Assembly Bill No. 2292

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Passed the Assembly August 25, 1998

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Chief Clerk of the Assembly

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Passed the Senate August 20, 1998

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Secretary of the Senate

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This bill was received by the Governor this ___ day

of _____, 1998, at ___ o'clock __M.

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Private Secretary of the Governor

CHAPTER ____

An act to amend Sections 301.5 and 2115 of the Corporations Code, and to amend Section 29 of Chapter 57 of the Statutes of 1996, relating to legal entities.

LEGISLATIVE COUNSEL'S DIGEST

AB 2292, Ackerman. Legal entities: organization and operation.

Existing law authorizes a listed corporation, as defined, to amend its articles or bylaws to divide its board of directors into 2 or 3 classes to serve for terms of 2 or 3 years, respectively, or to eliminate cumulative voting, or to do both of those things. Existing law also authorizes a corporation that is not a listed corporation, after the issuance of shares, to amend its articles or bylaws, to be effective when the corporation becomes a listed corporation, to divide its board of directors into 2 or 3 classes to serve for terms of 2 or 3 years, respectively, or to eliminate cumulative voting, or to do both of those things.

This bill would, among other things, provide for the elimination of those classes of directors, as specified, when the listed corporation ceases to be a listed corporation. It would also authorize shareholders of a corporation that ceases to be a listed corporation to cumulate their votes at any election of directors occurring while that corporation is not a listed corporation, notwithstanding any provision to the contrary in the corporation's articles or bylaws. This bill would also specify certain related effective dates governing when a listed corporation ceases to be a listed corporation and when a corporation that is not a listed corporation becomes a listed corporation. It would also make a change to the definition of ''listed corporation.''

Existing law provides that it is the intent of the Legislature that existing business entities, such as partnerships and corporations, be permitted to convert into or transfer real property to, limited liability

companies without incurring a documentary transfer tax provided that the direct or indirect proportionate interests in the property remain the same.

This bill would amend that provision to provide that existing business entities, such as partnerships and corporations, shall be permitted to convert into or transfer real property to, limited liability companies without incurring a documentary transfer tax, provided that the direct or indirect proportionate interests in the property remain the same.

Existing law requires a foreign corporation, as defined, to comply with various enumerated requirements and specify the times these requirements will apply, and cease to apply, to a foreign corporation.

This bill would revise those time periods.

The people of the State of California do enact as follows:

SECTION 1. Section 301.5 of the Corporations Code is amended to read:

301.5. (a) A listed corporation may, by amendment of its articles or bylaws, adopt provisions to divide the board of directors into two or three classes to serve for terms of two or three years respectively, or to eliminate cumulative voting, or both. After the issuance of shares, a corporation which is not a listed corporation may, by amendment of its articles or bylaws, adopt provisions to be effective when the corporation becomes a listed corporation to divide the board of directors into two or three classes to serve for terms of two or three years respectively, or to eliminate cumulative voting, or both. An article or bylaw amendment providing for division of the board of directors into classes, or any change in the number of classes, or the elimination of cumulative voting may only be adopted by the approval of the board and the outstanding shares (Section 152) voting as a single class, notwithstanding Section 903.

(b) If the board of directors is divided into two classes pursuant to subdivision (a), the authorized number of directors shall be no less than six and one-half of the

directors or as close an approximation as possible shall be elected at each annual meeting of shareholders. If the board of directors is divided into three classes, the authorized number of directors shall be no less than nine and one-third of the directors or as close an approximation as possible shall be elected at each annual meeting of shareholders. Directors of a listed corporation may be elected by classes at a meeting of shareholders at which an amendment to the articles or bylaws described in subdivision (a) is approved, but the extended terms for directors are contingent on that approval, and in the case of an amendment to the articles, the filing of any necessary amendment to the articles pursuant to Section 905 or 910.

(c) If directors for more than one class are to be elected by the shareholders at any one meeting of shareholders and the election is by cumulative voting pursuant to Section 708, votes may be cumulated only for directors to be elected within each class.

(d) For purposes of this section, a ‘‘listed corporation’’ means any of the following:

(1) A corporation with outstanding shares listed on the New York Stock Exchange or the American Stock Exchange.

(2) A corporation with outstanding securities designated as qualified for trading as a national market system security on the National Association Quotation System (or any successor national market system).

(e) Subject to subdivision (h), if a listed corporation having a board of directors divided into classes pursuant to subdivision (a) ceases to be a listed corporation for any reason, unless the articles of incorporation or bylaws of the corporation provide for the elimination of classes of directors at an earlier date or dates, the board of directors of the corporation shall cease to be divided into classes as to each class of directors on the date of the expiration of the term of the directors in that class and the term of each director serving at the time the corporation ceases to be a listed corporation (and the term of each director elected to fill a vacancy resulting from the death,

resignation, or removal of any of those directors) shall continue until its expiration as if the corporation had not ceased to be a listed corporation.

(f) Subject to subdivision (h), if a listed corporation having a provision in its articles or bylaws eliminating cumulative voting pursuant to subdivision (a) or permitting noncumulative voting in the election of directors pursuant to that subdivision, or both, ceases to be a listed corporation for any reason, the shareholders shall be entitled to cumulate their votes pursuant to Section 708 at any election of directors occurring while the corporation is not a listed corporation notwithstanding that provision in its articles of incorporation or bylaws.

(g) Subject to subdivision (i), if a corporation that is not a listed corporation adopts amendments to its articles of incorporation or bylaws to divide its board of directors into classes or to eliminate cumulative voting, or both, pursuant to subdivision (a) and then becomes a listed corporation, unless the articles of incorporation or bylaws provide for those provisions to become effective at some other time and, in cases where classes of directors are provided for, identify the directors who, or the directorships that, are to be in each class or the method by which those directors or directorships are to be identified, the provisions shall become effective for the next election of directors after the corporation becomes a listed corporation at which all directors are to be elected.

(h) If a corporation ceases to be a listed corporation on or after the record date for a meeting of shareholders and prior to the conclusion of the meeting, including the conclusion of the meeting after an adjournment or postponement that does not require or result in the setting of a new record date, then, solely for purposes of subdivisions (e) and (f), the corporation shall not be deemed to have ceased to be a listed corporation until the conclusion of the meeting of shareholders.

(i) If a corporation becomes a listed corporation on or after the record date for a meeting of shareholders and

prior to the conclusion of the meeting, including the conclusion of the meeting after an adjournment or postponement that does not require or result in the setting of a new record date, then, solely for purposes of subdivision (g), the corporation shall not be deemed to have become a listed corporation until the conclusion of the meeting of shareholders.

(j) If an article amendment referred to in subdivision (a) is adopted by a listed corporation, the certificate of amendment shall include a statement of the facts showing that the corporation is a listed corporation within the meaning of subdivision (d). If an article or bylaw amendment referred to in subdivision (a) is adopted by a corporation which is not a listed corporation, the provision, as adopted, shall include the following statement or the substantial equivalent: ‘‘This provision shall become effective only when the corporation becomes a listed corporation within the meaning of Section 301.5 of the Corporations Code.’’

SEC. 2. Section 2115 of the Corporations Code is amended to read:

2115. (a) A foreign corporation (other than a foreign association or foreign nonprofit corporation but including a foreign parent corporation even though it does not itself transact intrastate business) is subject to the requirements of subdivision (b) if the average of the property factor, the payroll factor, and the sales factor (as defined in Sections 25129, 25132, and 25134 of the Revenue and Taxation Code) with respect to it is more than 50 percent during its latest full income year and if more than one-half of its outstanding voting securities are held of record by persons having addresses in this state. The property factor, payroll factor, and sales factor shall be those used in computing the portion of its income allocable to this state in its franchise tax return or, with respect to corporations the allocation of whose income is governed by special formulas or that are not required to file separate or any tax returns, which would have been so used if they were governed by this three-factor formula. The determination of these factors with respect

to any parent corporation shall be made on a consolidated basis, including in a unitary computation (after elimination of intercompany transactions) the property, payroll, and sales of the parent and all of its subsidiaries in which it owns directly or indirectly more than 50 percent of the outstanding shares entitled to vote for the election of directors, but deducting a percentage of the property, payroll, and sales of any subsidiary equal to the percentage minority ownership, if any, in the subsidiary. For the purpose of this subdivision, any securities held to the knowledge of the issuer in the names of broker-dealers, nominees for broker-dealers (including clearing corporations), or banks, associations, or other entities holding securities in a nominee name or otherwise on behalf of a beneficial owner (collectively ''Nominee Holders''), shall not be considered outstanding. However, if the foreign corporation requests all Nominee Holders to certify, with respect to all beneficial owners for whom securities are held, the number of shares held for those beneficial owners having addresses (as shown on the records of the Nominee Holder) in this state and outside of this state, then all shares so certified shall be considered outstanding and held of record by persons having addresses either in this state or outside of this state as so certified, provided that the certification so provided shall be retained with the record of shareholders and made available for inspection and copying in the same manner as is provided in Section 1600 with respect to that record. A current list of beneficial owners of a foreign corporation's securities provided to the corporation by one or more Nominee Holders or their agent pursuant to the requirements of Rule 14b-1(b)(3) or 14b-2(b)(3) as adopted on January 6, 1992, promulgated under the Securities Exchange Act of 1934, shall constitute an acceptable certification with respect to beneficial owners for the purposes of this subdivision.

(b) Except as provided in subdivision (c), the following chapters and sections of this division shall apply to a foreign corporation as defined in subdivision (a) (to

the exclusion of the law of the jurisdiction in which it is incorporated):

Chapter 1 (general provisions and definitions), to the extent applicable to the following provisions;

Section 301 (annual election of directors);

Section 303 (removal of directors without cause);

Section 304 (removal of directors by court proceedings);

Section 305, subdivision (c) (filling of director vacancies where less than a majority in office elected by shareholders);

Section 309 (directors' standard of care);

Section 316 (excluding paragraph (3) of subdivision (a) and paragraph (3) of subdivision (f)) (liability of directors for unlawful distributions);

Section 317 (indemnification of directors, officers, and others);

Sections 500 to 505, inclusive (limitations on corporate distributions in cash or property);

Section 506 (liability of shareholder who receives unlawful distribution);

Section 600, subdivisions (b) and (c) (requirement for annual shareholders' meeting and remedy if same not timely held);

Section 708, subdivisions (a), (b), and (c) (shareholder's right to cumulate votes at any election of directors);

Section 710 (supermajority vote requirement);

Section 1001, subdivision (d) (limitations on sale of assets);

Section 1101 (provisions following subdivision (e)) (limitations on mergers);

Chapter 12 (commencing with Section 1200) (reorganizations);

Chapter 13 (commencing with Section 1300) (dissenters' rights);

Sections 1500 and 1501 (records and reports);

Section 1508 (action by Attorney General);

Chapter 16 (commencing with Section 1600) (rights of inspection).

(c) This section does not apply to any corporation (1) with outstanding securities listed on the New York Stock Exchange or the American Stock Exchange, or (2) with outstanding securities designated as qualified for trading as a national market security on the National Association of Securities Dealers Automatic Quotation System (or any successor national market system) if the corporation has at least 800 holders of its equity securities as of the record date of its most recent annual meeting of shareholders, or (3) if all of its voting shares (other than directors' qualifying shares) are owned directly or indirectly by a corporation or corporations not subject to this section. For purposes of determining the number of holders of a corporation's equity securities under clause (2) of this subdivision, there shall be included, in addition to the number of recordholders reflected on the corporation's stock records, the number of holders of the equity securities held in the name of any Nominee Holder that furnishes the corporation with a certification pursuant to subdivision (a) provided that the corporation retains the certification with the record of shareholders and makes it available for inspection and copying in the same manner as is provided in Section 1600 with respect to that record.

(d) For purposes of subdivision (a), the requirements of subdivision (b) shall become applicable to a foreign corporation only upon the first day of the first income year of the corporation (i) commencing on or after the 135th day of the income year immediately following the latest income year with respect to which the tests referred to in subdivision (a) have been met or (ii) commencing on or after the entry of a final order by a court of competent jurisdiction declaring that those tests have been met.

(e) For purposes of subdivision (a), the requirements of subdivision (b) shall cease to be applicable to a foreign corporation (i) at the end of the first income year of the corporation immediately following the latest income year with respect to which at least one of the tests referred to in subdivision (a) is not met or (ii) at the end of the

income year of the corporation during which a final order has been entered by a court of competent jurisdiction declaring that one of those tests is not met, provided that a contrary order has not been entered before the end of the income year.

SEC. 3. Section 29 of Chapter 57 of the Statutes of 1996 is amended to read:

Sec. 29. Existing business entities, such as partnerships and corporations, shall be permitted to convert into or transfer real property to, limited liability companies without incurring a documentary transfer tax, provided that the direct or indirect proportionate interests in the property remain the same.

Approved _____, 1998

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Governor