McGeorge Law Review

Volume 7 | Issue 2 Article 8

7-1-1976

California's New General Corporation Law: Prospects for Minority Shareholders

Ann H. Morris
University of the Pacific; McGeorge School of Law

California's New General Corporation Law: Prospects For Minority Shareholders

California has long been recognized as a jurisdiction having laws which tend to favor the corporate shareholder and creditor, sometimes at the expense of corporate management. One commentator wrote of the Old California Corporations Code:[1] "In a nutshell, what the . . . Code seeks to embody is an appreciation of the important role of shareholders and creditors in any prosperous business community."[2]

In addition to benefiting from statutory provisions which have been particularly protective of minority shareholders, such investors have been afforded a degree of protection through decisions of the California courts, as illustrated by the landmark case of *Jones v. Ahmanson*,[3] which expanded the traditional rules of fiduciary duties owed from majority to minority shareholders.[4] This case involved majority shareholders who formed a holding company to enhance the marketability of closely-held, high value stock.[5] The minority shareholders were excluded from the holding company, and as a result, were effectively deprived of a market for their shares.[6] Under the traditional approach, the court would have denied a cause of action to the minority plaintiffs who had

1. CAL. CORP. CODE §§100-35302, *enacted*, CAL. STATS. 1947, c. 1038 (*effective until January 1, 1977*) [hereinafter all citations and references to the General Corporation Law as enacted in 1947 will be cited as or referred to as CAL. CORP. CODE or Old Code].

2. Jennings, *The Role of the States in Corporate Regulation and Investor Protection*, 23 LAW & CONTEMP. PROB. 193, 199 (1958) [hereinafter cited as Jennings]. *See also* Comment, *Choice of Corporate Domicile*, 49 CAL. L. REV. 518, 519 (1961), citing California as "one of the leading states in the protection of security holder and public interests."

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

4. 6 B. WITKIN, SUMMARY OF CALIFORNIA LAW, *Corporations*, §§164-65 (8th ed. 1974) [hereinafter cited as 6 WITKIN, *Corporations*].

5. 1 Cal. 3d at 102, 460 P.2d at 466, 81 Cal. Rptr. at 594.

6. *Id.* at 103, 460 P.2d at 467, 81 Cal. Rptr. at 595.

asserted breach of fiduciary duty as the basis of their lawsuit, because fiduciary obligations of majority to minority attached only to sale of control or sale of assets situations.[7] However, the California court noted that

> [t]he increasingly complex transactions of the business and financial communities demonstrate the inadequacy of the traditional theories of fiduciary obligation as tests of majority shareholder responsibility to the minority. These theories have failed to afford adequate protection to minority shareholders and particularly to those in closely held corporations whose disadvantageous and often precarious position renders them particularly vulnerable to the vagaries of the majority.[8]

Although cases subsequent to the *Jones* decision have continued to assume this protective posture,[9] there are reasons to believe the trend may have been arrested or at least slowed by the adoption of the New General Corporation Law to be effective January 1, 1977.[10] Although many shareholder protections embodied in the Old Code[11] do remain in the New Code—indeed, there are areas of increased protection for shareholders—there are many respects in which the California minority shareholder appears to have lost ground and may be increasingly susceptible to management or majority oppression.

The purpose of this comment is to assess the status of the minority shareholder[12] in California and to evaluate the prospects for minority protection under the New Corporations Code. The comment attempts

---

7. 6 WITKIN, *Corporations, supra* note 4, §164-65. See also text accompanying note 112 (sale of assets) and note 231 (sale of control) *infra.*

8. 1 Cal. 3d at 111, 460 P.2d at 464, 81 Cal. Rptr. at 592, *quoted in* 6 WITKIN, *Corporations, supra* note 4, §165. *See also* In re Security Finance, 49 Cal. 2d 370, 317 P.2d 1 (1957) (a breach of the majority's duty to the minority in a dissolution setting where the majority induced the dissolution, purchased the assets of the dissolving corporation, then resumed business without the minority shareholders); Remillard Brick v. Remillard-Dandini Co., 109 Cal. App. 2d 405, 241 P.2d 66 (1952) (dominant shareholders breached their duty by transferring corporate business to their own separate corporation).

9. *See, e.g.*, Rankin v. Frebank Co., 47 Cal. App. 3d 75, 121 Cal. Rptr. 348 (1975); DeBaun v. First W. Bank & Trust Co., 46 Cal. App. 3d 686, 120 Cal. Rptr. 354 (1975).

10. CAL. STATS. 1975, c. 682 (*effective January 1, 1977*) [hereinafter all citations and references to the New General Corporation Law, *enacted*, CAL. STATS. 1975, c. 682, will be cited as or referred to as *New* CAL. CORP. CODE or New Code] *See generally* REVIEW OF SELECTED 1975 CALIFORNIA LEGISLATION, this volume at 258 (General Corporation Law).

11. See note 1 *supra.*

12. The term "minority shareholder" generally connotes an absence of control over corporate affairs. Theoretically a minority shareholder would be anyone with holdings of less than 50 percent of the outstanding stock of a corporation. However, there are many instances where a holder of less than half the stock nonetheless effectively controls the corporation, or at least has a substantial role in its management. *See* Andrews, *The Stockholder's Right to Equal Opportunity in the Sale of Shares*, 78 HARV. L. REV. 505, 506 (1965).

to catalogue various major concerns for minority shareholders, with particular emphasis upon methods by which the minority may be "squeezed-out"[13] or oppressed[14] by a self-serving majority. In some of the areas to be examined, the New Code does not change the minority shareholder's status. Nonetheless, these areas will be discussed in an effort to present a well-rounded picture of the minority shareholder's status in California. Although previous works have covered the spectrum of concerns for minority shareholders exhaustively,[15] none have focused on the California shareholder in particular.

The following areas will be examined with respect to the California minority shareholder: dividends, corporate employment and salaries, fundamental corporate changes, issuance of stock and preemptive rights, voting rights, meeting and quorum requirements, sale of corporate control, and shareholder suits. Each of these concerns will be evaluated regarding its potential for harming the minority shareholder, and the likelihood of such harms occurring will be assessed in light of the New Corporations Code and California case law. This discussion will be followed by a summary of the emerging status of the minority shareholder, and by some observations as to how the courts are likely to treat minority shareholders under the new statutory provisions which will alter several protective measures in favor of "majoritarianism"[16] policies.

In assessing the minority shareholder's status, it is important to keep in mind the delicate balance between corporate management interests and shareholder protections. In the past, California lawmakers have sought to make California corporate law

> liberal enough to facilitate business transactions without undue formalities of checks and balances, of votes and consents of shareholders, and applicants to courts, and at the same time not so lax that the management or the majority may manipulate the ma-

13. " 'Squeeze-out' means the elimination of one or more shareholders of a business by those who control it, through the use of their powers of control, inside information, or other technique without fair value being paid in return." O'Neal and Janke, *Utilizing Rule 10b-5 for Remedying Squeeze-Outs or Oppression of Minority Shareholders*, 16 B.C. IND. & COM. L. REV. 327 (1975) [hereinafter cited as O'Neal & Janke].

14. "Oppression" in the corporate context refers to conduct of directors or others in control which is" 'burdensome, harsh and wrongful conduct;' . . . '[lacking] probity and fair dealing in affairs of a company to the prejudice of some of its members;' or 'a visible departure from the standards of fair dealings, and a violation of fair play on which every shareholder who entrusts his money to a company is entitled to rely.' " Comment, *Oppression as a Statutory Ground For Corporate Dissolution*, 1965 DUKE L.J. 128, 134 (1965) (citations omitted).

15. *See, e.g.*, F. O'NEAL & J. DERWIN, EXPULSION OR OPPRESSION OF BUSINESS ASSOCIATIONS: "SQUEEZE-OUTS" IN SMALL ENTERPRISES (1961) [hereinafter cited as O'NEAL & DERWIN]; Note, *Freezing Out Minority Shareholders*, 74 HARV. L. REV. 1630 (1961); Symposium: *The Close Corporation*, 52 NW. U.L. REV. 384, 391-92 (1957). *See also* O'Neal & Janke, *supra* note 13.

16. See text accompanying notes 75, 160, and 200 *infra*.

> chinery to the prejudice of creditors or investors or the oppression of minority shareholders.[17]

Management oriented critics imply that this balance has not been achieved and that protective codes such as California's unduly inhibit management.[18] As a result, out-of-state incorporation is a prevalent phenomenon in California.[19] However, with the adoption of the New Code, it might be argued that the shift toward a stronger management orientation detectable in the New Code may make California a more attractive state for future incorporation.

As an added note of introduction, Chapter 21 of the New Corporations Code will more broadly extend California substantive law to quasi-foreign corporations.[20] Thus, certain corporations which are incorporated outside California will be subjected for the first time to many provisions of California law. It may well be this expanded out-of-state impact of the New Code which motivated the move toward a management orientation, as absent such a policy shift, one could speculate that out-of-state corporations might be discouraged from doing substantial business in California.[21]

DIVIDENDS

For the minority shareholder, dividends may be the only source of income realized as a result of his investment, and thus a failure of the corporation to declare dividends may seriously jeopardize a minority shareholder's ability to maintain his investment.[22] This is a concern of

---

17. Jennings, *supra* note 2, at 199.

18. *See, e.g.*, Comment, *Choice of a Corporate Domicile*, 49 CAL. L. REV. 518, 524 (1961) (the protective cumulative vote concept is attacked as "tend[ing] to make management overly conservative and unwilling to take necessary risks"). *See generally* Cary, *Federalism and Corporate Law: Reflections Upon Delaware*, 83 YALE L.J. 663, 664 (1974) [hereinafter cited as Cary].

19. See Comment, *California's New Corporation General Law: Quasi-Foreign Corporations*, this volume at 673.

20. Under the New Corporations Code Section 2115, quasi-foreign corporations are subject to the following provisions: *New* CAL. CORP. CODE §§301 (annual election of directors), 303 (removal of directors without cause), 304 (removal of directors by court proceedings), 305(c) (filling of director vacancies where less than a majority in office have been elected by shareholders), 309 (directors' standard of care), 316 excluding subdivisions (a)(3) and (f)(3) (liability of directors for unlawful distributions), 317 (indemnification of directors, officers and others), 500-505 (limitations on corporate distributions in cash or property), 506 (liability of shareholders who receive unlawful distributions), 600(b) and (c) (requirement for annual shareholders' meeting and remedy if same not timely held), 708(a), (b), and (c) (shareholders' right to cumulate votes any election of directors), 1200-1201 (reorganizations), 1300-1312 (dissenters' rights), 1500-1501 (records and reports), and 1600-1605 (rights of inspection).

21. For a discussion of what constitutes "substantial business," see Comment, *California's New General Corporation Law: Quasi-Foreign Corporations*, this volume at 673.

22. *See generally* O'NEAL & DERWIN, *supra* note 15, at 45-52. For a general discussion of the New Code's dividend provision see Comment, *California's New General Corporation Law: Dividends and Reacquisitions of Shares*, this volume at 645.

particular importance to the holder of shares in a very small or a closely-held corporation where the investment per shareholder may be substantial.[23] For the majority shareholder, the impact of withheld dividends may not be as substantial, particularly in a small corporation in which majority shareholders often are corporate employees and can withdraw corporate profits by way of salary payments rather than dividend payments, which would be subject to double taxation.[24]

One reason that the board of directors may withhold dividends might be to silence a dissident voice by forcing a minority shareholder to sell his shares. If the withholding of dividends is timed to coincide with known financial hardship of a minority shareholder, the majority shareholders may not only be able to force a minority holder to sell, but also may be able to obtain the minority shares at a bargain price.[25]

Faced with a situation of withheld dividends, the shareholder may be able to compel declaration of a dividend if he can show it has been wrongfully withheld. This is, however, a judicial remedy which is difficult to obtain. In addition to meeting the security-for-expense requirements,[26] the moving shareholder has the burden of showing fraud,[27] bad faith, or clear abuse of discretion[28] on the part of directors failing to declare dividends. This burden may be difficult to overcome, for the courts are reluctant to interfere with the "business judgment" aspects of corporate affairs.[29] Thus,

> [t]he mere fact that a corporation has surplus profits out of which a dividend might lawfully be declared is not of itself sufficient ground for the court . . . to compel . . . a dividend . . ., unless there is a clear abuse of discretion, or the action taken by the directors is unreasonable *and oppressive.*[30]

To establish an action as unreasonable or oppressive a shareholder must establish the amount of corporate earnings, the amount of capital required for operation and expansion (an area of much discretion for the

23. Elson, *Shareholders Agreements, A Shield for Minority Shareholders of Close Corporations,* 22 BUS. LAWYER 449, 451 (1967).

24. See text accompanying note 55 *infra.*

25. O'NEAL & DERWIN, *supra* note 15, at 45.

26. See text accompanying note 267, *infra.* There is a split of authority as to whether the compulsory dividend action is derivative or individual. 11 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS, §5326.1 (perm. ed. rev. 1971) [hereinafter cited as 11 FLETCHER]. Security for expense statutes generally apply only to derivative actions. *See* Comment, *Due Process and Security for Expense Statutes,* this volume at 176, 182.

27. 13 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS, §5829 (perm. ed. rev. 1970) [hereinafter cited as 13 FLETCHER].

28. 11 FLETCHER, *supra* note 26, at §5325.

29. *Id. See also* Comment, *California's New General Corporation Law: Directors' Liability to Corporations,* this volume at 613, 622-23, 626-27 (the business judgment rule).

30. 11 FLETCHER, *supra* note 26, at §5325 (emphasis added).

directors[31]), why there has been no dividend declaration, *and* a breach of fiduciary duty.[32]

The cases of *Zellerbach v. Allenburg*[33] and *Estate of Talbot*[34] illustrate the California courts' continued treatment of this issue as one within the parameters of the business judgment rule. In *Zellerbach*, a plaintiff who was indebted to the defendant corporation alleged that defendant fraudulently failed to declare and credit dividends against the debt.[35] The court stated:

> [T]he rule as to declaring dividends is that the apportionments of the net earnings to the payment of cash dividends . . . is largely one of policy, intrusted to the discretion of directors, which when honestly and intelligently exercised, will not be lightly overruled.[36]

Finding no fraud, the court denied petitioner's claim to compel a dividend.[37]

Estate of Talbot, a case in which the court was faced with the question of whether a corporate distribution was principal or income for trust purposes,[38] further illustrates the significance the California courts will afford to business discretion in the dividend setting. Because the distribution was made pursuant to a federal court decree compelling partial liquidation, the *Talbot* court characterized the distribution as involuntary, and hence principal rather than income.[39] In essence, the court refused to characterize the distribution as a dividend *because it had not been made by the board in the exercise of its "sound business judgment."*[40]

Chapter Five of the New California Corporations Code will control the distribution of corporate funds.[41] Section 500[42] sets out what the

---

31. O'NEAL & DERWIN, *supra* note 15, at 46.
32. *Id.* at 46, 50. To further illustrate the degree of discretion involved in assessing the adequacy of corporate funds, the courts consider: the amount of surplus, the ratio of current assets to current liabilities, working capital requirements, working capital retained in prior years, business prospects, the corporation's need for expansion, and present and future liabilities. *Id.* at 50.
33. 99 Cal. 57, 33 P. 786 (1893).
34. 269 Cal. App. 2d 526, 74 Cal. Rptr. 920 (1969).
35. 99 Cal. at 69, 73, 33 P. at 790-91.
36. 99 Cal. at 70-71, 33 P. at 790, *quoting* Mining Co. v. Pierce, 90 Cal. 131, 145-46, 27 P. 44, 47 (1891) (citations omitted).
37. 99 Cal. at 71, 33 P. at 790.
38. 269 Cal. App. 2d at 529, 74 Cal. Rptr. at 922.
39. *Id.* at 537, 74 Cal. Rptr. at 927.
40. *Id.* (emphasis added).
41. For a full discussion of CAL. CORP. CODE §1500 et. seq. which controls the distribution of dividends under the Old Code, *see* Comment, *California's New General Corporation Law: Dividends and Reacquisitions of Shares*, this volume at 645.
42. *New* CAL. CORP. CODE, §500 provides, *inter alia*:

> Neither a corporation nor any of its subsidiaries shall make a distribution to the corporation's shareholders . . . unless:
> (a) The amount of retained earnings . . . equals or exceeds the amount of the proposed distribution; or

drafters of the New Code call a "balance sheet" or "solvency" approach, which is to replace the "stated capital" and "surplus" approaches of the former law.[43] This provision, which the drafters of the New Code added "[f]or the purpose of establishing meaningful protection for creditors and shareholders . . . ,"[44] may eliminate one method of oppressing the minority insofar as it will prevent the declaration of "whopping" dividends which may deplete corporate assets.[45] Thus, the shareholder seeking dividends as a return on his investment would, under the new law, seem to be protected in the sense that any declared dividend would not jeopardize his basic investment. However, he would still face the obstacles presented by the business judgment rule in any action to compel a dividend.[46]

There are, in addition to the suit to compel dividends, other possible remedies for the shareholder who is not receiving dividends. Sections 531 through 537 of the Internal Revenue Code[47] impose penalties upon the unreasonable accumulation of earnings. The possibility of a tax penalty may serve to keep the directors in a fair dividend-declaring posture, or may arm the shareholder with an effective weapon. For example, the shareholder may be able to compel a dividend by threatening a report to the IRS, and evidence of a previously imposed tax penalty may bolster a shareholder's case in a suit to compel the dividend.

Another possibility for the deprived shareholder may be an action in federal courts, relying on Section 10(b) of the Securities and Exchange Act of 1934[48] and its implementing Rule 10b-5.[49] To illustrate,

---

(b) . . . [after the distribution]:
(1) The sum of the assets . . . would be at least equal to 1¼ times its liabilities . . . , and
(2) The current assets would be at least equal to its current liabilities or, if the average earnings . . . before taxes . . . and before interest expense for the two preceding fiscal years was less than the average of the interest expense . . . for such fiscal years, at least equal to 1¼ times its current liabilities . . . .

43. CALIFORNIA LEGISLATURE, ASSEMBLY SELECT COMMITTEE ON THE REVISION OF THE CORPORATIONS CODE, REPORT OF THE ASSEMBLY SELECT COMMITTEE ON THE REVISION OF THE CORPORATIONS CODE 72 (1975) [hereinafter cited as ASSEMBLY REPORT].

44. *Id.*

45. *See* O'NEAL & DERWIN, *supra* note 15, at 135; *see also* 11 FLETCHER, *supra* note 26, at §5325.

46. See text accompanying note 52 *infra.*

47. INT. REV. CODE OF 1954, §§531-37. *See also* O'NEAL & DERWIN, *supra* note 15, at 52.

48. Securities Exchange Act, 15 U.S.C. §78*j*(b) (1934). That Act provides:
It shall be unlawful for any person . . .
(b) To use or employ, in connection with the purchase or sale of any security registered on a national securities exchange or any security not so registered, any manipulative or deceptive device or contrivance in contravention of such rules as the Commission may prescribe. . . .
See also O'Neal & Janke, *supra* note 13, at 335.

49. 17 C.F.R. §240.10b-5 (1951). This regulation, which implements §10(b) of the Securities Exchange Act of 1934, *supra* note 48, provides:

where a board of directors fails to declare a dividend in hopes of forcing a dissident minority to sell his shares, there may well be a "fraud . . . in connection with . . . the sale of securities" sufficient to invoke the Rule 10b-5 remedy.[50]

Finally, a shareholder could seek to prospectively control dividends through a charter or bylaw provision specifying the conditions under which dividends will be mandatorily distributed.[51] In California, however, it is not certain whether dividends can be so controlled in the absence of a shareholders' agreement under Section 300(b) of the New Code. Though Section 505 of the New Code states that "[n]othing in this chapter prohibits *additional restrictions* upon the declaration of dividends . . . by provision in the articles or bylaws . . . ," there is no such specific grant of authority to *compel* distributions through the articles or bylaws.

To summarize, under the Old Corporations Code, the California minority shareholder is in a position similar to shareholders in other states with respect to dividends. He can be denied dividends in any situation short of fraud or clear abuse of discretion, and the California courts recognize the sanctity of business judgment in the dividend decision. In one sense, however, the New Code might offer some additional protection to the California shareholder by abandoning the balance sheet approach in favor of a basic solvency limitation, thereby minimizing the possibility of excessive dividends. The extent to which shareholders will be able to control dividends through bylaw provisions is unclear, as Section 505 of the New Code implies that *restrictions* on dividends may be placed in the bylaws, but the section is silent as to provisions which would *compel* dividends. Thus, it is difficult to ferret

---

> It shall be unlawful *for any person*, directly or indirectly, by use of *any* means or instrumentality of interstate commerce, or of the mails or of any facility of any national securities exchange,
> (a) to employ any device, scheme, or artifice to defraud,
> (b) To make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading, or
> (c) To engage in *any act*, practice or course of business which operates or would operate as a fraud or deceit *upon any person, in connection with the purchase or sale of any security* [emphasis added].

50. *See generally* Greenstein v. Paul, 400 F.2d 580 (2nd Cir. 1968) wherein the plaintiff, charging a violation of §10(b) of the Securities Exchange Act of 1934 and Rule 10b-5 of the Securities and Exchange Commission, was held to lack standing as he had not purchased or sold stock during or after the alleged fraud. Nonetheless, the court implied that but for the standing problem, a §10(b) violation might have occurred where defendant corporate officers manipulated the market value of the stock so as to be able to purchase the shares of minority stockholders at depressed prices and effectuate their "freeze-out." Under recent Supreme Court decisions, it appears that the shareholder would be unable to invoke Rule 10b-5 in the absence of an actual sale of shares. *See, e.g.*, Blue Chip Stamps v. Manor Drug Stores, 421 U.S. 723 (1975).

51. 11 FLETCHER, *supra* note 26, at §5325.

out a single conclusion regarding the minority shareholder and corporate dividends. In some circumstances he is protected from majority abuse; in other situations he appears vulnerable.[52] This vulnerability may, moreover, take on added significance when the denial of dividends is considered in conjunction with the problem of excessive corporate salaries.

CORPORATE EMPLOYMENT AND SALARIES

In many cases majority shareholders are offered corporate employment, especially in smaller or closely-held corporations. Additionally, the articles may allow directors, who are often majority shareholders, to provide for their own compensation in their roles as directors.[53] On the other hand, there is little a minority shareholder can do to compel his employment by the corporation, as such decisions are made by the board of directors or the officers selected by the board.[54] Where majority shareholders are employed by the corporation and minority shareholders are not, the former can compensate for loss of dividends (if none are declared, or if minimal dividends are declared) by drawing substantial salaries and favorable employee benefits in the form of bonuses and expense accounts.[55]

A minority shareholder may sue derivatively to recover excessive salaries, under a corporate waste theory.[56] However such recovery is difficult to effect, as the courts have not established definite rules of what constitutes reasonable compensation. As in the case of dividends, the issue is largely one of "business judgment" for the directors.[57] As might be expected, the relevant factors leave considerable leeway for the court. Thus executive ability, quantity of work and quality of services, time devoted, difficulty of work, success and profits realized, general corporate financial condition, and relative value of other corporate salaries are all deemed relevant to fixing and assessing a reasonable salary.[58] Therefore, it would seem that the likelihood of success of a

52. See text accompanying note 46 *supra*.
53. CAL. CORP. CODE §820; *New* CAL. CORP. CODE §310.
54. Even where a minority shareholder is able to secure employment or corporate office, the majority, acting through the board of directors, may be able to remove the minority shareholder from his position with or without cause. In California, removal without cause is available at the end of a term in office or upon removal of the *entire* board. CAL. CORP. CODE §810; *New* CAL. CORP. CODE §303. There may be a shareholder's derivative action available to the minority for misuse of corporate funds if the corporation is forced to pay damages for breach of an employment contract where removal was without cause. O'NEAL & DERWIN, *supra* note 15, at 53 n.47.
55. O'NEAL & DERWIN, *supra* note 15, at 45.
56. *Id.* at 54-55.
57. *Id.* at 59.
58. *Id.*

minority suit to recover excessive salaries is slim.[59] However, in the extreme cases resulting in oppression of the minority, recovery may be had. For example, a recent California case supported recovery of a salary paid a controlling shareholder-employee who had diverted substantial corporate business to a second corporation from which he also drew a salary.[60]

As an alternative to the suit to recover an excessive salary, a viable solution might be for the shareholder to simply sell his shares and invest elsewhere. In this regard, it is important whether the stock of the corporation is closely or publicly held.[61] Not only does the holder of public stock have a ready market which is generally not available to the close corporation shareholder, but the marketability of closely-held stock may be additionally impaired where there is a detrimental situation known to potential investors.[62] Further, the shareholders may be faced with "first option" transfer restrictions, which are often utilized in the close corporation setting.

Neither the Old nor the New Corporations Code offers specific protection to the minority shareholder being victimized by excessive corporate salaries. However, the fiduciary duty obligations of directors under Section 820 of the Old Code and the expanded provisions of Section 309 of the New Code offer limited protection. Given the latitude of the business judgment rule,[63] however, these provisions do not appear to offer significant protection to the minority shareholder in this regard.

Fundamental Corporate Changes

Fundamental corporate changes are those which substantially alter the nature of a shareholder's investment.[64] Such changes may be effected by certain types of article amendments, share redemptions,

---

59. *See, e.g.*, United States v. Byrum, 408 U.S. 125, 150 (1971), where the Court, though recognizing that a controlling shareholder must have some constraints placed on his ability to control his own salary, was willing to defer to the Internal Revenue Service to police the matter through disallowances of unreasonable compensation as a legitimate business expense.

60. Rankin v. Frebank, 47 Cal. App. 3d 75, 86, 121 Cal. Rptr. 348, 355 (1975). As the statute of limitations had run, the *Rankin* court did not allow recovery of the salary; however, the court indicated that but for this defect the plaintiffs could have retrieved the excessive salaries.

61. Fales, *Judicial Attitudes Toward the Rights of Minority Stockholders*, 22 Bus. Lawyer 459, 466 (1967). *See generally* Berger, *California's New General Corporation Law: Close and Closely-Held Corporations*, this volume at 585.

62. Since Rule 10b-5, which is applicable upon any use of an instrumentality of interstate commerce, see note 49 *supra*, requires disclosure of material facts relative to the transaction, a shareholder seeking to sell his shares arguably may be susceptible to liability for failing to apprise a potential buyer of the excessive salaries paid to management.

63. See text accompanying notes 29-40 and 57 *supra*.

64. *See generally* O'Neal & Derwin, *supra* note 15, at 61.

mergers, consolidations, and dissolutions. In each of these areas the New Code alters the protections which are afforded to the minority shareholders.

A. *Changes Affecting Shares*

Corporations may by article amendment seek to exchange,[65] classify or reclassify[66] the corporation's outstanding shares. For example, the result may be to eliminate preferences or to alter existing voting rights held by minority stockholders.[67] Limited protection for the affected shareholder may be found in statutes requiring shareholder approval of any such article change. Under Section 3634 of the Old Code and Section 903(a) of the New Code, some protection is provided insofar as any proposed fundamental amendment to the articles must be approved by the outstanding shares of the affected class, whether or not such class is otherwise entitled to vote.[68] Such a fundamental amendment must also be approved by the outstanding voting shares.[69] Under the New Code, requirement for approval is a *majority* of the affected shareholders and a *majority* of the outstanding shares entitled to vote,[70] unless a higher, or "supermajority,"[71] vote is provided for in the articles.[72] Section 3634 of the Old Code, however, requires at least a *two-thirds* vote to approve article amendments adversely affecting shares.[73] Hence, in the case of any fundamental amendment which could adversely affect

---

65. An exchange involves trading one security for a different security or for other property or rights. BLACK'S LAW DICTIONARY 671 (Rev. 4th ed., 1968).

66. To classify stock is to group the stock and assign different rights, limitations and preferences to the classes. *See* H. HENN, LAW OF CORPORATIONS 207 (2d ed. 1970) [hereinafter cited as HENN].

67. *See generally* O'NEAL & DERWIN, *supra* note 15, at 61-78.

68. *New* CAL. CORP. CODE §903 (emphasis added). This section applies if the amendment would:

> (1) Increase or decrease the aggregate number of authorized shares of such class. . . .
> (2) Effect an exchange, reclassification or cancellation of all or part of the shares of such class. . . .
> (3) Effect an exchange, or create a right of exchange, of all or part of the shares of another class into shares of such class.
> (4) Change the rights, preferences, privileges or restrictions of the shares of such class.
> (5) Create a new class . . . , or increase the rights, preferences or privileges or the number of authorized shares of any class having rights, preferences or privileges prior to the shares of each class.
> (6) In the case of preferred shares, divide the shares . . . into series having different rights. . . .
> (7) Cancel or otherwise affect dividends . . . accrued . . . but . . . not . . . paid.

69. *New* CAL. CORP. CODE §153.

70. *New* CAL. CORP. CODE §152.

71. "Supermajority" is a phrase describing any vote requiring more than a simple majority to carry the motion. *See* ASSEMBLY REPORT, *supra* note 43, at 5.

72. *New* CAL. CORP. CODE §204(a)(5).

73. CAL. CORP. CODE §3634.

his interests, the minority shareholder appears to have lost ground under the New Code.[74] The draftsmen of the New Code explain the change as "consistent with a general policy of the new law requiring a majority vote for the approval of corporate acts."[75] As will be shown, this new general policy could have broad implications for California minority shareholders in the future.

B. *Share Redemption*

Redemption[76] of outstanding shares may be used as a mechanism for ousting minority shareholders, particularly where the minority's shares aggregate within redeemable classes.[77] For example, if the corporation has 10,000 total shares outstanding, 7000 of these common and 3000 redeemable preferred, the corporation could recall the preferred stock, leaving only 7000 common shares outstanding. If the minority's shares are all preferred, the recall could eliminate the minority shareholders entirely.

Under the New Code, conditions may be contained in the articles which will trigger the redemption,[78] or the redemption may be exercised at the option of the corporation,[79] although not at the option of the shareholder.[80] Pursuant to Section 509 of the New Code, the corporation may redeem *any or all* of the shares subject to redemption. It would appear, therefore, that the board of directors could selectively reacquire the redeemable shares of minority shareholders and leave any redeemable shares of majority shareholders outstanding. Moreover, Section 510 of the New Code allows the reissuance of the reacquired shares, unless such action is precluded by the articles. Thus, the corporation could redeem the stock from certain shareholders and resell the stock to other persons to replenish the corporate funds used in the redemption.

Under the new redemption scheme, however, the California minority

74. This lowered vote requirement may be one of the most significant losses for minority shareholders under the new code. For further discussion, see text accompanying note 200 *infra*.

75. ASSEMBLY REPORT, *supra* note 43, at 58.

76. Redemption typically involves a corporation's reacquisition of shares by paying the holder the book value or other agreed upon redemption price. *See* HENN, *supra* note 66, at 287. For a discussion of California's new treatment of redemption, see text accompanying notes 56-66 *infra*.

77. O'NEAL & DERWIN, *supra* note 15, at 64.

78. *New* CAL. CORP. CODE §402(a). To illustrate, a redemption provision may be desirable as a less drastic alternative than dissolution in the event of deadlock. *See* Elson, *Shareholder's Agreements, A Shield for Minority Shareholders of Close Corporations*, 22 BUS. LAWYER 449, 454 (1967). No equivalent section appears in the Old CAL. CORP. CODE.

79. CAL. CORP. CODE §1101, *New* CAL. CORP. CODE §509.

80. CAL. CORP. CODE §1101, *New* CAL. CORP. CODE §402(a), (b).

shareholder is not entirely without protection. Redeemable shares must be clearly identified as such on the share certificate,[81] and thus a shareholder is on notice that he is subject to foreclosure. Further, Section 505 of the New Code states that "[n]othing in this chapter prohibits additional restrictions upon . . . redemption of a corporation's own shares . . . by provision in the articles or bylaws . . . ." This section could be construed to permit an article or bylaw requiring the affirmative vote of the affected shareholders prior to the redemption. Since such an approval requirement would not conflict with any provision of the New Code, it would seem to be a viable option.[82]

Of course, a shareholder suit would lie if the redemption scheme were fraudulent or in breach of the fiduciary duty of the directors.[83] Thus, if such a scheme were used *solely* as a device for expelling certain shareholders, there may be relief. If, however, the directors could show that eliminating the minority was in the corporation's interest, there would be no recovery and no protection.[84] When a shareholder has insufficient facts to prevail in a shareholder suit based on fraud or fiduciary breach of duty, he may still have a recourse through the federal courts for a Rule 10b-5 violation,[85] where a lesser degree of proof is required than in actions based on common law fraud.[86] Although no case was discovered calling for such an application of Rule 10b-5, a redemption situation can easily be conceived which would constitute fraud in the *purchase* or sale of shares, hence triggering the application of Rule 10b-5. Although faced with a distinguishable set of facts in *Superintendent of Insurance v. Bankers Life & Casualty Co.*,[87] the Court noted with approval:

---

81. CAL. CORP. CODE §2403(a), *New* CAL. CORP. CODE §418(a)(4).

82. *New* CAL. CORP. CODE §§204(d) (allowing articles not in conflict with statute), 212(b) (allowing bylaws not in conflict with articles or statute).

83. 13 FLETCHER, *supra* note 27, at §5829.

84. *E.g.*, Matteson v. Ziebarth, 40 Wash. 2d 286, 242 P.2d 1025 (1952), wherein a merger plan involved issuance of redeemable stock, thereby eliminating a dissenting stockholder. The court found the merger essential to corporate survival, and hence held the resulting squeeze-out justifiable. *But see* Theis v. Spokane Falls Gas Light Co., 34 Wash. 23, 74 P. 1004 (1904), where an attempted dissolution and transfer of assets, not for a bona fide business reason, but for the *sole* purpose of eliminating a disagreeable stockholder, was set aside by the court as fraudulent.

In California, shareholder approval is required for any reorganization in which holders receive shares of the surviving corporation having different rights, preferences, privileges or restrictions than those surrendered. *New* CAL. CORP. CODE §1201(d). However, the minority will not generally be able to control the reorganization because absent an article or bylaw provision requiring a "supermajority" vote, see note 71 *supra*, a mere majority may cause the transaction to occur. All dissenting shareholders, however, will have dissenter's rights pursuant to Chapter 13 of the New Code. See text accompanying note 245 *infra*, for a further discussion of dissenter's rights.

85. See note 49 *supra*.

86. Susman, *Use of Rule 10b-5 as a Remedy for Minority Shareholders of Close Corporations*, 22 BUS. LAWYER 1193, 1198 (1967).

87. 404 U.S. 6 (1971).

> "[We do not] think it sound to dismiss a complaint merely because the alleged scheme does not involve the type of fraud that is 'usually associated with the sale or purchase of securities.' We believe that § 10(b) and Rule 10b-5 prohibit *all* fraudulent schemes in connection with the purchase or sale of securities . . . ."[88]

Therefore, in light of expanding federal protection through the liberal application of Rule 10b-5, the California minority shareholder may have an adequate alternative to offset the New Code's decreased protection regarding the redemption and reissuance of corporate shares.

C. *Changes in Corporate Structure*

The corporate structure may be significantly affected in several ways, including merger, consolidation, short-merger,[89] or de facto merger.[90] In distinguishing between the concepts of merger and consolidation, a California court noted:

> Strictly speaking, a consolidation signifies such a union as necessarily results in the creation of a new corporation and the termination of the constituents whereas a merger signifies the "absorption of one corporation by another which retains its name and corporate identity with the added capital, franchises and powers of a merged corporation."[91]

Although this distinction was made as late as 1975, the New Code eliminates consolidation as an "outmoded" method of effecting corporate change.[92]

Corporate merger may substantially affect a shareholder's interests. Not only will the *nature* of his investment likely change (for example, a smaller, speculative endeavor may merge with a larger, more cautious corporation), but also his relative corporate holdings will probably change (for example, a holder of 30 of an outstanding 100 shares may become a holder of 30 of an outstanding 1000 shares in the new corporation). It is, of course, possible that shareholders will not suffer any harm in a merger—two companies may well be so symbiotic that a merger will benefit both corporations' shareholders. Even in such a case, however, there is the potential "loss of continued investment

88. *Id.* at 11 n.7, *quoting* A.T. Brod & Co. v. Perlow, 375 F.2d 393, 397 (2d Cir. 1967).
89. See text accompanying note 111 *infra.*
90. See text accompanying note 112 *infra.*
91. Ortiz v. South Bend Lathe, 46 Cal. App. 3d 842, 848, 120 Cal. Rptr. 556, 559 (1975), *citing* 15 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS, §7041 (perm. ed. rev. 1973).
92. ASSEMBLY REPORT, *supra* note 43, at 13.

opportunity *in the investment originally chosen.*"[93] At the other extreme, merger between two poorly operating companies could impose management burdens of sufficient magnitude to cripple the resulting corporation and hence destroy the shareholder's investment altogether.

Statutory protections for the shareholder in a merger situation are generally found in shareholder approval requirements and appraisal rights.[94] The Old Code required approval by *two-thirds* of the outstanding shares to effect a merger.[95] Regarding this requirement, it has been noted: "[B]y normally requiring two-thirds approval, the statutes give a veto not only to the shareholders as a body, *but also to minority shareholders*, at least to a minority of sufficient size (one-third of outstanding shares plus one)."[96] The New Code, however, will lower the statutory minimum vote requirement for shareholder approval. Although high-vote provisions may be added in the articles,[97] only a *majority* approval is required by the new law.[98] Additionally,

> [o]n the theory that a corporation should only be required to obtain shareholder approval for acts which result in *significant* changes in the rights or interests of the shareholders, . . . [Section 1201 of the New Code] requires shareholder approval for a reorganization *depending upon the extent to which their control of the corporation is diluted* by the transaction.[99]

Pursuant to this section,[100] shareholder approval is required only if immediately following the reorganization the shareholders possess less than five-sixths of the total combined voting power of the resulting corporation. This new approach to merger approval, characterized by the drafters as the "dilution test,"[101] is significant in at least two respects. First, the approach disregards the notions that a shareholder's interest in a corporation is more than voting power and that some

93. Rams, *Judicial Valuation of Dissenting Shareholder Interests*, 8 LINCOLN L. REV. 74, 88 (1973) (emphasis added) [hereinafter cited as Rams].

94. Appraisal rights, or dissenter's rights, allow a holder of shares voted against a merger to require that the corporation purchase the shares at fair market value. For a further discussion of dissenter's rights, see text accompanying notes 126-161 *infra*.

95. CAL. CORP. CODE §4107.

96. Eisenberg, *The Legal Roles of Shareholders and Management in Modern Corporate Decisionmaking*, 57 CAL. L. REV. 1, 64 (1969) (emphasis added) [hereinafter cited as Eisenberg].

97. *New* CAL. CORP. CODE §204(a)(5).

98. *New* CAL. CORP. CODE §§152, 1201.

99. ASSEMBLY REPORT, *supra* note 43, at 93-94 (emphasis added).

100. *New* CAL. CORP. CODE §1201 provides *inter alia*:

> (b) No approval of the outstanding shares . . . shall be required in the case of any corporation if such corporation, or its shareholders immediately before the reorganization, or both, shall own . . . more than five-sixths of the total combined voting power of the surviving or acquiring corporation or parent party.

101. ASSEMBLY REPORT, *supra* note 43, at 94.

significance is to be attached to his maintaining a "continued investment opportunity in the investment already chosen."[102] This criticism is perhaps overstated in that there are some exceptions to application of the "dilution test." Shareholder approval may be required if any article amendments are involved in the reorganization (as may be likely if the "nature" of the corporation changes);[103] or, shareholder approval may be required if the merger would result in shares being issued with different rights, preferences, or privileges than those surrendered;[104] or, if a close corporation is involved, two-thirds shareholder approval may be required if the resulting corporation will be a non-close corporation.[105] Even if shareholder approval is required to effect a merger, there is credible criticism to the effect that the shareholders' voice ". . . is a very small voice indeed . . . [because the statutes] limit the shareholders' power to approval or disapproval of the package formulated by the board, rather than giving shareholders the right to take a proposed merger and reformulate its details."[106] Second, and perhaps more significant, is the fact that shareholders not given approval opportunity will be unable to trigger dissenter's rights,[107] which are generally conditioned upon a shareholder's vote against a proposal.[108]

In summary, it would certainly seem that in the simple merger situation the minority shareholder has lost some ground under the New Code: approval minimums, even where approval is required,[109] have dropped from a two-thirds requirement to a simple majority, and dissenter's rights have been effectively eliminated for changes which are not "significant."[110]

Two other merger techniques remain to be discussed, the short merger or short-form merger and the *de facto* merger. In the short merger situation, a parent and its subsidiary merge *without being subjected to the requirement of shareholder approval.*[111] A de facto merger may occur when there is a sale of all of a corporation's assets to a second corporation, closely followed by a dissolution of the first corporation.[112]

---

102. See text accompanying note 93 *supra.*
103. *New* CAL. CORP. CODE §1201(c).
104. *New* CAL. CORP. CODE §1201(d).
105. *New* CAL. CORP. CODE §1201(e).
106. Eisenberg, *supra* note 96, at 62.
107. See note 94 *supra.*
108. In California, appraisal may be triggered by abstention or a vote against a proposal; however, appraisal rights do not attach where shareholder approval is not required. *New* CAL. CORP. CODE §1300. For a more complete discussion of California appraisal provisions, see text accompanying notes 126-161 *infra.*
109. See text accompanying note 100, *infra* (the dilution test may exempt certain changes from shareholder approval requirements).
110. See note 94 *supra* and text accompanying note 99 *supra.*
111. O'NEAL & DERWIN, *supra* note 15, at 69.
112. *Id.* at 74.

The New Code directly addresses both of these merger techniques. Unlike the Old Code,[113] Section 1110 of the New Code authorizes the short-form merger when the parent owns between 90 and 100 percent of the outstanding shares of a merging subsidiary. According to the drafters of the New Code, "[a]pproval by minority shareholders in this case is unnecessary as their vote could not prevent the merger."[114] However, unlike the case of the ordinary merger, in which insufficient dilution may exempt the transaction from the requirement of shareholder approval,[115] in the short-form merger dissenter's rights[116] are specifically granted a "dissenting" shareholder notwithstanding his lack of opportunity to formally express his disapproval through his vote.[117]

Section 181(c) of the New Code codifies the de facto merger situation and brings it within the meaning of the term "reorganization."[118] This codification will probably bolster the shareholders' position. Since under the Old Code the sale of assets/de facto merger is not accorded statutory recognition, it has heretofore been uncertain what approach the California courts might take to protect the shareholders with respect to dissenter's rights. On the one hand, some courts in other states have held the de facto merger situation to be sufficiently distinct from the ordinary merger to deny a shareholder's claim for appraisal rights when a sale of assets is followed by liquidation.[119] On the other hand, some jurisdictions have judicially extended the appraisal remedy to de facto merger situations.[120] The new law eliminates this dilemma for the California courts and

> treats various methods of corporate fusion as different means to the same end. This approach is intended to adopt and codify the so-called "de facto merger" doctrine so that the rights of shareholders in a corporate combination do not depend upon the form in which the transaction is cast.[121]

---

113. CAL. CORP. CODE §4124 encompasses the wholly owned subsidiary only.
114. ASSEMBLY REPORT, *supra* note 43, at 92.
115. See text accompanying note 100 *supra.*
116. See note 94 *supra* and text accompanying notes 126-161 *infra.*
117. *New* CAL. CORP. CODE §1110(i).
118. *New* CAL. CORP. CODE §181;
"Reorganization" means:
. . . .
(c) The acquisition by one corporation in exchange in whole or in part for its equity securities (or the equity securities of a corporation which is in control of the acquiring corporation) or for its debt securities which are not adequately secured and which have a maturity date in excess of five years after the consummation of the reorganization, or both, of all or substantially all of the property and assets of another corporation (a "sale-of-assets reorganization").
119. *E.g.*, Cary, *supra* note 18, at 679.
120. *E.g.*, Ferris v. Glen Alden Corp., 393 Pa. 427, 143 A.2d 25 (1958).
121. ASSEMBLY REPORT, *supra* note 43, at 27.

The effect of the de facto merger being cast as a reorganization is to subject the transactions to shareholder approval pursuant to Section 1201. It should be remembered that this section applies the "dilution test" to assess the necessity of shareholder approval.[122] Further, although rights of compulsory repurchase and appraisal are extended to the dissenting shareholder, presumably the reorganization which does not sufficiently dilute the voting power *(i.e.* if the dilution is less than one-sixth) would not affect dissenter's rights.[123]

In summary, the sales of assets/de facto reorganization provisions of the new California law will probably offer considerably more shareholder protection than the Old Code. Nonetheless, it might be argued that the New Code does not go far enough inasmuch as there remains a notable absence of approval and appraisal rights for the minority shareholders whose voting power has been "insufficiently" diluted.[124]

The unique problems of the minority shareholder in the entire fundamental changes arena evolve from his lack of control. Although the degree of harm suffered, if any, will always depend upon the particular circumstances of the corporate change, the minority shareholders are at the mercy of the majority unless precautions are taken in the corporate drafting stages to provide the minority with additional protections. Such protections might include high-vote provisions, which could give a sizeable minority a "veto power," or could include delineation in the articles of the conditions upon which corporate changes may be effected.[125] In the event the minority is unable to affect the outcome of a fundamental corporate decision, dissenter's rights may offer some compensation to minority shareholders.

Dissenter's Rights

Thus far, the dissenter's right to appraisal[126] has been frequently mentioned as a protective measure for minority shareholders. Chapter 13 of the New California Corporations Code[127] describes dissenter's appraisal rights: where shareholder approval is required to effect a corporate reorganization,[128] with some exceptions,[129] the shareholders

122. See text accompanying note 100 *supra.*
123. See note 100 *supra.*
124. See text accompanying note 100 *supra.*
125. As to the likelihood of pro-minority shareholder drafting actually occurring, see text accompanying note 293 *infra.*
126. The right is also commonly referred to as "judicial valuation," *see* Rams, *supra* note 93, at 74, or just "appraisal," O'Neal & Derwin, *supra* note 15, at 62.
127. *New* Cal. Corp. Code §§1300-1312; *see also* Cal. Corp. Code §§4300-4318 for the Old Code's appraisal provisions.
128. See text accompanying note 100 *supra.*
129. See text accompanying notes 99-100 *supra.*

who did not vote in favor of the reorganization will be given the right to demand that the corporation repurchase their "dissenting shares" at fair market value.[130] If there is a disagreement as to the shareholder's status as a dissenter or if the parties are unable to agree on the fair market value of the shares, the New Code provides for redress through the courts.[131] If necessary, the courts are authorized to determine the shareholder's status as a dissenter or a nondissenter, and to appoint appraisers to establish the market value at which the corporation will repurchase the shares.[132]

Appraisal is promoted by advocates for minority shareholders' rights as an opportunity for the minority dissenter to divest himself of his corporate interest at an assured fair market value.[133] Without this remedy, the shareholder might be forced to either tolerate an unacceptable situation or to try to sell his shares at whatever price he can obtain—with the turmoil of a reorganization quite possibly depressing the value of the shares.[134] The appraisal remedy has its critics, however. One commentator has noted that "[t]he appraisal statutes may be viewed either as a bulwark for the rights of the minority, or as a lubricant to speed the spread of majoritarianism."[135] This commentator explains that appraisal statutes

> Almost certainly . . . have made their major contributions not in shielding the minority, but in giving greater mobility of action to the majority—that is, to corporate managements. . . . When a dissenting shareholder seeks to enjoin a transaction, the courts tend to turn him away if he has the appraisal remedy available to him.[136]

This observation is especially valid in states where the appraisal remedy is exclusive, as "exclusive" appraisal statutes eliminate remedies which might otherwise be available to redress fraud or unfair dealings.[137] In California, the shareholder who qualifies as a dissenting shareholder is denied other remedies:

> No shareholder of a corporation who has a right under this chapter

130. *New* CAL. CORP. CODE §1300(a).
131. *New* CAL. CORP. CODE §1304(a).
132. *New* CAL. CORP. CODE §1304(c).
133. O'NEAL & DERWIN, *supra* note 15, at 62.
134. *But see* text accompanying notes 61-62 *supra*. A shareholder facing withheld dividends may be forced to divest, but a fair price is not guaranteed. Arguably, lack of dividend declaration may substantially affect the corporate interest, thus falling within the test suggested by the drafters for granting appraisal rights. See text accompanying note 100 *supra*.
135. Manning, *The Shareholder's Appraisal Remedy: An Essay for Frank Coker*, 72 YALE L.J. 223, 230 (1962) [hereinafter cited as Manning].
136. *Id.* at 227.
137. O'NEAL & DERWIN, *supra* note 15, at 71-72.

> to demand payment of cash for the shares held by the shareholder shall have any right at law or in equity to attack the validity of a reorganization or merger . . . .[138]

It would appear, however, that a shareholder who does *not* qualify to demand repurchase would still be able to obtain redress. For example, a shareholder whose voting power is insufficiently diluted by the merger[139] is not eligible for dissenter's rights and arguably could challenge the reorganization in the courts. It should be noted that the Old Code[140] lacks the conditional language which triggers dissenter's rights in the New Code, *i.e. "If the approval* of the outstanding shares . . . *is required* . . . ."[141] Hence, under the Old Code, any shareholder not voting in favor of a reorganization is granted dissenter's rights, and presumably this includes an abstaining shareholder as well, since the language of the statute grants dissenter's rights to any shares not voted in favor of the reorganization or merger.[142] Under either the Old Code or the New Code, shareholders who do not qualify for dissenter's rights by virtue of voting in favor of the plan would still not be able to successfully attack the transaction, as the affirmative vote would certainly raise a consent defense.

The New Code contains additional dissenter provisions: (1) "[t]o encourage fair treatment of dissenters,"[143] the corporation must pay the costs of an appraisal action if the appraisal price exceeds the originally offered price;[144] and (2) if the court-appraised price is greater than 125 percent of the originally offered price, the court may award attorney's costs, plus interest.[145] From a dissenter's perspective these additional protective measures may appear inadequate in that the dissenter will have to possess shares of substantially greater value than the corporaiton's offer in order to recover all the costs of maintaining his right to be paid fair market value. Faced with the likelihood of attorney's fees not being awarded (whenever the shares are assessed at less than 125 percent of the offer),[146] the dissenting shareholder is apt to accept the corporation's offer, knowing it to be low, but also knowing it would probably cost him more to compel the payment of fair market value through the courts. Thus, it would seem that the corporation's incentive would be to slightly underbid the value of shares, gambling on the

138. *New* CAL. CORP. CODE §1312(a).
139. See text accompanying note 100 *supra.*
140. CAL. CORP. CODE §4301.
141. *New* CAL. CORP. CODE §1300(a) (emphasis added).
142. *New* CAL. CORP. CODE §1300(b)(2).
143. ASSEMBLY REPORT, *supra* note 43, at 99.
144. *New* CAL. CORP. CODE §1305(e).
145. *New* CAL. CORP. CODE §1305(e).
146. *New* CAL. CORP. CODE §1305(e).

likelihood that the shareholder will not force the issue to court. On the other hand, the Old Code makes no provision for the recovery of attorney's fees, and thus the shareholder receiving an obviously insufficient offer from the corporation will be in a better position than he is under the Old Code.[147]

The New Code follows the Delaware lead in limiting dissenter's appraisal rights to non-exchange-listed corporations.[148] Section 1300(b)(1) of the New Code exempts from the dissenter's provisions any corporation listed on a national securities exchange or on the Over-the-Counter Market by the Board of Governors of the Federal Reserve System, unless at least five percent of such shareholders claim dissenter's rights. The rationale for this exemption is that a holder of listed shares "may cash out by selling his shares in the market if a liquid market for his shares exists . . . ."[149] Although such an exemption probably does not defeat the purpose of dissenter's provisions, *i.e.* to give the dissenting shareholder an opportunity to divest at fair market value, one might question whether the possible deterrent effect of appraisal might be lost in the future. Under the Old Code,[150] the imminence of having to apply corporate funds to such purchases may foster a more conservative management attitude toward reorganization. With the "exchange exemption," the corporation is freer to reorganize without fear of depletion brought about by the compulsory repurchase of dissenting shares. Though the dissenter may still have a financially fair remedy in the marketplace, he is nonethless deprived of a bargaining position potentially gained by notifying the corporation considering reorganization that he intends to assert his appraisal rights.

In assessing dissenter's appraisal remedy, it would be fair to note that most of the commentators seem to view appraisal as a satisfactory remedy for a distressed shareholder. Indeed, many authorities advocate the extension of appraisal rights to a broad range of circumstances,[151] including, for example, merger, consolidation (in states where this is still a recognized method of corporate fusion),[152] sale of assets, changes in corporate purpose, changes in shareholder's rights, and changes in the duration of corporate existence.[153] It has been suggested that minority

147. CAL. CORP. CODE §4313.
148. *See* Rams, *supra* note 93, at 75.
149. ASSEMBLY REPORT, *supra* note 43, at 96.
150. CAL. CORP. CODE §4300 *et seq.*
151. *See, e.g.*, Rams, *supra* note 93; Jennings, *supra* note 2, at 206; Note, *Jones v. Ahmanson: The Fiduciary Obligations of Majority Shareholders*, 70 COLUM. L. REV. 1079, 1096 (1970). *But see*, Manning, *supra* note 135, at 227.
152. See text accompanying note 92 *supra.*
153. *See, e.g.*, Manning, *supra* note 135, at 262-65, for a list of states allowing dissenter's rights for the circumstances herein listed.

shareholders' rights could be considerably augmented by extending appraisal statutes to cover all transactions which substantially affect the stockholder.[154] The courts have added some support to such an extension of appraisal rights. For example, in *Farnsworth v. Massey*[155] an appraisal remedy was fashioned for a breach of the majority shareholder's fiduciary duty to the minority. Additionally, the courts have expanded the nature of the remedy by taking a broad view of what constitutes fair market value. In addition to the actual market price of the shares, there is a modern trend toward:

> 1. Judicial recognition of the essentially involuntary nature of the sale of dissenting shares, predicated upon the loss of continued investment opportunity in the investment originally chosen. . . . [and]
> 2. Legal recognition that the loss of an investment opportunity is the loss of a property right, which can permit the award of consequential damages for resultant tax liabilities, hitherto treated as *damnum absque injuria.*[156]

Thus, the California court in *Jones v. Ahmanson*[157] recognized that market price alone would not sufficiently compensate the minority. The facts in that case were conducive to augmenting the market price in that the defendants' acts resulting in capture of the market and depression of the market price were significant factors in establishing their breach of duty to the minority.[158] In the course of the opinion, the court stated that the "[r]eceipt of an appraised value reflecting book value and earnings alone could not compensate the minority shareholders for the loss of this potential"[159] investment value. If the courts are willing to incorporate such considerations into their appraisal values, minority shareholders are at least compensated to some degree for the actual loss they may suffer in a reorganization commenced against their will. As will be discussed below,[160] one might suspect that the overall tone of the New Code will imply new guidelines for the courts evaluating consequences to the minority. In some significant respects, protections to the minority are statutorily diminished,[161] and the courts may well infer that

---

154. O'NEAL & DERWIN, *supra* note 15, at 199.
155. 365 S.W.2d 1 (Tex. 1963). See also text accompanying note 96 *supra.*
156. Rams, *supra* note 93, at 88. He expands:
> For example the dilution of investment position in a going concern resulting from merger or consolidation . . . and, the tax liabilities attaching to a sale of shares, bordering on the involuntary, which in many instances is unplanned in terms of tax avoidance, integrity of investment portfolio and related aspects of estate preservation and growth. *Id.* at 87.

157. 1 Cal. 3d 93, 460 P.2d 464, 81 Cal. Rptr. 592 (1969).
158. *Id.* at 112-114, 460 P.2d at 474-76, 81 Cal. Rptr. at 602-604.
159. *Id.*, at 117, 460 P.2d at 478, 81 Cal. Rptr. at 606.
160. See text accompanying note 200 *infra.*
161. See text accompanying note 200 *infra.*

current legislative policy comprehends a shift away from allowing extraordinary consideration for the minority in an appraisal situation as well.

Issuance of Stock and Preemptive Rights

The minority shareholders' corporate interest can be substantially depleted by the issuance of new stock. Such an issuance can be oppressive to the minority depending upon the number of shares involved, the timing of the issuance, and whether preemptive rights are involved.[162] Preemptive rights afford existing shareholders the first right to purchase newly issued shares, in proportion to their existing holdings.[163] Such rights must usually be provided for in the articles in order to attach.[164]

Though preemptive rights are designed to preserve shareholders' positions in the corporation, this effect can be circumvented by several methods. First, preemptive rights could be granted on a class basis.[165] If the minority's shares are predominantly limited to one or two classes of shares, the denial of preemptive rights to that (those) class(es) would allow issuance of new stock to operate as a squeeze technique[166]—particularly where the majority shareholders do have preemptive rights attached to their classes of shares. Second, even where granted to all classes, preemptive rights can be of limited value to the minority in some cases. For example, the time frame for exercise of the right may be made very brief. The majority, knowing of an imminent new issue, can be financially prepared to purchase additional shares. In contrast, if the new issue is declared at a time when the minority shareholders are known to be at a financial disadvantage, the majority may be able to accurately predict that the minority will not exercise their preemptive rights.[167] In this regard, the volume of the

162. *See* O'Neal & Derwin, *supra* note 15, at 91-95.
163. *Id.* at 92.
164. *New* Cal. Corp. Code §204(a)(2). In the nature of an exception to the requirement that preemptive rights must be granted in the articles is the judicial doctrine of quasi-preemptive rights. The California court describes this doctrine in *Sheppard v. Wilcox*, 210 Cal. App. 2d 53, 26 Cal. Rptr. 412 (1962), where a group of shareholders caused shares to be issued to themselves in order to change their position from minority to majority. Quoting from the New York case of *Dunlay v. Avenue M. etc. Co.*, 253 N.Y. 274, 174 N.E. 917 (1930), the court noted:

> "One formula of fair dealing is universally recognized, i.e., directors may not authorize the issue of unissued shares to themselves for the primary purpose of converting them from minority to majority shareholders. . . ." Under these circumstances, a shareholder in California is said to have quasi-preemptive rights.

210 Cal. App. 2d at 60, 26 Cal. Rptr. at 417. *See also* Shaw v. Empire Savings & Loan Ass'n, 186 Cal. App. 2d 401, 9 Cal. Rptr. 204 (1960).
165. *See generally* Cal. Corp. Code §3601(f).
166. See note 13 *supra*.
167. O'Neal & Derwin, *supra* note 15, at 94.

new issuance is significant. If many new shares are issued, the maintenance of relative holdings may require a substantial outlay of funds. In light of these limitations on the effectiveness of preemptive rights, it may be that the most effective protection for the minority would be an article provision which controls the circumstances of share issuance, thereby allowing the small investor to evaluate in advance the potential of a detrimental issuance.

VOTING RIGHTS

Of fifteen "principal rights" of shareholders listed in *Fletcher's Cyclopedia of Corporations*,[168] seven are directly related to the shareholders' vote. In addition to the right to vote at shareholders' meetings and the right to elect directors and officers, shareholders effect the following rights through their vote: adoption of bylaws, amendment of the corporate charter, reorganization, consolidation, merger, and voluntary dissolution.[169] An examination of the New Code reveals a decrease in the protective measures associated with the shareholder vote.

A. Cumulative Voting

The cumulative vote is regarded as a technique to assure minority representation on the board of directors.[170] Though there is valid criticism to the contrary, some authorities consider the presence of a minority director to be a positive corporate influence. O'Neal and Derwin suggest that the minority representative serves as a watchdog on the board, creating "fear" among the majority that any misdeeds will be reported to the constituency.[171] However, other commentators conclude that the value of cumulative voting may be overestimated. One such commentator contends that the minority board member may be ineffectual—he may be excluded from executive session and from informal agreements, and may not be able to persuade the majority to this viewpoint.[172] Thus, in some situations the minority director may have no impact upon corporate affairs.

Like Section 2235 of the Old Code, Section 708 of the New Code mandates that California corporations afford the shareholders the right

168. 13 FLETCHER, *supra* note 27, §5717.
169. *Id.*
170. The cumulative vote works as follows: "Each share carries as many votes as there are vacancies to be filled, the shareholder being permitted to distribute the votes for all his shares among the candidates in any way he desires." HENN, *supra* note 66, at 364.
171. O'NEAL & DERWIN, *supra* note 15, at 116-17.
172. Mattes, *The Burden of the Corporate Director Elected Noncumulatively*, 63 CAL. L. REV. 463, 465 (1975).

to cumulate their votes.[173] However, certain board functions may be delegated to an executive committee,[174] from which a minority director could presumably be excluded, although matters of "fundamental importance" are reserved to the full board (for example, the declaration of dividends or the amendment, adoption, or repeal of bylaws).[175] In one article which characterizes the cumulative vote as a factor which discourages corporate promoters from incorporating in California, the author offers the use of the executive committee as a mitigating factor:

> [I]f dissention should arise on the board, the use of an executive committee by the majority directors would mitigate its effects. Even though an executive committee might not eliminate the more conservative management attitude that could result from constant criticism, it would enable the corporation to retain a smoothly functioning administrative team of directors.[176]

In addition to the use of an executive committee, there are other ways to circumvent the effects of the cumulative vote. In some states a director may be removed without cause and majority representatives may then be appointed to fill the vacancy. Sections 810 of the Old Code and 303(a)(1) of the New Code protect the minority's representative by providing, in effect, a cumulating of votes in the removal decision as well as in the election decision: "No director may be removed . . . [without cause] when the votes cast against removal . . . would be sufficient to elect such director if voted cumulatively at the election at which the same total number of votes were cast. . . ."[177]

---

173. Though retained in the finally enacted version of the New Corporations Code, it is interesting to note the apparently decreasing stature of the cumulative vote. Pursuant to article 7, §17, the cumulative vote enjoyed constitutional status in California prior to 1930; after that date it assumed a statutory role. *See* Mattes, *supra* note 172, at 465. Even though retained in the new law, the drafts of A.B. 376 (1975-76 Regular Session), which enacted the New California Corporations Code, called for permissive rather than for mandatory cumulative vote. Further, it appears that cumulative voting may be eliminated pursuant to a shareholders' agreement under Section 300(b) of the New Code. It would appear that opponents are gradually gaining support, and one might well suspect its elimination as a mandatory provision in the not too distant future.

Among the objections raised by cumulative vote opponents are:

> [1] The possibility that a rival company might be able to plant a spy on the board of directors in order to obtain commercial secrets. [2] [T]he presence on the board of a crank or the representative of a dissident faction might impede its smooth functioning, or might tend to make the management overly conservative and unwilling to take necessary risks. [3] [U]nder cumulative voting an individual shareholder might find it somewhat easier to induce corporate action favorable to his interests alone.

However, as noted by the author of these observations, a 1951 study indicated these typically cited problems occur only infrequently, if at all. Comment, *Choice of a Corporate Domicile*, 49 CAL. L. REV. 518, 525 (1961).

174. CAL. CORP. CODE §501, *New* CAL. CORP. CODE §311.

175. CAL. CORP. CODE §501, *New* CAL. CORP. CODE §311.

176. Comment, *Choice of a Corporate Domicile*, 49 CAL. L. REV. 518, 525 (1961) (footnotes omitted).

177. *New* CAL. CORP. CODE §303(a)(1).

Reduction of the number of directors can also circumvent the cumulative vote. For example, a 20 percent shareholder would be able to cumulatively elect a member of a five member board, but could not elect a representative if the board were reduced to three or four. The minimum number of directors allowed in California is three.[178] According to Section 303(b) of the New Code, the number of directors may not be reduced to remove a director during his term, but such a reduction may be accomplished between terms. Since only a majority vote is required to amend the corporate articles to reduce the number of directors, this manner of circumventing the cumulative vote would at first appear viable in California, provided there is compliance with Section 303(b). However, the minority shareholders have an added protection against this method of squeezing out their interests as Section 212(a) of the New Code allows, in effect, a cumulative vote on this issue as well.[179]

"Staggered" boards also may negative the impact of the cumulative vote. If only one or two directors are elected at any one time, the cumulative vote may not produce enough votes to elect a director. However, it would appear that Section 301 of the New Code precludes staggered boards in California. On first reading this conclusion is not obvious: "The articles may provide for the election of *one or more* directors by the holders of the shares of any class of series. . . ."[180] However, since elections must be held annually and the terms of office are only one year,[181] it may be inferred that the "may provide for one or more directors to be elected" language refers to assigning directors to particular classes, rather than to staggering the board.

Thus, although there are indications that support for the mandatory cumulative vote is weakening,[182] California law still preserves this right for the minority, and the law contains sufficient safeguards to prevent circumventing the cumulative vote by reducing the number of directors or by staggering the elections. There are, however, two respects in which the effectiveness of the cumulative vote may have suffered by

178. *New* CAL. CORP. CODE §212(a). Pursuant to this section there are, however, exceptions that allow as few as one director if all shares are yet unissued or if there are only one or two shareholders.

179. *New* CAL. CORP. CODE §212(a) provides *inter alia*:

> . . . a bylaw or amendment of the articles reducing the number or the minimum number of directors cannot be adopted if the votes cast against its adoption at a meeting or the shares not consenting in the case of action by written consent would be sufficient to elect at least one director *if voted cumulatively* at an election at which all of the outstanding shares entitled to vote were voted and the entire number of previously authorized directors were then being elected (emphasis added).

180. *New* CAL. CORP. CODE §301 (emphasis added).

181. *New* CAL. CORP. CODE §301(a).

182. See text accompanying note 173 *supra*.

adoption of the New Code. Section 708(b) of the New Code requires that the candidates' names be placed on the ballot prior to the voting and at least one shareholder must have expressed an intention to vote cumulatively prior to the election.[183] While these prerequisites shift some of the burden to the minority shareholders, the overall effect upon the exercise of the cumulative vote may be insignificant."

B. "Supermajority" Vote Requirements

In addition to the cumulative vote, minority shareholders may find vote-related protection in "supermajority" vote requirements, that is, requirements which call for two-thirds, ninety percent, or even unanimous shareholder approval to give effect to certain measures. By requiring at least a two-thirds vote, minority shareholders in sufficient numbers (one-third of the outstanding shares plus one) are given a veto power with which to protect their interests.[184] Such high-vote provisions are required in many states to effect fundamental changes, such as charter amendment, merger, consolidation, or sale of assets.[185]

Under the Old Code, a two-thirds vote is required to approve loans or guarantees to corporate officers, directors, or others;[186] to effect a stock purchase plan without exercising preemptive rights;[187] to authorize the corporate purchase of shares out of reduction surplus;[188] to amend the articles;[189] or to approve a consolidation of merger plan.[190] Additionally, unanimous shareholder approval is required to hold a corporate meeting at a place other than the principal corporate office (unless otherwise specified in the bylaws),[191] and unanimous approval is required to recover an assessment on fully paid shares.[192] The New Code calls for a *majority* vote in all the above circumstances unless there are contrary provisions in the bylaws.[193] The rationale for this lowering of the vote requirement is that "corporate actions should be subject to control by a majority" of the shareholders.[194]

As mentioned above, however, there is authorization in the New Code, as there has been in the past,[195] for a greater-than-majority vote

183. REVIEW OF SELECTED 1975 CALIFORNIA LEGISLATION, this volume at 268.
184. *Eisenberg, supra* note 96, at 64. See also text accompanying note 80 *supra.*
185. O'NEAL & DERWIN, *supra* note 15, at 62.
186. CAL. CORP. CODE §823. *See also* 15 CAL. JUR. 3d, *Corporations* §288 n.27.
187. CAL. CORP. CODE §1108.
188. CAL. CORP. CODE §1906.
189. CAL. CORP. CODE §3634.
190. CAL. CORP. CODE §4107.
191. CAL. CORP. CODE §2210.
192. CAL. CORP. CODE §3639.
193. *New* CAL. CORP. CODE §§315, 903.
194. ASSEMBLY REPORT, *supra* note 43, at 90.
195. *See* CAL. CORP. CODE §500.

for all but election of directors and the voluntary dissolution vote. To effect a supermajority vote requirement, a provision embodying this requirement must be written into the articles or bylaws.[196] In this regard the code's drafters noted:

> This "super-majority" vote requirement for approval of certain corporate acts is frequently desired in close corporations for the protection of a minority shareholder against adverse joint action by other shareholders. Additionally, a higher percentage requirement may be useful in non-close corporations, particularly where special protection is desired for a certain class of shares.[197]

This legislative recognition of the protective nature of a high-vote provision is significant in that a legislative policy can possibly be inferred: the legislature considered and rejected a high-vote posture in favor of a more management-oriented majority vote. The impact of this new California policy in favor of majoritanism may go well beyond the obvious effect of requiring the approval of fewer shareholders to carry a measure. The courts, when faced with litigation between the shareholder and the corporation or the shareholder and a director, are reluctant to grant relief where doing so would impinge upon either the business judgment of management or the principal of majority rule.[198] As one authority has noted, the "unavoidable result of the fundamental principal that the majority can regulate and control the lawful exercise of the powers"[199] is that the courts will not interfere in favor of the minority absent a plain showing that an action is contrary to the corporation's interest and that the director(s) " . . . must have acted with an intent to subserve some outside purpose . . . in a manner inconsistent with . . . [the corporation's] interest."[200] With such judicial reluctance to interfere with majority rule in mind, the legislative policy which may be inferred from the two-thirds vote provisions contained in the Old Code is significant. The courts might justifiably rely upon legislative expressions that in certain circumstances the minority's special interests are to be protected, even at the expense of majority.[201] To whatever degree

196. A bill currently before the legislature, A.B. 2849 (1975-76 Regular Session), would amend §902 of the New Code so that provisions in the articles of incorporation calling for a larger proportion of the votes of the directors or shareholders to carry an issue than those provided in the general corporation law shall not be altered, amended or repealed except by the greater vote unless otherwise provided for in the articles.

197. ASSEMBLY REPORT, *supra* note 43, at 38.

198. O'NEAL & DERWIN, *supra* note 15, at 42. See also text accompanying note 57 *supra.*

199. 13 FLETCHER, *supra* note 27, at §5821.

200. *Id.*

201. *See* Cary, *supra* note 18, at 670. Speaking of judicial interpretations in Delaware, Cary noted that

> the courts have undertaken to carry out the "public policy" of the state and create a "favorable climate" for management. Consciously or unconsciously, fiduciary standards and the standards of fairness generally have been relaxed.

the simple majority voting provisions contained in the New Code foreshadow a shift away from minority interest in favor of the majority and management, the courts may in the future infer a mandate to reassess their consideration of minority shareholder's rights.

CORPORATE RECORDS AND REPORTS

Access to corporate records and information may be an important factor in protecting minority rights. Whether or not the minority is represented on the board, the ability to inspect essential corporate documents may give the minority an opportunity to monitor majority and board activities. This in itself could be an effective control against misdealings.[202] Though minority shareholders generally have a right to receive certain information regarding corporate activities,[203] this right is not unlimited.[204]

The New Corporations Code considerably augments the shareholder's right to receive information from the corporation. The Old Code allows a shareholder to inspect corporate records and to extract information therefrom for any purpose reasonably related to a shareholder's interests as such.[205] The new law will grant a five percent shareholder an *absolute* right to inspect *and copy* stockholders lists, and it will allow a similar right to *any* shareholder conditioned upon a reasonable relation to his or her interest as a shareholder.[206] Other corporate records[207] also will be accessible for inspection and copying for any shareholder-related purpose.[208]

Reports to the shareholders also lend a degree of visibility to corporate activities, and thus help conform such activities to the best interests of the shareholders. The Old Code allows financial reports to be waived by bylaw or article provisions.[209] Under the New Code, however, annual financial reports to the shareholders are required;[210] and waiver is allowed only for corporations having 100 or fewer shareholders.

---

202. *See* Cary, *Corporate Standards and Legal Rules*, 50 CAL. L. REV. 408, 409: "[d]isclosure is the most realistic means of coping with the ever-present problem of conflicts of interest [in a business enterprise]."

203. 13 FLETCHER, *supra* note 27, at §5818.

204. *Goldstein v. Lees*, 46 Cal. App. 3d 614, 621, 120 Cal. Rptr. 253, 257 (1975), wherein the court noted:

> [A]lthough shareholders have some rights to corporate information not available to the general public, shareholder status does not in and of itself entitle an individual to unfettered access to corporate confidences and secrets . . . .

205. CAL. CORP. CODE §3003.

206. *New* CAL. CORP. CODE §1600.

207. *E.g.*, accounting books and minutes. *New* CAL. CORP. CODE §1601.

208. *New* CAL. CORP. CODE §1601(a).

209. CAL. CORP. CODE §3006.

210. *New* CAL. CORP. CODE §1501.

Moreover, even if annual reports are waived,[211] any shareholder will be able to compel the production of certain corporate financial statements.[212]

Additionally, Section 1501(b) of the new law expands the disclosure requirements mandated by Section 16(b) of the Securities and Exchange Act of 1934.[213] The 1934 Act calls for disclosure of any transactions between the corporation and its officers or directors or between the corporation and any ten percent shareholder. However, that Act applies only to corporations with more than 500 shares, with assets greater than $1,000,000 *and* which are engaged in interstate commerce.[214] California's New Code increases the visibility of corporate activities by extending similar disclosure requirements to cover smaller, non-listed corporations which are exempt from federal Section 16(b) disclosure requirements.[215]

Finally, the New Code reduces from ten percent to five percent the shareholder interest required to compel an income statement,[216] again serving to bring corporate activities within the view of minority shareholders. Just as a minority director on the board may serve as a watchdog to keep corporate activities in line with the interests of shareholders,[217] the knowledge that five-percent shareholders can compel the production of records may serve to lessen the likelihood of misdealings. Cary supports this contention, saying in essence that disclosure is a "prophylactic" which prevents people from taking an action they know might be publicized.[218] If such a contention is correct, the increased accessibility of corporate records represents perhaps the most significant of the few additional shareholder protections afforded by the New Code.

Meetings and Quorums

By failing to hold shareholders' meetings, the corporation may be able to suppress much of the shareholders' influence on the corporation.[219] At the meetings the shareholders elect directors, review corporate activities and vote on those corporate activities which require shareholder approval. As with many other oppressive techniques described thus far, the minority shareholder may be uniquely affected in that, lacking actual control, he might often rely upon the examination of corporate

211. *New* Cal. Corp. Code §1501(a).
212. *New* Cal. Corp. Code §1501(d).
213. 15 U.S.C. §78*p* (1934).
214. 15 U.S.C. §78*l* (1934).
215. *New* Cal. Corp. Code §1501(b).
216. Cal. Corp. Code §3011 (requiring 10% holdings to compel a statement); *New* Cal. Corp. Code §1501(c) (requiring 5% holdings).
217. See text accompanying note 171 *supra.*
218. Cary, *supra* note 18, at 700.
219. O'Neal & Derwin, *supra* note 15, at 113.

affairs that may occur at shareholders' meetings as an indirect control upon those affairs.[220]

In California annual meetings are required, and under the New Code shareholders are offered an expanded opportunity to compel the annual meeting should the corporation attempt to avoid it.[221] Moreover, under the New Code[222] special meetings may be induced by 10 percent of the voting shareholders, whereas the Old Code requires the affirmative vote of 20 percent of the voting shareholders to compel a special meeting.[223]

Even though an annual meeting or special meeting is called, there are ways to circumvent the purpose and effectiveness of a shareholders' meeting. One method is to hold a meeting at a relatively inaccessible location. California law allows out-of-state meeting places to be provided for in the bylaws.[224] A shareholder looking for protection against remote shareholders' meetings should seek a bylaw specifying a particular convenient location, or should look for the absence of a bylaw specifying out-of-state meetings; in the absence of a contrary bylaw, the meeting must be held at the principal executive offices of the corporation.[225]

Another method of minimizing the effectiveness of shareholders' meetings can be found in very low quorum requirements. The Model Business Corporations Act of the American Bar Association suggests that a majority of the voting shares should be represented in order to constitute a quorum, and in no case should less than one-third of the voting shares comprise a quorum.[226] Thus, if less than one-third of the shares are represented at the meeting, some authorities suggest that the meeting inadequately represents the interests of the shareholders.[227] A high quorum requirement, on the other hand, secures to the minority a veto power, since if a sufficient minority fail to attend a meeting, any transaction requiring shareholder approval will be precluded.

220. It has been suggested by some corporate managers that the visibility of corporate affairs gained through disclosure requirements obviates the need for shareholder's meetings. But Cary concludes, "[m]anagement's action . . . should be disclosed to and monitored by outside groups; as a practical matter this group should be the shareholders." Cary, *supra* note 18, at 699.

221. *New* CAL. CORP. CODE §600(c) allows any shareholder to petition directly to superior court to compel the meeting. *But see* CAL. CORP. CODE §2240, which currently limits remedial action to the Attorney General who *may*, upon complaint of a shareholder, notify the corporation of the complaint, after which the corporation has 30 days to reply before the Attorney General may institute court action to compel the meeting.

222. *New* CAL. CORP. CODE §600(d).

223. CAL. CORP. CODE §2202(c).

224. CAL. CORP. CODE §815; *New* CAL. CORP. CODE §600.

225. CAL. CORP. CODE §815; *New* CAL. CORP. CODE §600.

226. COMMITTEE ON CORPORATE LAWS OF THE AMERICAN BAR ASSOCIATION, MODEL BUSINESS CORPORATIONS ACT 32 (rev. 1969).

227. *See* 5 W. FLETCHER, CYCLOPEDIA OF THE LAW OF PRIVATE CORPORATIONS, §2013 (perm. ed. rev. 1967).

The Old Code establishes a quorum at a majority of the voting stock, with different provisions allowable by article or bylaw in the case of a non-profit corporation or a mutual water company.[228] The New Code also sets the quorum at a majority; however, the articles or bylaws of any but a close corporation may provide for a quorum between one-third and majority.[229] The Old Code's lack of restrictions on the quorum in the non-profit setting allows quorums ranging from very low to very high. Thus, a minority shareholder could be very susceptible to majoritarian abuse in the case of low quorum requirements, or could occupy a protected and even controlling position in the case of high quorum requirements. The New Code, by setting the maximum quorum at a majority of the outstanding shares, effectively eliminates minority control, yet it precludes very low (below one-third) quorums, thereby protecting against that potential abuse. In the "for profit" setting, on the other hand, the New Code will allow lower quorum requirements than the Old Code, which could be viewed as a slight decrease in minority protection. To ensure maximum protection of his interests, a minority shareholder should seek establishment of the maximum quorum number allowable (fifty percent plus one),[230] and should seek bylaw or article provisions specifying convenient meeting places.

Sale of Control

Litigation of minority shareholder rights is often based upon the sale-of-control situation,[231] the court being asked to determine if non-controlling stockholders should be allowed to share in the profits realized in the sale. The basis of the dispute stems from a theoretical disagreement as to the nature of corporate control. Generally, two views of corporate control and its sale are recognized. One view holds that the sale of control is similar to the sale of any other kind of property, thus the owner may sell at a profit without obligation to share the profit (or premium as it is generally called) with other shareholders.[232] The other view is that dominant shareholders are in a position to influence and control corporate affairs, and therefore the controlling shareholders owe a fiduciary duty to the corporation and to the minority shareholders.[233]

228. Cal. Corp. Code §2211.
229. *New* Cal. Corp. Code §602(a).
230. This result could also be assured if the articles were silent as to quorum, as the presumption would then be a 50% plus one quorum. *New* Cal. Corp. Code §602(a).
231. Note, *Jones v. Ahmanson, The Fiduciary Obligations of Majority Shareholders*, 70 Colum. L. Rev. 1079, 1086 (1970). The author notes that prior to Jones v. Ahmanson, the only cases prevailing on breach of fiduciary duty theories were those in which the breach involved a negligent sale of control to looters.
232. Annot., 38 A.L.R.3d 738 (1971).
233. *Id.* at 741.

Under this view, if the sale of controlling shares can be interpreted as a sale of stock *only*, the selling stockholder may retain the full price received.[234] On the other hand, if the controlling stockholder was paid *to transfer control*, he is under obligation to share the premium (that portion of the price received which can be attributed to the control factor apart from the bare share value) with the other stockholders.[235]

California modernly follows the latter approach in evaluating the sale of control situation. In a recent shareholder's derivative action against a former majority shareholder who sold to a "looter,"[236] a California appellate court in *Debaun v. First Western Bank*[237] described the evolution of California case law in this area:

> Early case law held that a controlling shareholder owed no duty to minority shareholders or to the controlled corporation in the sale of his stock. . . . Decisional law, however, has since recognized the fact of financial life that corporate control . . . may be misused. Thus the applicable proposition now is that "in any transaction where the control of the corporation is material," the controlling majority shareholder must exercise good faith and fairness "from the viewpoint of the corporation and those interested therein."[238]

The particular concern of the minority shareholder in a sale of control situation is that if the sale meets the standards of "good faith and fairness,"[239] there is no recourse, such as dissenter's rights. For example, the buyer of control may be inexperienced or may be a poor corporate manager, but neither inadequacy will satisfy the "intent to do harm" standard suggested by the *Debaun* court.[240] Short of negligence sufficient to characterize the conduct of the new controlling shareholder as a breach of fiduciary duty,[241] the minority shareholder may find investment expectations substantially altered with no recourse short of selling his shares on the open market.

The courts' recognition of this susceptibility is evidenced by the judicial approach to the sale of control cases. The minority sharehold-

---

234. *Id.* at 741-42.
235. *Id.* at 742.
236. A "looter" is one who, in bad faith, misappropriates and depletes corporate assets. *See* DeBaun v. First W. Bank & Trust Co., 46 Cal. App. 3d 686, 120 Cal. Rptr. 354 (1975).
237. *Id.* at 696, 120 Cal. Rptr. at 359-60 (citations omitted).
238. *Id.* at 696, 120 Cal. Rptr. at 359-60.
239. The *DeBaun* court went on to describe the qualities of "good faith" to include a duty to investigate the buyer whenever there are circumstances from which a reasonable person would suspect the potential buyer intended to harm the corporation or its shareholders. *Id.* at 696, 120 Cal. Rptr. at 360.
240. *Id.*
241. For a discussion of fiduciary standards pursuant to §309 of the New Code, *see* Comment, *California's New General Corporation Law: Directors' Liability to Corporations*, this volume at 613.

ers are "compensated" by allowing their participation in the premium proceeds.[242] This modern approach followed by the California courts affords the minority shareholder a fair consideration not available in states following the older, personal property approach to sale of control.[243] Although one might expect the California courts to reassess their consideration of minority shareholders in light of those provisions in the New Code which seem to favor majoritarianism, the judicial theory in the sale of control cases does not rest wholly upon policy considerations, but also upon a characterization of control as an asset.[244] Thus, the minority shareholder could probably expect the court's protective posture to continue in this instance.

Involuntary Dissolution

The oppressed minority shareholder may find that involuntary dissolution offers the appropriate solution to his or her situation. Involuntary dissolution involves a "qualified" shareholder petitioning the court to wind up the affairs of the corporation.[245] This is a sensitive and extreme remedy, and though it may be discussed as a protective measure for the oppressed stockholder, it must be considered a possible squeeze technique as well.[246] The New Code extends the right to petition for dissolution to a broader range of persons, and it narrows the grounds upon which dissolution may be sought.

Under the New Code, the action to dissolve may be initiated by one-half or more of the directors, by at least one-third of the shareholders, by any shareholder in a close corporation, or by any person specified in the articles.[247] These new provisions differ from those contained in the Old Code[248] in several important respects. First, *any* shareholder in a close corporation may petition for dissolution under the New Code, while the Old Code neither defines nor addresses the close corporation. From the New Code's extensive close corporation dissolution provision one might infer a legislative recognition that in the very small corporation, the minority shareholder is more susceptible to oppression.[249] In their discussion of close corporation squeeze-outs, O'Neal and Derwin

242. *See, e.g.*, Perlman v. Feldmann, 219 F.2d 173 (1973); Brown v. Halbert, 271 Cal. App. 2d 252, 76 Cal. Rptr. 781 (2nd Cir. 1969).
243. *See, e.g.*, Honigman v. Green Giant Co., 309 F.2d 667, 670 (8th Cir. 1962), *cert. denied*, 372 U.S. 941 (1963) (exemplifying a state which follows the traditional personal property approach to sale of control).
244. *See, e.g.*, 219 F.2d 173.
245. See text accompanying note 247 *infra*.
246. See note 13 *supra*.
247. *New* Cal. Corp. Code §1800.
248. Cal. Corp. Code §4650.
249. See text accompanying note 254 *infra*.

suggest that as a protective measure the minority shareholder should seek to be among the persons eligible to petition for dissolution;[250] in the close corporation setting under the New Code, this suggestion is certainly accommodated. Second, the New Code allows an article provision authorizing additional persons to petition for dissolution. The Old Code requires at least one-half or more of the directors or one-third or more of the shareholders to seek involuntary dissolution.[251] The New Code's authorization is very broad, and there are no statutory limitations upon who may be granted the opportunity to dissolve. In keeping with the suggestion above, minority shareholders in publicly held corporations should seek to be included among the persons authorized to seek dissolution.

To offset the broader range of persons eligible to seek dissolution under the New Code, the grounds upon which dissolution may be sought will be slightly more restrictive than the grounds under the Old Code.[252] The New Code requires, as one of several bases for seeking dissolution, the conjunctive operation of (a) director deadlock *and* (b) factionalization of voting shares or failure to fill vacancies on the board for two successive annual meetings.[253] The Old Code is silent as to dissolution based on board vacancy, and deadlock and factionalization are each independent bases for seeking dissolution.[254] Thus, under the New Code, dissolution based on deadlock may be slightly more difficult to effect because the shareholder must first seek to resolve the deadlock by voting in another director. From the minority's perspective, this provision is probably more beneficial than detrimental in that the minority will have more control—if the board is deadlocked, the shareholder has the opportunity to try to elect a director to break the deadlock; if dissolution is desired, the vote may be cast in a manner which will preserve the deadlock. The Old Code, on the other hand, does not require consultation with the shareholder in the event of director deadlock.[255]

Another basis for dissolution under the Old Code is that "liquidation. . . is reasonably necesary for the protection of the rights or interests of any substantial number of the shareholders or of the

250. O'NEAL & DERWIN, *supra* note 15, at 211. *See also* Note, *Unusual Statutory Remedies for the Deadlocked Corporation in California: Voluntary Dissolution and the Provisional Director*, 48 CAL. L. REV. 272 (1960) (other states have more stringent limits upon who may seek dissolution: Delaware, 2/3 vote; Illinois, unanimous or 2/3; Iowa, unanimous, unless otherwise set in articles; Pennsylvania, unanimous unless otherwise recommended by directors).

251. CAL. CORP. CODE §4650.

252. *See* CAL. CORP. CODE §4651.

253. *New* CAL. CORP. CODE §1800(b)(2).

254. CAL. CORP. CODE §4651(b), (c).

255. CAL. CORP. CODE §4651(b).

complaining shareholders."[256] This provision has the least definite standards for dissolution, leaving the most leeway for judicial interpretation. This section was the subject of recent litigation in *Stumpf v. C. E. Stumpf and Sons, Inc.*,[257] wherein the court recognized that similar provisions in other states had been narrowly construed to require management misconduct or deadlock in order to grant relief.[258] A similar interpretation, the court noted, had been urged by Ballantine, who argued that broad construction "makes it too easy for an obstreperous minority to interfere with the legitimate control and management of the majority. . . ."[259] The court found, however, that the potential for minority abuse had been recognized by the legislature, and that the section was to be interpreted as an independent ground for dissolution. The protection for the majority and the corporation, said the court, was to be found in Section 4658 (of the Old Code), which provides that opponents may prevent liquidation by buying out the shares of the plaintiffs for dissolution at fair market value.[260] The legislature has responded to this broad interpretation by specifying in the New Code that dissolution based upon "protection of the rights or interests"[261] of the shareholder will be restricted to corporations having 35 or fewer shareholders. The drafters felt this limitation was necessary because of the broader range of persons eligible to seek dissolution,[262] namely *any* close corporate shareholder and *anyone* named in the articles.[263] The minority shareholder in a smaller corporation thus has retained an avenue lost to stockholders in the larger corporation. In order to effect dissolution in the larger corporation, stockholders must rely upon one of the other bases listed in Section 1800, all of which allow less leeway for judicial interpretation and require more grievous circumstances to establish the need for a winding up of corporate affairs.[264]

In any event, the shareholder seeking dissolution is required to petition in good faith.[265] Regarding this requirement it has been written:

> The duty of good faith required of a dissolving shareholder is of a limited and selfish sort. It is not the same standard of good faith

256. CAL. CORP. CODE §4651(f).
257. 47 Cal. App. 3d 230, 120 Cal. Rptr. 671 (1975).
258. *Id.* at 234, 120 Cal. Rptr. at 674.
259. *Id., quoting* H. BALLANTINE & G. STERLING, CALIFORNIA CORPORATION LAWS §318, at 308 (1938 ed.).
260. 47 Cal. App. 3d at 235, 120 Cal. Rptr. at 671.
261. *New* CAL. CORP. CODE §1800(b)(5).
262. ASSEMBLY REPORT, *supra* note 43, at 103.
263. *See New* CAL. CORP. CODE §1800(a)(2).
264. *See New* CAL. CORP. CODE §1800.
265. Comment, *Unusual Statutory Remedies for the Deadlocked Corporation in California: Voluntary Dissolution and the Provisional Director*, 48 CAL. L. REV. 272, 273 (1960).

> used to test the actions of directors and controlling shareholders in the general conduct of corporate affairs. Where no advantage over the other shareholders is gained, no prejudice to third parties results, and no other way out is available, the good faith requirement is satisfied by any conduct short of fraud.[266]

It is upon the good faith limitations that the minority shareholder must rely to prevent oppressive dissolution. The above comment suggests that in such a critical matter as dissolution, the courts are willing to subject the parties to a *lesser* standard than is normally required. Thus, under such circumstances, the expanded dissolution rights contained in the New Code may place the minority shareholder in a more vulnerable position than he currently occupies; nonetheless, the dissolution alternative may become more accessible to the minority shareholder if he is among the persons to whom "initiating rights" are granted.

SHAREHOLDER SUITS

Because the shareholder must often resort to the courts to vindicate his rights, it is important to look at some of the procedural aspects of California law relative to shareholder litigation. In particular, two changes in California law will be examined for their possible effect on shareholder suits: the security-for-expense requirements and the indemnity provisions of the Old and New Codes.

A. Security for Expenses

Security-for-expense statutes were designed to discourage the prosecution of unmeritorious claims against corporate managers and directors.[267] The statutes require the shareholder plaintiff to post a bond attributable to corporate expenses in the event the plaintiff does not prevail.[268] There are differing opinions as to the effect of security for expense statutes upon shareholder litigation. One researcher found support for the contention that the statutes had a "dramatic effect" in producing "a substantial decline in the number of derivative suits commenced in the New York courts."[269] This decline caused critics of the New York statute to conclude that the security requirement "was not only discouraging unmeritorious claims, but also effectively preventing minority shareholders with meritorious claims from seeking derivative relief."[270] On the other hand, a New York attorney interviewed by that

266. *Id.*
267. Comment, *Security for Expenses in Shareholder's Derivative Suits: 23 Years' Experience*, 4 COLUM. J. OF LAW & SOC. PROB. 50 (1968).
268. *Id.* at 52.
269. *Id.* at 54.
270. *Id.* at 54.

commentator noted that in most cases, the sophisticated defendant would not move for security because by doing so the corporation might subject itself to additional expense in corporate time and effort.[271]

The security for expense provisions contained in the Old Code, which attach in derivative actions,[272] are unique in that they require showings by the moving corporation that (1) there is no reasonable possibility that the suit will benefit the corporation, or (2) that the corporation was in no way a party to the transaction that is the subject of the litigation.[273] Not only do these security prerequisites assure the suing shareholder due process in any assessment of security,[274] they somewhat mitigate the increased security minimum imposed by the new law (raising the minimum from $25,000 to $50,000).[275] The rationale for this increased bond is to partially offset the effects of inflation upon corporate costs.[276] Although the cost of living has risen sharply since 1949 when the $25,000 security requirement was first imposed,[277] this doubling of security costs may certainly be considered a deterrent to future shareholder derivative litigation.

B. *Indemnification*

The New Code's provisions for director indemnification of expenses incurred in litigation and in withstanding insurgent movements might also be viewed as another deterrent to the shareholder suit. The drafters characterize the new indemnity provisions as "substantially improved";[278] from the perspective of management this may be so, but from the minority's viewpoint this is doubtful. Whereas the Old Code limits indemnity to cases where a director prevails in the litigation or where the court approves a settlement of the claim,[279] the New Code broadens the indemnity situations to include situations where the director acts in good faith in a manner reasonably believed to be in the best interests of the corporation.[280] Although the new indemnification prov-

271. *Id.* at 65.
272. CAL. CORP. CODE §834.
273. CAL. CORP. CODE §834.
274. *See* Comment, *Due Process and Security for Expense Statutes*, this volume at 176, 182-84 (1976) (concluding that the Cal. Corp. Code §834 requirements produce "clearly the type of procedure which would be considered 'meaningful' and 'appropriate to the nature of the case,' and therefore in keeping with the requirements of procedural due process." (citation omitted).
275. *New* CAL. CORP. CODE §800(d). See also *New* CAL. CORP. CODE §800(b)(1) (contemporaneous ownership requirement).
276. ASSEMBLY REPORT, *supra* note 43, at 89.
277. CAL. CORP. CODE § 834, *enacted*, CAL. STATS. 1949, c. 499, §1, at 857.
278. ASSEMBLY REPORT, *supra* note 43, at 7.
279. CAL. CORP. CODE §830.
280. *New* CAL. CORP. CODE §317. For further discussion of director's indemnifcation, *see* Comment, *California's New General Corporation Law: Directors' Liability to Corporations*, this volume at 613.

isions are probably not unreasonable, the minority shareholders may arguably find themselves in a detrimental position nonetheless. This result may obtain simply because the directors are offered broader opportunity for indemnification. With their risks minimized, they may be expected to more vigorously oppose minority surges.[281]

SUMMARY

The minority shareholder's position in California is undergoing a change. As shown in the preceding comments, his protection in some instances has been broadened and strengthened by provisions in the New Corporations Code; in other cases, his protection has decreased. A brief summary will assist in evaluating the evolving status of the California minority shareholder.

1. Dividends[282]—The business judgment aspects of dividend declaration make it difficult for the minority to compel dividends, but the New Code's basic solvency limitations should afford added protection against dividends which the corporation cannot afford. The ability to control dividends through the articles or bylaws is uncertain, although it would appear an unavailable alternative.

2. Employment and Salaries[283]—The California minority shareholder could be victimized by majority shareholders employed by or directing the corporation. Excessive salaries and generous benefits may offset withheld dividends and may deplete corporate assets. The New Code offers added protection to the minority only indirectly through new fiduciary duty standards; however, other protective measures may be added to the corporate charter.

3. Corporate Changes[284] and Dissenter's Rights[285]—The New Corporations Code will require only a majority as opposed to a current two-thirds vote to effect most corporate changes. Moreover, shares may be redeemed, then reissued, thus affording the majority a tool for eliminating any unwanted shareholders. Reorganizations will be subjected to a "dilution test" to determine if dissenter's rights are to be granted, but more structural changes are encompassed by the statute. Thus, once the threshold requirement of sufficient dilution is surpassed, shareholders are given greater opportunity in which to exercise their dissenter's

281. However, there is a possible argument that the broader indemnification provisions may attract more competent managers.
282. See text accompanying notes 22-52 *supra.*
283. See text accompanying notes 53-63 *supra.*
284. See text accompanying notes 64-125 *supra.*
285. See text accompanying notes 126-61 *supra.*

rights. Shareholders in large exchange-listed corporations, however, may lose their dissenter's rights altogether.

4. Stock Issuance and Preemptive Rights[286]—The New Code does not change the shareholder's status relative to stock issuance. The minority's relative corporate holdings could be significantly depleted by a stock issuance, but article or bylaw protections could alleviate this potential problem.

5. Voting[287]—The cumulative vote is retained and offers an effective tool to the minority shareholders seeking representation on the board of directors. The number of votes required to effect shareholder decisions has, in most cases, been set at a simple majority by the New Code. This reduction from the present two-thirds vote is perhaps the most significant change affecting the minority shareholder in that it not only reduces his ability to impact upon corporate affairs, but also it implies a legislative posture favoring majority rule of corporations.

6. Corporate Records and Reports[288]—Corporate records will be more accessible to the minority shareholder under the New Code. This may somewhat offset the reduction of the two-thirds vote required to effect shareholder decisions.

7. Meetings and Quorums[289]—Under the New Code, the shareholder is offered an expanded opportunity to compel corporate meetings. This, too, may help alleviate his lowered voting effectiveness. Quorum requirements are appropriately set to ensure adequate shareholder representation, although in the case of a close corporation, there is the added protection of a majority-quorum requirement.

8. Sale of Control[290]—California courts are protective of the minority in the sale of control situation. Presumably this position will continue despite the detectible policy shift toward the majority.

9. Involuntary Dissolution[291]—The New Code alters dissolution provisions in ways which will impact upon minority shareholders. A proposed dissolution based upon management deadlock will be subjected to a shareholder vote prior to the dissolution. A basis presently available for dissolution, *i.e.* for the protection of the rights or interests of shareholders, will be limited to corporations having 35 or fewer shareholders. This limitation is offset somewhat by the expansion of persons eligible

286. See text accompanying notes 162-67 *supra.*
287. See text accompanying notes 168-201 *supra.*
288. See text accompanying notes 202-18 *supra.*
289. See text accompanying notes 219-30 *supra.*
290. See text accompanying notes 231-44 *supra.*
291. See text accompanying notes 245-66 *supra.*

to initiate dissolution to include anyone named in the articles or any shareholders in a close corporation.

10. Shareholder Suits[292]—Security-for-expense minimums have been doubled by the New Code (from $25,000 to $50,000). Moreover, broadened indemnification provisons make it likely that management will more vigorously oppose a shareholder suit. Both of these changes could significantly deter the minority shareholder seeking to assert his interests through the judicial process.

CONCLUSION

Possibly the greatest *potential* for protecting the minority shareholders lies in the corporate articles and bylaws. Throughout this comment, suggestions have been offered for protective corporate drafting. However, the likelihood of actually seeing protective-to-minority provisions written into the articles or bylaws is probably minimal. One authority states: "Managements want freedom from bothersome stockholders, government agencies, public opinion, and judicial review. This is also what most of the corporate bar would prefer. . . ."[293] In light of such an attitude, it would be unrealistic for the minority shareholders to expect favorable drafting absent considerable pressure on their behalf.

It is more likely that the minority shareholder will have to rely upon the provisions of the California Corporations Code and upon the courts to protect his interests. To the extent that California statutory law may be moving away from shareholder protections and toward corporate management, especially with respect to the concept of majority rule, the California courts may well infer a mandate that current public policy is to give greater consideration to the majority's position—even at the expense of minority shareholders.

Ann H. Morris

292. See text accompanying notes 267-281 *supra.*
293. Cary, *supra* note 18, at 699.