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Corporations

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Corporations

by *Harry C. Sigman**

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I. Introduction

The major 1969 corporate law developments of particular interest to the California practitioner were: (1) California appellate decisions which, at least by implication, greatly broaden the scope of a controlling shareholder's duty to minority shareholders; (2) amendments to the California Corporations Code; and (3) amendments to the Delaware General Corporation Law.

In *Jones v. H. F. Ahmanson & Co.*,¹ the California Supreme Court declared that majority shareholders must adhere to a standard of good faith and inherent fairness to minority shareholders in transactions where control of the corporation is material. In *Brown v. Halbert*,² the Court of Appeal spoke of a "fiduciary relationship" between the dominant stockholder and the minority stockholders even in the absence of "special facts."

There were several amendments to the California Corporations Code in 1969, the most important of which concern

1. 1 Cal.3d 93, 81 Cal. Rptr. 592, 460 P.2d 464 (1969).

2. 271 Cal. App.2d 252, 76 Cal. Rptr. 781 (1969).

expanded corporate information filings with the Secretary of State and increased flexibility in determining accounting treatment of certain transactions.³

In response to the desires of corporate management as reflected by the efforts of the corporate bar, extensive changes were made in the Delaware General Corporation Law in 1969, carrying further Delaware's pro-management orientation vis-à-vis stockholders and creditors; much of this legislation was also in furtherance of the goal of minimizing formality. Although this publication is concerned primarily with trends and developments in California law, Delaware corporation law is of great importance to the California bar. Most California attorneys have clients that are, should be, or may in the future be incorporated under Delaware law, or clients that may acquire or be acquired by Delaware corporations, or clients that may become stockholders or creditors of Delaware corporations.⁴

3. The extensive revision of California's "blue sky" law, which became effective January 2, 1969, was enacted during 1968. See Bader, *BUSINESS ASSOCIATIONS, Cal Law—Trends and Developments 1969*, p. 139.

4. As a result of Delaware's liberal statute, its extensive and rather sophisticated judicial development of corporation law and its sympathetic attitude towards business corporations, "Delaware became and remains the most popular state in which to incorporate any interstate company of substantial size." Cary, *Cases and Materials on Corporations* 9 (4th ed. 1969). See generally, Israels, *Corporate Practice*, pp. 159-160 (2d ed. 1969), and Rohrlich, *Organizing Corporate and Other Business Enterprises* Ch. VI (4th ed. 1967). Some of the key features of Delaware law that make it attractive have been described as follows: In addition to lower capital stock or franchise taxes in Delaware, other advantages which induce corporate

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managements to seek incorporation in Delaware include: greater freedom to pay dividends and make distributions; greater ease of charter amendment and less restrictions upon selling assets, mortgaging, leasing, and merging, due to the lower percentage of shareholder approval required and also by virtue of lesser rights of appraisal for dissenting minority shareholders; freedom from mandatory cumulative voting; permission to have staggered boards of directors; lesser pre-emptive rights for shareholders; clearer rights of indemnification for directors and officers; greater freedom of action in many crucial respects for management; and a climate of opinion, thought to be prevalent in the legislature and courts, generally favorable to management and generally unreceptive to the dissident minority shareholder. Kaplan, *Foreign Corporations and Local Corporate Policy*, 21 Vand. L. Rev. 433 at 436 (1968).

II. Judicial Development of Protection of Minority Shareholders

The need for protection of minority shareholders, particularly in connection with the disposition of controlling stock interests, has been the subject of much scholarly analysis.⁵ *Brown v. Halbert*,⁶ decided by the Court of Appeal on March 28, 1969, and *Jones v. H. F. Ahmanson & Co.*,⁷ decided by the Supreme Court on November 7, 1969,⁸ held that a requirement of fairness to the minority exists in transactions where control of the corporation is material.

The so-called "traditional" or "majority" approach holds that a controlling shareholder owes a fiduciary duty to the corporation but not to minority shareholders, and that the sale of control⁹ at a premium is permissible provided that the sale

5. See, e.g., Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 Harv. L. Rev. 505 (1965); Javaras, *Equal Opportunity in the Sale of Controlling Shares: A Reply to Professor Andrews*, 32 U. Chi. L. Rev. 420 (1965); Berle, *The Price of Power: Sale of Corporate Control*, 50 Cornell L.Q. 628 (1965); Jennings, *Trading in Corporate Control*, 44 Cal. L. Rev. 1 (1956); Eisenberg, *The Legal Role of Shareholders and Management in Modern Corporation Decision Making*, 57 Cal. L. Rev. 1 (1969); and Bayne, *The Sale-of-Control Premium: The Intrinsic Illegitimacy*, 47 Texas L. Rev. 215 (1969).

6. 271 Cal. App.2d 252, 76 Cal. Rptr. 781 (1969); original opinion modified, April 25, 1969 (see 271 ACA 881).

7. 1 Cal.3d 93, 81 Cal. Rptr. 592, 460 P.2d 464 (1969).

8. Opinion modified on denial of rehearing, December 10, 1969.

9. With regard to the meaning of "control" in this context, see the Andrews and Jennings articles cited at

note 5 above. In both the *Jones* and *Brown* cases, the defendants owned and dealt with stock interests greater than 50%. It remains to be seen how the doctrine enunciated in those cases will be applied to transactions in shares aggregating less than 50% but still constituting "control" for various purposes. See, e.g., *Essex Universal Corp. v. Yates*, 305 F.2d 572, 13 ALR3d 346 (2d Cir., 1962) where, on remand, the District Judge would be required to make a finding that there was a "practical certainty" that the purchaser of the 30% block could indeed elect a majority of the board in order to hold valid a clause in the transfer agreement requiring the resignation of directors. See also *Caplan v. Lionel Corp.*, 20 App. Div.2d 301, 246 N.Y.S.2d 913 (1964), *aff'd* 14 N.Y.2d 877 (1964), 249 N.Y.S. 2d 877, 198 N.E.2d 908 (owner of 3% stock interest agreed to have seven directors resign seriatim; court voided election, holding that corporate management is not a subject of trade and cannot be bought apart from actual stock control, but stating that "where there has been a transfer of a majority of stock, or even such a percentage

does not result in injury to the corporation and does not involve an unlawful sale of corporate office. Injury to the corporation has been found where the controlling shareholder fraudulently or negligently transfers control to purchasers who subsequently mismanage or loot the corporation.¹⁰ Also, liability has been imposed where the seller induced the purchaser to buy the controlling shares rather than the corporate assets sought by the purchaser, thus diverting to himself a corporate opportunity.¹¹ In other jurisdictions, the so-called "special facts" doctrine was adopted to permit minority shareholders to obtain a portion of the premium or to recover damages in certain situations where the transfer of control did not result in injury to the corporation but there was inequitable conduct on the part of the controlling shareholder. Modern California cases¹² have applied the "special facts" doctrine, although older cases contain language asserting the "traditional" approach.¹³ In *American Trust Co. v. California Western States Life Insurance Co.*,¹⁴ the Supreme Court analyzed these earlier cases, stating that such language was dicta, and observed that "the question is still open in this state as to whether we shall follow the majority rule, the majority rule as modified by the 'special facts' doctrine, or the minority rule;"¹⁵ In *Taylor v. Wright*,¹⁶ Justice Peters predicted that the Supreme Court would "adopt either the 'special facts' doctrine or the minority rule."¹⁷

as gives working control, a change of directors by resignation and filled vacancies is proper." (246 N.Y.S.2d 913, 950).

10. See, e.g., *Gerdes v. Reynolds*, 28 N.Y.S.2d 622 (1941); *Insuranshares Corp. v. Northern Fiscal Corp.*, 35 F. Supp. 22 (E.D., Pa. 1940).

11. See, e.g., *Dunnett v. Arn*, 71 F. 2d 912 (10th Cir., 1934); *American Trust Co. v. California Western States Life Insurance Co.*, 15 Cal.2d 42, 98 P.2d 497 (1940); *Commonwealth Title Insurance & Trust Co. v. Seltzer*, 227 Pa. 410, 76 A. 77 (1910); but see

Tryon v. Smith, 191 Ore. 172, 229 P.2d 251 (1951).

12. E.g., *Low v. Wheeler*, 207 Cal. App.2d 477, 24 Cal. Rptr. 538 (1962).

13. E.g., *Ryder v. Bamberger*, 172 Cal. 791, 158 P. 753 (1916).

14. 15 Cal.2d 42, 98 P.2d 497 (1940).

15. 15 Cal.2d 42, 61, 98 P.2d 497, 507 (1940).

16. 69 Cal. App.2d 371, 159 P.2d 980 (1945).

17. 69 Cal. App.2d 371, 382, 159 P.2d 980, 985 (1945).

Against this background, let us examine the *Brown* and *Jones* cases.

In *Brown v. Halbert*,¹⁸ four minority stockholders brought a class action¹⁹ seeking, inter alia, to impose a trust on a portion of the funds the defendants realized from the sale of their majority stock interest in the Tulare Savings & Loan Association.²⁰

Halbert, president, chairman of the board and dominant stockholder of the association, was approached by a prospective purchaser and asked *if the association was for sale*. Halbert replied that it was not, but that he and his wife would consider selling their shares (53% of the outstanding stock) at 2-1/2 times book value. The association's board of directors and the other stockholders were apparently never consulted as to the offer to buy the association. Subsequently, the Halberts entered into an agreement to sell their stock for 2-1/2 times book value, or \$1,548.05 per share. The agreement provided, among other things, that the buyer could inspect the books of the association; that, contrary to past practice, no dividends were to be paid during the period of escrow; and that, upon the close of escrow, the selling stockholders would submit resignations as officers and directors and hold such meetings as might be requested by the buyer. The minority stockholders were not informed of the transaction until after it had been negotiated.

18. 271 Cal. App.2d 252, 76 Cal. Rptr. 781 (1969).

19. The complaint named four defendants, of whom only Edward Halbert was claimed to be the principal violator of fiduciary duties. The three other defendants "are charged with accountability for their acquiescence in his actions and by reason of their acceptance of the benefits." (271 Cal. App.2d 252, 253, n. 1, 76 Cal. Rptr. 781, 782 (1969). The other defendants were Halbert's wife; R. Morris, who was secretary-treasurer, a director and second in command of the operation

of the association, and who was retained as the manager by the purchaser; and Robert Tienken. The opinion does not tell of any connection between Tienken and either Halbert or the association.

20. After the judgment for the defendants was reversed on appeal, the parties reached a settlement agreement providing for liability in the amount of \$175,000. (See Crocker, *Brown v. Halbert—One Small Step for Stockholder Equal Opportunity*, 45 L.A. Bar. Bull. 57 at 80 (1969).)

Upon completion of the purchase of Halbert's stock, the buyer indicated its desire to acquire the stock of the minority stockholders at \$300 per share. Halbert, while still president and chairman of the board, assisted the buyer by pressuring the minority stockholders to sell their shares at that price, telling them that dividends would not be paid for a number of years and that the stock would not be worth much. All but a few minority stockholders sold their stock at prices ranging between \$300 and \$650 per share.

The Court of Appeal reviewed the authorities and stated that the more recent California cases have followed the "special facts" doctrine. It decided, however, that the "special facts" doctrine should not be applied where the "majority stockholder-director sells the controlling block of stock to outside purchasers and by doing so causes the minority stock to be devaluated,"¹ holding that in his capacity as president, chairman of the board and dominant stockholder, Halbert stood in a fiduciary relationship to both the corporation and the minority stockholders. The burden of proof, the court stated, was on Halbert to show that he had not breached his duty in securing a return for his stock higher than that received by the minority stockholders for theirs. In discussing this fiduciary duty, the court stated that:

Every sale of a block of control stock should not per se be subject to attack, but where the amount received by the majority stockholder-director seller is so disproportionate to the price available to the minority stockholders, then such fiduciary-seller must show that no advantage was taken if the sale is questioned.²

Here, Halbert not only failed to make any effort to obtain for the minority the same price that he received, but he used his position to actively assist the buyer to acquire the minority stock at a lower price. The court cited a number of commentators and concluded that:

1. 271 Cal. App.2d 252, 264, 76 Cal. Rptr. 781, 788 (1969).

2. 271 Cal. App.2d 252, 268, 76 Cal. Rptr. 781, 791 (1969).

The rule we have adopted here simply is that it is the duty of the majority stockholder-director, when contemplating the sale of the majority stock at a price not available to other stockholders and which sale may prejudice the minority stockholders, is [sic] to act affirmatively and openly with full disclosure so that every opportunity is given to obtain substantially the same advantages that such fiduciary secured and for the full protection of the minority.³

In a concurring opinion, Justice Draper stated that the *Brown* case "seems to me to fall within the rule of *Low v. Wheeler* [citation omitted], or, at most to require but a moderate and reasonable extension of that rule. Hence I would base the decision upon the special facts doctrine as applied in *Low*."⁴

The complex facts of *Jones v. H. F. Ahmanson & Co.*⁵ are summarized as follows: In May, 1959, 85% of the outstanding stock of United Savings and Loan Association was owned by H. F. Ahmanson & Co. and certain relatives and business associates of H. F. Ahmanson. The remaining 15% was owned by some four hundred persons, including the plaintiff. The Ahmanson group organized a holding company, United Financial Corporation of California, and exchanged their shares in the Association for shares of United.⁶ In 1960, United issued stock and convertible debentures to the public; of the \$7,200,000 proceeds, \$6,200,000 was distributed as a return of capital to the original United stockholders. The accompanying prospectus noted that dividends from the Association would be utilized if the direct earnings of the holding company were insufficient to meet the obligations under the debentures.⁷ In February, 1961, another public

3. 271 Cal. App.2d 252, 272, 76 Cal. Rptr. 781, 793-794 (1969).

4. 271 Cal. App.2d 252, 273-274, 76 Cal. Rptr. 781, 795 (1969).

5. 1 Cal.3d 93, 81 Cal. Rptr. 592, 460 P.2d 464 (1969).

6. In addition to the Association stock, United also owned three insurance agencies and stock in a fourth.

7. In addition, the representations of United to the Corporations Commissioner (according to plaintiff's allegations) asserted that the financial

offering was made by United, accompanied by a secondary offering by the original investors, at an aggregate offering price of \$15,275,000. This created a public market for United stock and, incident thereto, substantially precluded the creation of a public market for the Association stock. In September, 1960, when the book value of the Association stock was \$1,411.57 per share, United (then the owner of 87.3% of the Association stock) offered to purchase some of the minority shares for \$1,100 per share. In December, 1960, the president of the Association, who was at that time a director of both United and the Association, contacted the remaining minority shareholders of the Association and advised them that there would be no dividends paid on the Association stock in the near future except the regular annual \$4 per share dividend. In May, 1961, the minority shareholders were offered United shares worth approximately \$2,400 for each Association share. By way of contrast, the value in August, 1961, of the United shares received by defendants for each Association share exchanged by them in the formation of the holding company had risen to approximately \$8,800, and during 1960–1961 had sold for as much as \$13,127.41. In 1962, the Association paid an extra dividend of \$84 per share.

The defendants in the case were United, fifteen individuals and four corporations, all of whom were present or former shareholders or officers of the Association and all but one of whom incorporated United. Judgment was rendered for defendants after an order sustaining demurrers, and the case on appeal was presented on the pleadings supplemented by stipulated facts.

The Supreme Court dealt first with the contention that plaintiff lacked capacity to sue on the theory that any injury suffered by plaintiff was common to all minority shareholders of the Association and, therefore, that any cause of action

reserves for debenture repayment required by the Commissioner's rules would be satisfied by having United exercise its control to cause the Association to liquidate or encumber its income-producing assets and then cause the Association to distribute the cash proceeds to United.

was derivative in nature.⁸ Rejecting this contention, the Court held that plaintiff did not seek to recover on behalf of the corporation for injury done to the corporation and that the gravamen of her cause of action was injury directly to her and the other minority shareholders. “The individual wrong necessary to support a suit by a shareholder need not be unique to that plaintiff If the injury is not incidental to an injury to the corporation, an individual cause of action exists.”⁹

Plaintiff claimed to represent “all of that portion of the other minority stockholders who are similarly situated who wish to rely thereon and who agree to compensate plaintiff and her attorneys for reasonable attorneys’ fees in an amount to be determined by the court after trial.”¹⁰ The Court held that this was not an allegation of a class composed simply of persons who agreed with plaintiff but that the class designated consisted of the minority shareholders of the Association, i.e., those who held Association stock after the defendants exchanged their shares for United shares. The language concerning agreement to share in the litigation expenses “does no more than state the applicable rule with regard to equitable apportionment of the litigation expenses incurred by a plaintiff who successfully prosecutes an action on behalf of a class.”¹¹ The Court held that the requisite community of interest existed among the minority shareholders and that the class was readily ascertainable.¹²

The Court then turned to the heart of the case in a portion of the opinion captioned “Majority Shareholders’ Fiduciary Responsibility.” The Court rejected the position that shareholders owe no fiduciary obligation to other shareholders “absent reliance on inside information, use of corporate as-

8. See Cal. Fin. Code § 7616.

9. 1 Cal.3d 93, 107, 81 Cal. Rptr. 592, 599, 460 P.2d 464, 471 (1969).

10. 1 Cal.3d 93, 120, 81 Cal. Rptr. 592, 608, 460 P.2d 464, 480 (1969).

11. 1 Cal.3d 93, 120, 81 Cal. Rptr. 592, 608, 460 P.2d 464, 480 (1969).

12. In the *Brown* case, the court stated that the action was clearly a proper class action and that the matter had not been questioned. 271 Cal. App.2d 252, 272, 76 Cal. Rptr. 781, 794 (1969).

sets, or fraud.”¹³ Citing, inter alia, *Brown v. Halbert*,¹⁴ the Court stated: “Any use to which [majority shareholders] put the corporation or their power to control the corporation must benefit all shareholders proportionately and must not conflict with the proper conduct of the corporation’s business.”¹⁵

The Court reviewed earlier California cases and concluded that “[t]he rule that has developed in California is a comprehensive rule of ‘inherent fairness from the viewpoint of the corporation and those interested therein,’ ”¹⁶ and held that this rule applies to officers, directors, and controlling shareholders in the exercise of powers enjoyed by virtue of their position and that it applies to transactions wherein controlling shareholders seek an advantage in the transfer or use of their controlling stock. The opinion declared that the traditional theories of fiduciary obligation as tests of the responsibility of majority shareholders to the minority are not adequate, particularly in view of the increasing complexity of financial transactions. Although the courts have recognized the potential for abuse or unfair advantage in the sale of control at a premium or the sale of control to looters or incompetents, no comprehensive rule had emerged in other jurisdictions, and most of the commentators had approached the problem from the perspective of advantage gained in the sale of control. The Court concluded that the case at bench, in which no transfer of actual control was directly involved, demonstrated that the injury to the minority anticipated by the commentators could be inflicted with impunity under the traditional rules and supported the conclusion that “the comprehensive rule of good faith and inherent fairness to the minority in any transaction where control of the corporation is material”¹⁷ is applicable to controlling shareholders.

13. 1 Cal.3d 93, 108, 81 Cal. Rptr. 592, 599, 460 P.2d 464, 471 (1969).

14. 271 Cal. App.2d 252, 76 Cal. Rptr. 781 (1969).

15. 1 Cal.3d 93, 108, 81 Cal. Rptr. 592, 599, 460 P.2d 464, 471 (1969).

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16. 1 Cal.3d 93, 110, 81 Cal. Rptr. 592, 600, 460 P.2d 464, 472 (1969).

17. 1 Cal.3d 93, 112, 81 Cal. Rptr. 592, 602, 460 P.2d 464, 474 (1969).

The Court then turned to an analysis of the facts, stating that in an effort to exploit the investor interest in stock of savings and loan associations, defendants, in their controlling position, could have created a market for the Association's stock, or could have created a holding company and permitted all of the Association's shareholders to exchange their shares before offering the holding company stock to the public. Under either of these routes, all shareholders would have benefited equally and the minority shareholders would have been able to extricate themselves without sacrifice of their investment if they chose not to remain in the new structure. Thus, said the Court, the defendants chose a course of action in which they used control of the Association to obtain for themselves an advantage not made available to all shareholders, and, on the facts alleged, did so without regard to the resulting detriment to the minority shareholders and in the absence of any compelling business purpose.¹⁸

The opinion points out that the defendants may present evidence at trial tending to show "such good faith or compelling business purpose that would render their action fair under the circumstances,"¹⁹ noting that defendants' burden would have been much less had they afforded the minority an opportunity to exchange their stock on an equal basis or offered to purchase the minority stock at a price arrived at by independent appraisal.²⁰

18. The opinion pointed out that the defendants had secured an additional advantage for themselves through their use of control of the Association when they pledged that control of the Association's assets and earnings to secure the debt of the holding company, a debt that had been incurred for their benefit. The court expressed concern that any decision regarding use of the Association's assets and earnings would have to be made in the context of the potentially conflicting interests of the business needs of the Association and the duty to the United stockholders.

19. 1 Cal.3d 93, 114, 81 Cal. Rptr. 592, 604, 460 P.2d 464, 476 (1969).

20. The defendants suggested that their transfer to United of related insurance businesses and the subsequent acquisition of another savings and loan association by United were necessary to the creation of the market for United shares. "Whether defendants could have created a market for a holding company that controlled a single association or reasonably believed that they could not, goes to their good faith and to the existence of a proper business purpose for electing

Turning to the question of damages,¹ the opinion noted that the transactions in question had resulted in a substantial change in the position of the minority shareholders since control of the Association had been transferred to a publicly held corporation; thereafter the business goals of the Association could be expected to reflect the interests of the holding company rather than the aims of the Association's shareholders. The Court noted that the more familiar fundamental corporate changes—merger, consolidation and dissolution—are accompanied by statutory and judicial safeguards for minority shareholders.

Finding the exchange of stock an integral part of a scheme that the defendants could reasonably have foreseen would have, as an incidental effect, the destruction of a potential public market for Association stock, the Court reasoned that receipt of an appraised value reflecting only book value and earnings would not compensate the minority shareholders for loss of the opportunity to realize a profit from the intangible characteristics that attach to publicly traded stock and enhance its value above book value. Therefore, held the Court, if plaintiff, after trial, establishes facts in conformity with the allegations of the complaint and the stipulated facts, then, upon tender of the Association stock to defendants, plaintiff would be entitled to receive for each share tendered, at her election, either (1) the appraised value of such shares as of the date of the exchange, together with interest at 7% per annum from the commencement of suit, or (2) a sum equivalent to the fair market value, on the date of the commencement of suit, of the United securities received for each share of Association stock, together with interest thereon from the date of the commencement of suit, and the sum of

the course that they chose to follow. At the trial of the cause defendants can introduce evidence relevant to the necessity for inclusion of other businesses." 1 Cal.3d 93, 114, 81 Cal. Rptr. 592, 603-604, 460 P.2d 464, 475-476 (1969).

1. The defendants (in their Petition for Rehearing or Modification of Opinion, pp. 3-8) urged that the discussion of remedies be deleted from the opinion so as to allow the trial court in the first instance to fashion an appropriate remedy based upon the evidence adduced at trial.

\$927.50 (the return of capital received by the original United stockholders), with interest thereon from the date of such return of capital.² This remedy, fashioned by the Court in reviewing a judgment after demurrer, appears to be based on the assumption that the marketing scheme could have been carried out (either directly in the Association stock or through the use of United) had all the minority shareholders been taken along at the outset. In the typical case involving sale of the controlling stock interest at a premium, the extent of the premium would be established as of the time of sale. The Court's second alternative, on the other hand, provides for valuation at a substantially later date, the date plaintiff commences suit.³ Presumably the controlling shareholder can prevent market speculation by the minority by making or procuring a reasonable (e.g., independent appraisal) offer for the minority stock which would, in the event of subsequent suit, put a ceiling on recovery.

Finally, the Court dealt also with the contention that a cause of action had been stated as to restraint of trade in violation of the Cartwright Act,⁴ holding that, assuming arguendo that the Cartwright Act applies to transactions in corporate shares, the complaint was insufficient in that it did not allege a purpose to restrain trade or an agreement among defendants not to purchase shares of Association stock from the minority.

The language of *Brown* and *Jones* is far broader than is necessitated by the facts,⁵ and the practitioner faces

2. An example of the valuation problems presented in the sale-at-a-premium cases is found in the case of *Perlman v. Feldmann*, 219 F.2d 173, 50 A.L.R.2d 1134 (2d Cir., 1955), cert. denied, 349 U.S. 952, 99 L.Ed. 1277, 75 S.Ct. 880 (1955), and, particularly, the opinion of the lower court on remand, 154 F.Supp. 436 (1957).

3. The appraisal remedy given to dissenters in the event of a merger provides for valuation, under Cal. Corps. Code § 4300, as of the "day

before the vote of the shareholders approving the agreement of merger or consolidation, excluding any appreciation or depreciation in consequence of the proposed action."

4. Cal. Bus. & Prof. Code §§ 16720-16758.

5. For example, although the *Brown* opinion speaks of a "fiduciary relationship" between Halbert and the minority, the *Jones* opinion characterizes *Brown* as a "sale of only controlling shareholder's shares to purchaser offer-

substantial problems in dealing with potential applications of these cases. Not the least of these difficulties is the potential conflict-of-laws problem lurking in fact situations where the seller, purchaser or minority stockholders are domiciled outside of California, or the corporate domicile or principal place of business is located elsewhere. Because *Brown* and *Jones* involved California contacts⁶ almost exclusively, there was no need to consider this matter. With these cases the last appellate word on the subject, cautious counsel will probably have to advise prospective sellers (at least those who are actually exercising control or holding corporate office and are not merely passive investors) against accepting an offer for a 51% or greater stock interest (and perhaps even an offer for a smaller stock interest if it represents, by itself or together with stock known to the seller to be then owned by the buyer, "working control"), where the offer is arguably at a premium price (bearing in mind that this will be determined with the benefit of hindsight), unless the offer is accompanied by a like offer (or perhaps a commitment to make such an offer promptly) to the minority stockholders. Like offer meaning the same per share price for all or a similar proportion of their

ing to buy assets of corporation or all shares." 1 Cal.3d 93, 111, 81 Cal. Rptr. 592, 601, 460 P.2d 464, 473 (1969).

6. United was incorporated under Delaware law. The case law on this subject in other jurisdictions is far from clear. *Perlman v. Feldmann*, 219 F.2d 173, 50 A.L.R. 1134 (2d Cir., 1955), cert. denied, 349 U.S. 952, 99 L.Ed. 1277, 75 S.Ct. 880 (1955), supra, decided by the Second Circuit, purportedly applying Indiana law, has generally been considered the leading case imposing liability on majority stockholders for dealing in controlling stock interests. In *Essex Universal Corp. v. Yates*, 305 F.2d 572, 13 A.L.R.3d 346 (2d Cir., 1962), the court said of *Perlman*:

. . . [The] theory was basically that the controlling shareholders in
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selling control to a potential customer had appropriated to their personal benefit a corporate asset: the premium which the company's product could command in a time of market shortage. (305 F.2d 572, 576.)

Furthermore, a Delaware Chancellor said the following about *Perlman* in *Manacher v. Reynolds*, 39 Del. Ch. 401, 165 A.2d 741, 751 (1960):

As to the *Perlman* case, which made such an impact on the legal fraternity, I think it may be distinguished on the ground that its shares were sold to a buyer with predictable resultant sacrifice in the corporation's good will. If this distinction lacks substance, I can only express a preference for the dissent's view that the increment in stock value arising from control belongs to the sellers, absent some breach of duty.

holdings.⁷ At the very least, the seller may have an obligation to notify the minority of the existence of the offer.⁸ The scope of the seller's "fiduciary" obligation remains to be determined. While the foregoing advice to the seller may protect him from a lawsuit, it certainly casts on the buyer burdens not previously thought to exist.⁹ Whether it is now (or ever was) true that the buyer has an absolute right to buy as cheaply as possible, it should be borne in mind that the buyer becomes the dominant shareholder, subject to the "duty of fairness," as soon as his purchase is consummated. It is arguable that this duty devolves upon him even before the transaction is completed.

In summary, while the results of the *Jones* and *Brown* cases were predictable, many unanswered questions remain.

I say this because I am satisfied that a practical decision of this issue has been in existence in the business community for too many years for a court to upset it.

7. According to Professor Andrews: [W]henver a controlling stockholder sells his shares, every other holder of shares (of the same class) is entitled to have an equal opportunity to sell his shares or a pro rata part of them on substantially the same terms. Or in terms of the correlative duty: before a controlling stockholder may sell his shares to an outsider he must assure his fellow stockholders an equal opportunity to sell their shares, or as high a proportion of theirs as he ultimately sells of his own.

. . . First, it neither compels nor prohibits a sale of stock at any particular price; it leaves a controlling stockholder wholly free to decide for himself the price above which he will sell and below which he will hold his shares. The rule only says that in executing his decision to sell, a con-

trolling stockholder cannot sell pursuant to a purchase offer more favorable than any available to other stockholders. Second, the rule does not compel a prospective purchaser to make an open offer for all shares on the same terms. He can offer to purchase shares on the condition that he gets a certain proportion of the total. Or he can even make an offer to purchase 51 per cent of the shares, no more and no less. The only requirement is that his offer, whatever it may be, be made equally or proportionately available to all stockholders.

Andrews, *supra*, at 515-516.

8. In the *Jones* case, the defendants asserted that they had made full disclosure of all of the circumstances surrounding the formation of United.

9. For example, buyers attempting to reach all of the minority shareholders may have to comply with the Williams Bill. (Pub. Law No. 90-439, adding sections 13(d) and (e) and 14 (d), (e) and (f) to the Securities Exchange Act of 1934.)

III. 1969 Amendments to the California Corporations Code

A. Corporate Information Filings

The most notable of the 1969 legislative changes in the California Corporations Code was the amendment of section 3301,¹⁰ and the addition of sections 3301.1–3, effective January 1, 1971.¹¹ The new provisions require more frequent and expanded corporate information filings with the Secretary of State, and impose the drastic sanction of suspension for failure to comply. Section 3301 requires that every domestic corporation organized after January 1, 1971, file with the Secretary of State, within 90 days after the filing of its articles, a statement of the names and complete business or residence addresses of its president, vice president, secretary and treasurer. Furthermore, beginning in 1971, every domestic corporation (except new corporations which file within 90 days after formation) must file such a statement annually during the period between April 1 and June 30.¹² Such filings are to be made on a form to be prescribed by the Secretary of State, together with a filing fee of not more than three dollars.¹³ A copy of any filed statement can be obtained for a one-dollar fee. A corporation is also required to attach a statement of the names and addresses of its current officers when notifying the Secretary of State of a change in the location or address of the corporation's principal office, or in the stated address of its designated agent. Section 3301 was also amended to permit the revocation of a designation of an agent for service of process without a simultaneous designation of a new agent. Finally, new section 3301.3 authorizes the destruction by the Secretary of State of any statement filed under section 3301, when it has been superseded by the filing of a new statement.

10. Unless otherwise indicated, all references in this segment of the article to code sections refer to sections of the California Corporations Code.

11. Stats. 1969, Ch. 1159.

12. The existing requirement for

filing a statement of the location and address of the corporation's principal office was retained.

13. A \$5 filing fee is set for a combined officer's statement, principal office statement, and designation of agent for service.

It is the sanction attached to the failure to comply with the filing requirements that makes these amendments so important. Formerly, the statute prescribed no penalty for failure to file. New section 3301.1 requires that the Secretary of State shall, "as soon as practicable," suspend an offending corporation's powers, rights and privileges and notify the corporation (at the last address disclosed in the records of the Secretary of State) and the Franchise Tax Board thereof.¹⁴ One consequence of such suspension would be the risk that the corporate name might be appropriated by another person during the suspension. Section 3301.2 provides a procedure for obtaining relief from suspension by applying to the Secretary of State on a prescribed form, filing the required information and paying the filing fee.¹⁵

B. *Reservation of Corporate Names*

Another important change amends section 310 to extend the effective period of certificates of reservation of a corporate name from 30 to 60 days; concurrently, Government Code section 12199 was amended to increase the fee for issuing such certificates to \$4.00.

C. *Accounting Treatment of Certain Transactions*

Several changes were made¹⁶ with regard to methods of accounting for capital items. These changes vest the board of directors with greater discretion in determining the accounting treatment of various transactions. The board may now allocate to paid-in surplus a portion of the consideration re-

14. The Secretary of State's office has announced it will give advance notice of the filing requirements to the domestic corporations for which it has addresses. Commencing in 1971, each person submitting articles for filing will receive a copy of the statement form. As to the annual filing requirement, the Secretary of State's office plans to mail a copy of the required form to each corporation early in March of each year. This

should help to prevent suspensions arising out of inadvertent failures to comply with the new requirements. *Reports*, State Bar of California, vol. 10, no. 1, p. 2 (Jan., 1970).

15. Such application may be made by any shareholder or creditor or by a majority of the surviving directors or trustees of the corporation.

16. Stats. 1969, Ch. 481, amending §§ 1900, 1901, 3905 and 4117.

ceived for no-par stock (without regard to liquidation preference); heretofore all such consideration was required to be credited to stated capital.¹⁷ Surplus on the books of a corporation acquired by purchase (section 3905) or by merger or consolidation (section 4117) may now, to the extent not capitalized by the issue of shares or otherwise, be entered as earned or paid-in surplus, if to do so would be “in accordance with generally accepted accounting principles.”¹⁸ Finally, excess consideration received from the issuance of par value shares may now, upon a sale of the corporation’s assets, or upon a merger or a consolidation, be entered as either earned or paid-in surplus, in accordance with generally accepted accounting principles.

D. *Treasury Shares*

When a corporation acquires its own shares in connection with a merger or consolidation or a distribution of another corporation’s assets, section 1709 requires that those shares either be carried as treasury shares or retired. This section was amended to specify that this rule applies whether the other corporation involved is domestic or foreign.

E. *Plan of Arrangement*

Section 4400 authorizes various fundamental changes in the operation or structure of a corporation without director or shareholder approval, if the changes are carried out pursuant to a reorganization under federal law confirmed by an order of a federal court. The scope of sections 310, 4400, 4403 and 4404, was expanded¹⁹ to include actions carried out pursuant to a plan of arrangement authorized under federal law, under the same conditions as those specified for reorganizations.²⁰ Authority so granted may be exercised by

17. This could be of consequence since dividends may be paid and stock may be redeemed out of paid-in surplus. (See §§ 1500, 1706.)

18. This standard is in contrast to the previous standard of “sound accounting practice.”

19. Stats. 1969, Ch. 322.

20. Section 4401 enumerates the types of reorganizations for which § 4400 authority is available; there is no similar provision limiting the eligible types of arrangements, and presumably any plan of arrangement

or under the supervision of a trustee, receiver, or committee of creditors.

F. *Miscellaneous*

Finally, several minor changes were adopted, including the following: New section 3632.5¹ provides an additional method for amending the articles of incorporation of a nonstock corporation.² If the bylaws so provide, the articles may now be amended by the vote or written consent of two-thirds of a policy-making committee created by and composed solely of members of the corporation.³ A.B. 1096 codified various provisions presently found in the state Constitution, which are omitted from the proposed revised Constitution. New section 129 states: "No corporation, association or individual shall issue or put in circulation, as money, anything but the lawful money of the United States."

IV. 1969 Amendments to the Delaware General Corporation Law

The 1969 amendments to the Delaware General Corporation Law affected some thirty sections.⁴ Since that statute had undergone extensive revision in 1967, many of the 1969

approved by a federal court under a federal statute will qualify.

1. Stats. 1969, Ch. 396.
2. Other methods are set forth in § 3632.
3. Section 3672, dealing with the certificate of amendment to be filed with the Secretary of State, was amended to conform with this new provision.
4. House Bill No. 270, Laws of 1969, approved June 23, 1969, and effective July 15, 1969, amended sections 102, 103, 122, 126, 141, 144, 151, 153, 155, 212, 213, 214, 218, 224, 228, 229, 242, 251, 252, 253, 256, 258, 262, 271, 275, 311, 344, 371 and 379 of the General Corporation Law. House Bill No. 290, Laws of 1969, approved and

effective June 23, 1969, amended section 243. House Bill No. 252, Laws of 1969, approved June 23, 1969, and effective July 15, 1969, amended sections 371 and 391 to increase certain filing fees. The same bill also increased, by 10%, the Delaware annual franchise tax and raised the minimum tax from \$10 to \$20 and the maximum from \$100,000 to \$110,000. Also, the annual report filing fee was increased to \$10 for domestic corporations and to \$30 for foreign corporations.

Unless otherwise indicated, all references in this segment of the article to code sections refer to sections of the Delaware General Corporation Law.

changes were of a housekeeping nature. It is the purpose of this segment of the article to call attention to the more important changes, particularly those of a substantive nature, keying (by footnote citation) the amendments discussed to the parallel California statutory provisions. The amendments are discussed under four headings: "Corporate Finance Matters;" "Corporate Management Matters"; "Stockholders Matters"; and "Miscellaneous". The general thrust of the amendments is to enhance the attractiveness of the Delaware corporation as an intreprenurial tool by facilitating corporate activity and increasing the power and flexibility of corporate management.⁵

A. *Corporate Finance Matters*

1. Merger, Consolidation and Sale of Assets

Two of the most important changes made in 1969 were in the area of merger, consolidation and sale of assets. First, the requirement for stockholder approval of a merger or consolidation was reduced from two-thirds of the total number of the outstanding shares of capital stock to "a majority of the outstanding stock of the corporation entitled to vote thereon."⁶ This is not merely a reduction from two-thirds to a majority; the amendment also makes it possible to deprive a stockholder of the right to vote on this issue. Whether stock is entitled to vote on a merger is determined by the certificate of incorporation.⁷ The provision for stockholder

5. For other discussions of the subject matter of this segment of the article see Folk, *Amendments to the Delaware General Corporation Law and Technical Amendments Act* (Corporation Service Company, 1969), and Arshat and Stapleton, *Analysis of the 1969 Amendments to the Delaware Corporation Law* (Prentice-Hall Corporation Law Service 347).

6. Del. Corp. Law § 251. Unless the articles require a greater percentage, Cal. Corps. Code § 4107 requires

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approval of "not less than two-thirds of the issued and outstanding shares of each class, regardless of limitations or restrictions on the voting power thereof, entitled to vote at a meeting. . . ."

7. This amendment, when read in conjunction with Del. Corp. Law § 212, as amended, authorizes the granting to a particular class or series of stock of a weighted vote in connection with a merger or consolidation.

approval of a sale of all or substantially all of the corporation's assets was amended to make its language identical to that of the amended merger provisions.⁸

Second, the permissible forms of consideration which may be given to effect a merger have been enlarged; now "property" and "rights" may be utilized, as well as cash and securities. The statute expressly authorizes the conversion or exchange of shares of a constituent corporation into or for "cash, property, rights or securities of any other corporation," as well as shares of the surviving or resulting corporation.⁹ Thus, the merger agreement may now provide for the conversion of shares into a right to receive shares of the resulting or surviving corporation, or a parent thereof (the so-called triangular merger), in the future upon the happening of specified events, even if that right is not evidenced by a "security." Parallel changes have been made in the provisions permitting the merger of Delaware and non-Delaware corporations and the provisions concerning short-form mergers between parent and subsidiary.¹⁰

By virtue of the 1967 general revision, a merger could be consummated without stockholder approval where the surviving corporation did not amend its charter or issue or deliver shares (authorized and unissued or treasury shares) of any class of its stock in excess of 15 percent of the number of shares of that class outstanding immediately prior to the merger. The 1969 amendment continues this exemption from stockholder approval, but requires that there be executed and filed a certificate reciting the facts which excuse stock-

8. Del. Corp. Law § 271(a); the former language called for "the affirmative vote of the holders of a majority of the stock issued and outstanding having voting power at a stockholders' meeting." Cal. Corps. Code § 3901 requires approval of "a majority of the voting power of the corporation," unless the articles impose a more stringent approval requirement.

9. Del. Corp. Law §§ 251, 252; compare Cal. Corps. Code § 4103

("cash, property, or securities, in whole or in part, in lieu of shares [of the consolidated or surviving corporation]. . . .")

10. Del. Corp. Law §§ 252, 253; compare Cal. Corps. Code §§ 4118 (merger or consolidation of California and foreign corporation), 4124 (short-form merger of California corporation and California or foreign wholly-owned subsidiary).

holder approval. The amendment further provides that such filing constitutes a representation that the facts remain true immediately prior to the filing.¹¹

A requirement that an agreement governing the merger of Delaware corporations set forth the provisions or facts required or permitted under Delaware law to be stated in the charter was deleted. The substitute provision requires that the merger agreement state such amendments in the charter of the surviving corporation as are desired to be effected by the merger or consolidation, or if no such amendments are desired, a statement that the charter of one of the constituents shall be the charter of the surviving or resulting corporation.¹²

Finally, several language changes were made in the provisions governing the merger or consolidation of foreign and Delaware corporations.¹³ Previously, the statute authorized such a merger if the foreign jurisdiction was one “which permit(s) such merger or consolidation.” It was unclear whether this clause required that the foreign law authorize the particular form of merger authorized in Delaware, or merely that the foreign law authorize generally a merger between domestic and foreign corporations.¹⁴ The statutory language was amended to make clear that the latter interpretation was correct. Therefore, a Delaware corporation may utilize the short-form procedure even though the domicile of the foreign corporation with which it is merging does not authorize such short-form mergers. Of course, the foreign corporation must still comply with the requirements of the law of its domicile.¹⁵

2. Appraisal Rights

In Delaware, appraisal rights are given only to dissenters from proposed mergers and consolidations.¹⁶ Even as to

11. Del. Corp. Law § 251(f).

12. Del. Corp. Law § 251(b).

13. Del. Corp. Law §§ 252, 253, 256 and 258.

14. This question arose particularly in the context of short-form mergers pursuant to Del. Corp. Law § 253.

15. Compare Cal. Corps. Code § 4118, dealing with mergers and consolidations of California and foreign corporations.

16. This is true in California as well. See Cal. Corps. Code §§ 4300 et seq.

these, Section 262(k) heretofore denied (in the absence of a contrary charter provision) appraisal rights with respect to any class or series of shares registered on a national securities exchange or held of record by not less than 2,000 stockholders. Appraisal rights were also denied to stockholders of a surviving corporation if, by virtue of section 251(f), a vote of the stockholders of the surviving corporation was not required. Appraisal rights were withheld from these two categories, however, only if the plan provided for the stockholders to receive only stock of the resulting or surviving corporation or stock and cash in lieu of fractional shares. So-called triangular mergers have become quite common, and the effect of this provision was to deny appraisal rights to the stockholders of a publicly held company who received stock of the resulting or surviving corporation, but to confer such rights upon stockholders of such a corporation who received shares of a parent of the resulting or surviving corporation. Section 262(k) now denies the appraisal remedy if the stockholders receive stock of "any other corporation" so long as the stock they are to receive is either registered on a national securities exchange or is held of record by not less than 2,000 stockholders. Thus, the appraisal right is now avoidable in the common situation where the stockholders of a constituent corporation receive the stock of the parent of the resulting or surviving corporation.¹⁷

On the other hand, section 262(b) was amended¹⁸ to provide the appraisal remedy to stockholders who "were not entitled to vote" on the merger or consolidation and who filed written objection thereto before the taking of the vote.¹⁹ Also, section 262 was further amended to preserve the appraisal right, where the merger or consolidation is approved by

17. Provided that the stock received is either registered on a national securities exchange or is held of record by not less than 2,000 shareholders.

18. This change was necessitated by the amendment to Del. Corp. Law § 251(c), discussed above in connection with mergers and consolidations.

19. Under the amended merger provisions, notice of the stockholders' meeting called to vote upon a merger must be sent to all stockholders whether or not they are entitled to vote on the merger. Del. Corp. Law § 251(c).

written consent rather than at a stockholders' meeting, for those stockholders who either did not, or had no right to, consent thereto.

3. Consideration for Shares

Section 153 was amended to delete the requirement that consideration for shares be expressed in dollars.²⁰

4. Convertible Securities

By greatly expanding the types of permissible convertible securities, the amendment to section 151(e) increased flexibility in corporate finance matters. Stock of any class or series may now be made convertible into or exchangeable for stock of any other class or series; convertibility had previously been limited to "preferred or special stock." Thus, there is now explicit authorization for convertible common stock and for the convertibility of shares of any series into another series of the same class. Furthermore, the statute now explicitly states that such conversion or exchange may be (1) at the option of the corporation, or (2) at the option of the holder of the security, or (3) upon the happening of a specified event.¹

5. Fractional Shares

The 1969 amendments also increased flexibility in instances when a corporation elects not to issue fractional shares. Previously, the corporation had either (1) to pay in cash the fair value of fractional shares as of the time of the determination of persons entitled to receive them, or (2) to issue scrip or warrants entitling the holder to receive a certificate for a full share upon surrender of scrip or warrants aggregating a full share. Section 155 now permits the corporation, as a third alternative, to "arrange for the disposition of fractional interests by those entitled thereto." Further, the amendments

²⁰ Compare Cal. Corps. Code § 1112, requiring the board to "state by resolution its determination of the fair value to the corporation in mone-

tary terms" of the non-money consideration for shares.

¹ Compare Cal. Corps. Code §§ 1100, 1103 and 1104.

specified the rights (voting, receipt of dividends, and participation in liquidation distributions) which are enjoyed by holders of fractional shares, but not by scrip or warrant holders absent specific provision therefor.²

B. *Corporate Management Matters*

Delaware law has long provided that a corporation may, by charter provision, deviate from the norm of management of its business by the board of directors.³ It was thereby intended to permit owners to establish whatever managerial structure best suited a particular enterprise. Nevertheless, questions persisted as to the scope of the authorization to situate ultimate managerial power elsewhere than in the board, and as to the relationship between section 141(a), and statutory provisions expressly calling for action by directors. Section 141(a) now provides that where in allocation of such powers diverges from the norm, all powers and duties usually conferred or imposed upon the board "shall be exercised or performed to such extent and by such person or persons" as the charter provides.

In addition to the powers granted in the charter and elsewhere in the statute, Delaware corporations have the powers specified in section 122. Prior to the 1969 amendments, Delaware corporations were empowered, in time of war or other national emergency, notwithstanding charter restrictions, to do any lawful business in aid thereof at the request or direction of any apparently authorized governmental authority. Section 122(12) was amended to empower the corporation to "transact any lawful business which the corporation's board of directors shall find to be in aid of governmental authority." This removes the limitation to emer-

2. Compare Cal. Corps. Code § 2215 (articles or by-laws may deprive fractional shares of voting rights).

3. Del. Corp. Law § 141(a); compare Cal. Corps. Code § 800, which provides: "Subject to limitations of the articles and of this division as to

action which shall be authorized or approved by the shareholders, all corporate powers shall be exercised by or under authority of, and the business and affairs of every corporation shall be controlled by [the board of directors]."

gency conditions and shifts the focus to the board's finding of facts and exercise of business judgment.

The board may now consist of a single member.⁴ The statute previously had set a minimum of three, unless all shares were owned beneficially and of record by fewer than three persons, in which event the number of directors could be equal to or greater than the number of stockholders. Another amendment to section 141(b) clarified existing law by explicitly stating that the number of directors may be fixed by either the charter or the by-laws.⁵ Section 141(b) was also amended to delete the numerical minimum with regard to a quorum of directors (formerly two directors, except in the case of a one-man board); the fractional minimum of 1/3, however, has been retained. Thus, the statute now provides that a majority of the board constitutes a quorum unless a greater number is required by the charter or by-laws and, unless the charter otherwise provides, the by-laws may provide for a smaller quorum so long as it is not less than 1/3 of the entire board, e.g., one director when the board consists of three or fewer directors.⁶

Amendments to section 229 and the addition of section 141(i) have facilitated the conduct of board meetings and dispensed with unnecessary formalities. Attendance at a meeting of the board or any committee now operates as a waiver of notice of that meeting, and where a written waiver of notice is utilized the waiver need not recite the purpose of the meeting.⁷ These provisions previously applied only

4. Del. Corp. Law § 141(b); Cal. Corps. Code § 800 requires a board of not less than three directors.

5. Compare Cal. Corps. Code §§ 301 (d) and 501(d), permitting the articles or by-laws to provide for an indefinite number of directors (not less than a stated minimum of five or more), and permitting the number of directors to be changed by amendment of the articles or, unless the articles provide otherwise, amendment of the by-laws.

6. Compare Cal. Corps. Code § 816, CAL LAW 1970

which provides as follows: "A majority of the authorized number of directors constitutes a quorum of the board for the transaction of business unless the articles or by-laws provide that a different number, which in no case shall be less than one-third the authorized number of directors, nor less than two, constitutes a quorum."

7. Compare Cal. Corps. Code § 814, which provides in part as follows: "The transactions of any meeting of the board of directors, however called

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to stockholder meetings. Furthermore, a member of the board or of a committee is deemed present in person at a meeting if, by virtue of a conference telephone call or similar communications arrangement, all persons participating in the meeting can hear each other. The applicability of this provision can be negated by a provision in the charter or by-laws.

Section 141(c) previously contained a sweeping authorization which, read literally, empowered committees of the board of directors to exercise all powers of the board to the extent that they were delegated in the by-laws or in the resolution creating the committee. The 1969 amendments more specifically defined the scope of the power that may be delegated. This eliminated the possibility that there might be certain "fundamental" or "extraordinary" powers which are nondelegable. The statute now authorizes any committee, to the extent provided in the by-laws or in the board resolution creating the committee, to exercise all of the power and authority of the board, subject to two classes of exceptions. First, no committee may exercise the board's power with respect to amending the charter, adopting an agreement of merger or consolidation, recommending to stockholders the transfer of all or substantially all of the corporation's property, recommending to stockholders a dissolution or the revocation of a dissolution, or amending the by-laws. Second, a committee may declare dividends or authorize the issuance of stock only pursuant to an express delegation of these powers in the charter, by-laws or resolution creating the committee.⁸ Another amendment to section 141(c) reduced the minimum

and noticed or wherever held, are as valid as though had at a meeting duly held after regular call and notice, if a quorum is present and if, either before or after the meeting, each of the directors not present signs a written waiver of notice, a consent to holding the meeting, or an approval of the minutes thereof."

8. Compare Cal. Corps. Code § 822, which provides in part as follows:

"The by-laws may provide for the appointment by the board of directors of an executive committee and other committees and may authorize the board to delegate to the executive committee any of the powers and authority of the board in the management of the business and affairs of the corporation, except the power to declare dividends and to adopt, amend or repeal by-laws."

size of a committee of the board from two directors to one.⁹

The board is now expressly authorized to fix the compensation of directors, absent a restriction in the charter or by-laws.¹⁰

In the area of transactions involving common or interested directors or officers, the validation provisions were expanded so that a transaction which would otherwise be tainted is now validated if approved by the affirmative votes of a majority of the disinterested directors, even though the disinterested directors comprise less than a quorum.¹¹ Previously, approval was required by a vote sufficient for such purpose without counting the vote of interested directors. Furthermore, other amendments to section 144 make it clear that the entire section is applicable to both the common and the interested director situation.

The statute broadly authorizes corporations to keep their records (including stock ledgers, books of account, and minute books)¹² on any convenient information storage device, including devices utilized with computers. Section 224 was amended to provide that a "clearly legible written form produced" from the original record-keeping mechanism is admissible in evidence and shall be accepted for all other purposes to the same extent an original written record would have been, "when said written form accurately portrays the record." The statute had previously specified that the original form (e.g., cards, tapes, microphotographs, etc.) would be admissible.

9. The executive committee of a California corporation must be composed of two or more directors. Cal. Corps. Code § 822.

10. Compare Cal. Corps. Code § 501 (d), providing that the by-laws may make provision, not in conflict with law or the articles, for the compensation of directors.

11. Del. Corp. Law § 144; compare Cal. Corps. Code § 820, permitting common or interested directors to be counted in determining the presence of a quorum, but requiring action by a vote sufficient for the purpose with-

out counting the votes of such directors.

12. Compare Cal. Corps. Code §§ 3000-3004; in 1963, Cal. Corps. Code § 3002 was amended to permit the keeping of information required in the share register on "punchcards, magnetic tape, or other information storage device related to electronic data processing equipment provided that such card, tape, or other equipment is capable of reproducing the information in clearly legible form for the purposes of inspection as provided in Section 3003."

C. Stockholder Matters

Stockholder action by nonunanimous written consent was originally validated in the 1967 Delaware Code revision. This is in sharp contrast with the majority of other jurisdictions where stockholder action by written consent is permitted only if unanimous.¹³ Now, Delaware has gone even further to facilitate stockholder action by written consent. An amendment to section 228 authorizes such nonunanimous written consent (i.e., consent by the holders of stock having not less than the minimum number of votes that would be necessary to take such action at a meeting at which all shares entitled to vote thereon were present and voted) unless the charter provides otherwise. Previously, such action was permitted only if the charter affirmatively authorized it. Furthermore, notice of action by nonunanimous written consent need be given only to the nonconsenting stockholders. If action so taken results in a document required to be filed with the Secretary of State, such filing must contain appropriate recitals that the action was taken in conformity with the statute, and that written notice has been given to nonconsenting stockholders. A related provision¹⁴ specifies that the record date for expressing stockholder action by written consent is the day when the first consent is given, unless a record date is formally set under the statutory procedure therefor.

Several of the 1969 amendments directly concerned voting rights. With regard to cumulative voting, Delaware,¹⁵ unlike California,¹⁶ continues to make cumulative voting permissive rather than mandatory. Section 214 has been amended to make it clear that a charter provision conferring cumulative voting rights may specify that such privilege will be enjoyed by one or more classes or series within classes. Previously, the statute spoke only of "each holder of stock." This section was also amended to make clear that a stockholder having

¹³ Compare, e.g., Cal. Corps. Code § 2239.

¹⁴ Del. Corp. Law § 213; compare Cal. Corps. Code §§ 2214, 2215.

¹⁵ Del. Corp. Law § 214.

¹⁶ Cal. Corps. Code § 2235.

cumulative voting rights is entitled to the number of votes he would otherwise have, multiplied by the number of directors to be elected by him. The prior language, when read literally, did not fit the situation where a class that enjoyed cumulative voting rights was entitled to elect only part of the board.

Another amendment in this area concerned fractional and multiple voting. Before the 1969 amendments, a charter provision prescribing a deviation from the one-share-one-vote norm, at least as to election of directors, was permitted.¹⁷ It was not clear whether fractional or multiple voting was permissible as to other matters. Section 212(a) has been amended to provide that where the charter prescribes more or less than one vote for any share on any matter, all statutory references to “a majority or other proportion of stock shall refer to such majority or other proportion of the votes of such stock.”

Section 275, which sets forth the procedure for dissolution, now provides that a proposed dissolution requires the approval of a majority of the outstanding stock entitled to vote thereon; heretofore, the affirmative vote of two-thirds of the voting stock was required.¹⁸ Section 311, pertaining to the revocation of a voluntary dissolution, was amended to conform by permitting such revocation by the vote of a majority of the stock which was outstanding and entitled to vote on a dissolution at the time of dissolution.¹⁹ Furthermore, a new provision²⁰ authorizes dissolution, without meetings of directors or stockholders, upon the written consent of *all* stockholders entitled to vote on a dissolution.

Section 242 was amended to provide that if a proposed charter amendment would adversely affect less than all of the

17. Del. Corp. Law § 212; compare Cal. Corps. Code § 2215, which provides in part: “In the absence of any contrary provision in the articles or in any statute relating to the election of directors or to other particular matters, each [record shareholder] is entitled to one vote for each share.”

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18. Compare Cal. Corps. Code § 4600 (vote or written consent of “50 percent or more” of the voting power).

19. Compare Cal. Corps. Code § 4606 (vote or written consent of “not less than a majority” of the voting power).

20. Del. Corp. Law § 275(c).

series within a class of stock, then the class vote required to approve such action applies only to the series affected, rather than to the class as a whole.¹ Thus, affected stockholders are no longer lumped together with others who have no interest in the action proposed.

The Delaware statute, as revised in 1967, provided that unless extended in the prescribed manner, a voting trust or other stockholder voting agreement would be effective for a maximum period of 10 years. Section 218 was amended in 1969 to specify that the validity of a voting trust is not adversely affected during the 10-year period of validity, even though by its terms it purports to run beyond 10 years; the savings clause previously referred only to voting agreements.²

The 1967 revision reversed the pre-existing common law preemptive right by providing that in the absence of an express charter provision granting preemptive rights, no such rights would exist.³ It was intended that this change would operate prospectively without destroying existing preemptive rights. The 1969 amendments clarified this savings provision by expressly declaring that all preemptive rights in existence on July 3, 1967, the effective date of the 1967 revision, remain unaffected by section 102(b)(3), unless altered by appropriate action expressly making such alteration. Section 102(b)(3) was also amended to provide that preemptive rights might be granted as to a particular class or series, and to provide explicitly that preemptive rights to subscribe to a security convertible into a designated class or series do not exist unless the charter expressly grants such rights as to the convertible security.

1. Compare Cal. Corps. Code §§ 3632-3638.

2. Compare Cal. Corps. Code §§ 2230 and 2231, validating voting trusts for a period not greater than 21 years.

3. Compare Cal. Corps. Code § 305, permitting inclusion in the articles of provisions granting "preemptive rights

to subscribe to any or all issues of shares or securities," and Cal. Corps. Code § 1106, which provides as follows: "Unless the articles provide otherwise, the board of directors may issue shares, option rights, or securities having conversion or option rights, without first offering them to shareholders of any class."

D. *Miscellaneous*

New section 103(f) validates the existing administrative practice in the office of the Delaware Secretary of State by which a corporation may correct a previously filed inaccurate or defective instrument. The statute now expressly authorizes the filing of a certificate of correction which specifies the inaccuracy or defect to be corrected and sets forth the portion of the instrument in corrected form. The corrected instrument is made retroactively effective as of the date of the filing of the original instrument, except for preserving the interests of those "substantially and adversely affected by the correction," as to whom it is effective as of the filing of the certificate of correction.

The restrictions on name use which have heretofore been applicable to businesses incorporated in Delaware have now been made applicable to foreign corporations. Section 371 (c) was amended to prohibit the issuance to a foreign corporation of a certificate stating that it has filed its charter with the Delaware Secretary of State, unless the foreign corporation's name is such as to distinguish it from the names of corporations organized in Delaware and the names of other foreign corporations reserved or registered with the Secretary of State (unless the other corporation consents).⁴

Not unexpectedly, Section 391 was amended to increase various fees to be charged by the Secretary of State.

Finally, in 1969, the Delaware legislature enacted a Professional Service Corporation Act which, generally speaking, permits the incorporation of individuals or groups engaged in licensed professions.⁵

The net effect of the 1969 amendments was to make Dela-

4. Compare Cal. Corps. Code § 6404.

5. Ch. 6, tit. 8, Del. Code, enacted by House Bill No. 106, approved and effective June 7, 1969. In California, the Moscone-Knox Professional Corporation Act, Cal. Corps. Code §§ 13400-13410, which became effective November 13, 1968, authorized the

formation of professional corporations for the rendering of professional services by lawyers, doctors, osteopaths, podiatrists and dentists. In 1969, this privilege was extended to certified psychologists under § 2995 of the California Business and Professions Code.

ware corporation law an even better tool for corporate management, and to require even more care than before in the drafting of charter and by-law provisions for Delaware corporations.