to what charges are involved in financing funeral services, by amending Section 7685.2 to require disclosure of the same.

This resolution is related to 05-04-2008.

**TEXT OF RESOLUTION**

RESOLVED, that the Conference of Delegates recommend that legislation be sponsored to amend the California Business and Professions Code § 7685.2 to read as follows:

- 1 § 7685.2
- 2 (a) No funeral director shall enter into a contract for furnishing services or
- 3 property in connection with the burial or other disposal of human remains until he or she
- 4 has first submitted to the potential purchaser of those services or property a written or
- 5 printed memorandum containing the following information, provided that information is
- 6 available at the time of execution of the contract:
- 7 (1) The total charge for the funeral director's services and the use of his or her

8 facilities, including the preparation of the body and other professional services, and the  
9 charge for the use of automotive and other necessary equipment.

10 (2) An itemization of charges for the following merchandise as selected: the casket,  
11 an outside receptacle, and clothing.

12 (3) An itemization of fees or charges and the total amount of cash advances made  
13 by the funeral director for transportation, flowers, cemetery or crematory charges,  
14 newspaper notices, clergy honorarium, transcripts, telegrams, long distance telephone calls,  
15 music, and any other advances as authorized by the purchaser.

16 (4) An itemization of all interest charges and fees which will be added to bill of  
17 sale or which will be added to the total charges not otherwise indicated in the funeral  
18 contract.

19 (4)(5) An itemization of any other fees or charges not included above.

20 (5)(6) The total of the amount specified in paragraphs (1) to (4) (6), inclusive.

21 If the charge for any of the above items is not known at the time the contract is  
22 entered into, the funeral director shall advise the purchaser of the charge therefor, within a  
23 reasonable period after the information becomes available. All prices charged for items  
24 covered under §§ 7685 and 7685.1 shall be the same as those given under such sections.

25 [Subdivisions (b) – (c) remain unchanged.]

(Proposed new language underlined; language to be deleted stricken)

**PROPONENT:** San Fernando Valley Bar Association

**STATEMENT OF REASONS:**

Existing Law: There is no law governing any itemization of any interest charges for funeral services contract.

This Resolution: This resolution would provide for a structure wherein the interest charges added to a funeral services contract would be itemized so that the consumer is aware of the total amount to be paid over the lifetime of the contract.

The Problem: Currently, funeral services contracts itemize the costs for: funeral director's funeral director's time and services, the use of the facilities, the preparation of the body and other professional services, the use of automotive and other necessary equipment to move and transport the body, the casket, the outside receptacle, clothing if necessary, or to dress the body, flowers, cemetery or crematory charges, newspaper notices, clergy honorarium, transcripts, telegrams, long distance telephone calls, and music. However, there is no requirement that interest charges, if applicable, be made aware to the consumer. Often, funeral services contracts have a listing of the items purchased and then a grand total with a payment plan for those who cannot afford to pay the entire balance in full. However, there is no indication as to any interest charged or the interest rate charged, nor is it required to indicate so on the funeral services contract. This resolution would require that the funeral services contract list any interest or fees added to the contract.

**IMPACT STATEMENT:**

This resolution does not affect any other law, statute or rule.

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**RESPONSIBLE FLOOR DELEGATE:**