

Memorandum 76-37

Subject: Study 77.160 - Nonprofit Corporations (Rights of Inspection)

Attached to this memorandum is a staff draft of Chapter 16 (Rights of Inspection) of the new General Nonprofit Corporation Law. The staff draft is based on Chapter 16 of the new General Corporation Law. The important departures from the General Corporation Law are the following:

1. Continues the provision for inspection of membership records of the nonprofit corporation, regardless of whether the inspection is for a "purpose reasonably related" to the member's interests as a member if the member has the written authorization of at least five percent of the voting power (Sections 6620, 6622) but allows the bylaws to specify a lesser authorization (Section 6620).

2. Allows the nonprofit corporation to avoid disclosure of its membership list (Section 6622) to a member having the written authorization of five percent of the voting power by adopting a bylaw giving such member the right to communicate with members at corporate expense (Section 6621). This provision is new and is included to permit the nonprofit corporation to protect its membership list by adopting such a bylaw. See Exhibit I (attached).

3. Specifically provides that the power of the court to ensure a "fair and equitable" procedure for the nomination and election of directors is not limited by the statutory provisions (Section 6623).

4. When judicial enforcement of the right of inspection is sought, places the burden of establishing the right to such inspection on the member seeking it (Section 6650).

5. Expands the venue for judicial enforcement to include the county where any of the books, records, or documents are located (Section 6650).

6. Limits the right to recover reasonable expenses and attorney's fees to cases where noncompliance by the nonprofit corporation with a proper demand was "arbitrary" and "completely" without justification (Section 6651).

These departures from General Corporation Law are significant, both in policy and drafting. Accordingly, the staff submits Chapter 16 to the Commission for discussion and resolution of the policy issues presented rather than as a finished draft for approval.

Respectfully submitted,

Robert J. Murphy III
Legal Counsel

Memorandum 76-37

EXHIBIT I

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March 8, 1976

John H. DeMouilly
Executive Secretary
California Law Revision Commission
Stanford Law School
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Nonprofit Corporations
Study 77.160

Dear Mr. DeMouilly:

Addressing Article 2 of Chapter 16, a problem comes to mind which should be dealt with, and is worthy of accommodation.

It seems clear that members should be offered a reasonable method of communication with other members at the member's expense, e. g., re a proxy contest with respect to election of directors; and, this is a reasonable objective of the law.

At the same time, the list of names and addresses of the members of an organization may constitute an extremely valuable trade secret which should be protected from abuse, for the benefit of all of the members. This should be equally clear, and an equally reasonable objective of the statute.

In a small organization, manual or other copying of a membership list might be an entirely appropriate way of accommodating the first objective, and in many organizations the second might not be a problem.

In a very large organization, copying the membership list would probably be an unsatisfactory way of achieving the first objective; but, if accomplished could very well jeopardize the second, as would mechanical or other machine reproduction.

In view of the vast number of nonprofit corporations, and the almost infinite variety of their natures, purposes, sizes, presence or absence of proprietary interests, and demographics of the members, the Commission should not attempt to prescribe exclusive, mandatory procedures. Rather, it would seem appropriate to afford alternatives, e. g., provide that a nonprofit corporation may, in lieu of the specific requirements, develop, adopt and implement procedures which are fair, just and reasonable under the circumstances and the nature of the particular organization, and which afford satisfaction of the first

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objective, yet retain the protection of the membership list from abuse and exploitation, thereby satisfying the second.

Sincerely,

A handwritten signature in black ink, appearing to read "Wells A. Hutchins", with a large, sweeping flourish at the end.

Wells A. Hutchins

WAH/hb

PENNSYLVANIA NONPROFIT CORPORATION LAW

§ 7508. Corporate records; inspection

(a) **Required records.**—Every nonprofit corporation shall keep an original or duplicate record of the proceedings of the members and the directors, and of any other body exercising powers or performing duties which under this article may be exercised or performed by such other body, the original or a copy of its bylaws, including all amendments thereto to date, certified by the secretary of the corporation, and an original or a duplicate membership register, giving the names of the members, and showing their respective addresses and the class and other details of the membership of each. Every such corporation shall also keep appropriate, complete and accurate books or records of account. The records provided for in this subsection shall be kept at either the registered office of the corporation in this Commonwealth or at its principal place of business wherever situated.

(b) **Right of inspection.**—Every member shall, upon written demand under oath stating the purpose thereof, have a right to examine, in person or by agent or attorney, during the usual hours for business for any proper purpose, the membership register, books and records of account, and records of the proceedings of the members, directors and such other body, and to make copies or extracts therefrom. A proper purpose shall mean a purpose reasonably related to the interest of such person as a member. In every instance where an attorney or other agent shall be the person who seeks the right to inspection, the demand under oath shall be accompanied by a power of attorney or such other writing which authorizes the attorney or other agent to so act on behalf of the member. The demand under oath shall be directed to the corporation at its registered office in this Commonwealth or at its principal place of business wherever situated.

(c) **Proceedings for the enforcement of inspection.**—If the corporation, or an officer or agent thereof, refuses to permit an inspection sought by a member or attorney or other agent acting for the member pursuant to subsection (b) of this section or does not reply to the demand within five business days after the demand has been made, the member may apply to the court for an order to compel such inspection. The court shall determine whether or not the person seeking inspection is entitled to the inspection sought. The court may summarily order the corporation to permit the member to inspect the membership register and the other books and records of the corporation and to make copies or extracts therefrom; or the court may order the corporation to furnish to the

member a list of its members as of a specific date on condition that the member first pay to the corporation the reasonable cost of obtaining and furnishing such list and on such other conditions as the court deems appropriate. Where the member seeks to inspect the books and records of the corporation, other than its membership register or list of members, he shall first establish:

(1) that he has complied with the provisions of this section respecting the form and manner of making demand for inspection of such document; and

(2) that the inspection he seeks is for a proper purpose.

Where the member seeks to inspect the membership register or list of members of the corporation and he has complied with the provisions of this section respecting the form and manner of making demand for inspection of such documents, the burden of proof shall be upon the corporation to establish that the inspection he seeks is for an improper purpose. The court may, in its discretion, prescribe any limitations or conditions with reference to the inspection, or award such other or further relief as the court may deem just and proper. The court may order books, documents and records, pertinent extracts therefrom, or duly authenticated copies thereof, to be brought within this Commonwealth and kept in this Commonwealth upon such terms and conditions as the order may prescribe.

Rough Outline

GENERAL NONPROFIT CORPORATION LAW

CHAPTER 16. RIGHTS OF INSPECTION

Article 1. General Provisions

- § 6610. Rights may not be limited by articles or bylaws
- § 6611. Inspection by agent or attorney; right to copy and make extracts
- § 6612. Records to be made available in written form

Article 2. Membership Records

- § 6620. Authorized member defined
- § 6621. Adoption of bylaw providing procedure for communicating to members
- § 6622. Right to inspect and obtain membership record
- § 6623. Application of article
- § 6624. Authority of court not limited

Article 3. Books, Records, and Minutes

- § 6630. Inspection of books, records, and minutes
- § 6631. Application of article

Article 4. Director's Rights of Inspection

- § 6640. Director's right to inspect and copy
- § 6641. Application of article

Article 5. Judicial Enforcement

- § 6650. Enforcement of right of inspection; appointment of inspectors or accountants
- § 6651. Recovery of reasonable expenses by member or director

CHAPTER 16. RIGHTS OF INSPECTION

Article 1. General Provisions§ 6610. Rights may not be limited by articles or bylaws

6610. The rights provided in this chapter may not be limited by the articles or bylaws.

Comment. Section 6610 is based on comparable provisions in Sections 1600(d) and 1601(b). Although no comparable provision is found in Section 1602, it appears that there was no intent that the rights given directors by that section could be limited by the articles or bylaws. Section 6610 makes clear that the rights of inspection given directors cannot be limited in the articles or bylaws.

§ 6611. Inspection by agent or attorney; right to copy and make extracts

6611. Inspection under this chapter may be made in person or by agent or attorney. The right of inspection includes the right to copy and make extracts.

Comment. Section 6611 is the same as comparable provisions in Sections 1600, 1601, and 1602.

§ 6612. Records to be made available in written form

6612. If any record subject to inspection pursuant to this chapter is not maintained in written form, a request for inspection is not complied with unless and until the nonprofit corporation at its expense makes such record available in written form.

Comment. Section 6612 is the same in substance as Section 1605.

Article 2. Membership Records

§ 6620. Authorized member defined

6620. As used in this article, "authorized member" means a member having the written authorization of at least five percent of the voting power or such lesser authorization as is specified in the bylaws.

Comment. Section 6620 adopts the five-percent requirement of Section 1600 (General Corporation Law) but permits a lesser authorization to be specified in the bylaws.

§ 6621. Adoption of bylaw providing procedure for communicating to members

6621. (a) As used in this section:

(1) "Candidate's statement" means a statement of not more than 200 words, or such greater number of words as may be provided in the bylaw, giving biographical information for and a statement of the views of the nominee or person sought to be nominated.

(2) "Nominee" means any person who has been nominated, by petition or otherwise, for election as a director.

(3) "Proxy solicitation statement" means a statement of not more than 300 words, or such greater number of words as may be provided in the bylaw, soliciting the proxies of members.

(4) "Voting members" means the members of the nonprofit corporation entitled to vote for directors.

(b) Unless the bylaws require that it be adopted by the members, the board may adopt a bylaw pursuant to this section.

(c) A bylaw adopted pursuant to this section shall, at a minimum, include all of the following:

(1) A statement that the bylaw is adopted pursuant to this section.

(2) A procedure to permit an authorized member to communicate with the voting members, without cost to the authorized member, for the purpose of seeking support for the nomination of any member or members for election as directors of the nonprofit corporation. The authorized member shall be permitted to communicate the name, together with a candidate's statement, for each member so sought to be nominated. The number so sought to be nominated by an authorized member shall not exceed the number of positions to be filled at the next election of directors.

(3) A procedure to permit any nominee to communicate to the voting members, without cost to the nominee, a candidate's statement for the nominee.

(4) If the nonprofit corporation permits the use of proxies in voting for directors, a procedure to permit an authorized member to communicate with the voting members, without cost to the authorized member, for the purpose of soliciting proxies. The authorized member shall be permitted to communicate a proxy solicitation statement and a proxy form to be returned, at the expense of the member giving the proxy, by a member who desires to give a proxy to the authorized member.

(d) If a bylaw is adopted pursuant to this section, the limitations as to the number of words permitted in a candidate's statement or proxy

solicitation statement apply to all such statements, whether sent on behalf of the nonprofit corporation, its management, or an authorized member or nominee.

(e) No candidate's statement or proxy solicitation statement may be altered or modified by the nonprofit corporation without the written consent of the person submitting the statement except to eliminate matter which in the opinion of independent counsel would likely result in the imposition of liability on the nonprofit corporation, such as matter which is libelous.

(f) The procedure provided in the bylaw for communicating with the voting members may include a separate mailing, inclusion in a publication mailed to voting members, or any other method whereby substantially all of the voting members receive the communication.

(g) The bylaw may provide that Section 6622 does not apply to the nonprofit corporation.

Comment. Section 6621, which is new, permits a nonprofit corporation to adopt a bylaw to provide a procedure for communicating to voting members. If such a procedure is provided, the nonprofit corporation may refuse to permit inspection and copying of its membership list. See subdivision (g). This will permit a nonprofit corporation that considers its membership list to be a valuable trade secret, for example, to protect the membership list from possible improper use.

The bylaw may be adopted by the board unless the bylaws require that it be adopted by the members. See subdivision (b). The minimum requirements for the bylaw are stated in subdivision (c).

§ 6622. Right to inspect and obtain membership record

6622. (a) This section does not apply to a nonprofit corporation which:

(1) Has adopted a bylaw which (i) satisfies the requirements of Section 6621 and (ii) includes a provision making this section not applicable to the nonprofit corporation; and

(2) Is complying with the provisions of the bylaw adopted pursuant to Section 6621.

(b) As used in this section, "membership record" means the record required by subdivisions (c) and (d) of Section 6510.

(c) Every member has the right to inspect the membership record during usual business hours upon five business days' prior written demand upon the nonprofit corporation for a purpose reasonably related to such member's interests as a member. The written demand shall be under oath and shall state the purpose of the inspection.

(d) An authorized member has the absolute right to do either or both of the following:

(1) Inspect the membership record during usual business hours upon five business days' prior written demand upon the nonprofit corporation.

(2) Obtain from the nonprofit corporation, upon five business days' prior written demand, a list of the members entitled to vote for directors, showing the name and address of each such member, the class of membership held by the member if there are classes of members entitled to vote for director, and the number of memberships held by the member, as of the most recent record date for which such a list has been compiled or as of a date specified by the authorized member subsequent to

the date of the demand. The nonprofit corporation may require, as a condition of obtaining the membership list, that the demand be accompanied by a tender of a reasonable charge specified by the nonprofit corporation, not in excess of an amount equal to five cents for each name to be so provided or the actual cost to the nonprofit corporation of furnishing the list, whichever is the lesser amount.

(e) Any delay by the nonprofit corporation in complying with a demand under subdivision (d) beyond the time limits specified in that subdivision shall give the authorized member properly making the demand, and paying the amount, if any, required by the nonprofit corporation as a condition of providing the membership list, a right to obtain from the superior court, upon the filing of a verified complaint in the proper county and after a hearing, notice of which shall be given to such persons and in such manner as the court may direct, an order postponing any meeting of the members previously noticed for a period equal to the period of such delay. This right is in addition to any other legal or equitable remedies to which the authorized member may be entitled.

Comment. Section 6622 does not apply to a nonprofit corporation which has adopted a bylaw pursuant to Section 6621, which satisfies the requirements of that section and makes Section 6622 not applicable to the nonprofit corporation.

Subdivision (c) is the same in substance as subdivision (c) of Section 1600 (General Corporation Law) except that (1) the nonprofit corporation is given five business days to comply with the demand for inspection and (2) the demand must be under oath and state the purpose of the inspection.

Subdivision (d) is based on subdivision (a) of Section 1600. Subdivision (d), however, allows the nonprofit corporation to require the member to pay a reasonable charge, not to exceed the lesser of five

cents per name or the actual cost to the nonprofit corporation of furnishing the information rather than referring to "its usual charges for such a list."

Subdivision (e) is the same in substance as subdivision (b) of Section 1600.

992/902

§ 6623. Application of article

6623. This article applies to any domestic nonprofit corporation and to any foreign nonprofit corporation keeping its record of members or a duplicate thereof in this state or having its principal executive office in this state.

Comment. Section 6623 is the same in substance as the last sentence of subdivision (d) of Section 1600. The application of this article is not limited to foreign nonprofit corporations described in Section 6623. See Section [provision comparable to Section 2115].

405/802

§ 6624. Authority of court not limited

6624. Nothing in this article limits the authority of the court to prescribe a different procedure that includes additional requirements, limitations, or conditions, including a lesser percentage of voting power to qualify as an authorized member for the purposes of this arti-

cle, as the court determines are necessary to provide a procedure for the nomination and election of directors that is fair and equitable in view of the circumstances, practices, and nature of the particular nonprofit corporation.

Comment. Section 6624 recognizes the power of the court to determine that electoral procedures for directors are unfair and unlawful and as a court of equity to require the nonprofit corporation to put into effect such electoral process as the court may consider just and proper under the circumstances of the particular case. See Braude v. Havenner, 38 Cal. App.3d 526, 113 Cal. Rptr. 386 (1974).

Article 3. Books, Records, and Minutes

§ 6630. Inspection of books, records, and minutes

6630. The books and records of account and minutes of proceedings of the members and the board and committees of the board of a nonprofit corporation shall be open to inspection by any member during usual business hours upon five business days' prior written demand for a purpose reasonably related to such member's interests as a member. The written demand shall be under oath and shall state the purpose of the inspection.

Comment. Section 6630 is based on subdivision (a) of Section 1601 (General Corporation Law). The requirement that the demand be under oath and state the purpose of the inspection is taken from Pennsylvania nonprofit corporation law. See Pa. Stat. Ann. tit. 15, § 7508(b)(1972). The requirement that the nonprofit corporation be given five business days to comply with the demand is not found in the comparable provision of the General Corporation Law, but it is included here to permit the nonprofit corporation time to determine whether the demand is for a proper purpose and to schedule the inspection so that there will be a minimum disruption of its office personnel.

§ 6631. Application of article

6631. This article applies to a domestic nonprofit corporation, to a foreign nonprofit corporation having its principal executive office in this state, and to any other foreign nonprofit corporation with respect

to books or records actually or customarily located in this state.

Comment. Section 6631 is based on a portion of subdivision (a) of Section 1601 (General Corporation Law). The application of this article is not limited to foreign nonprofit corporations described in Section 6631. See Section [provision comparable to Section 2115].

Policy Issue:

Should this section be phrased like Section 6641? Recommendation:
Yes.

Article 4. Director's Rights of Inspection

§ 6640. Director's right to inspect and copy

6640. Every director of a nonprofit corporation has the absolute right at any reasonable time to inspect and copy all books, records, and documents of every kind and to inspect the physical properties of the nonprofit corporation.

Comment. Section 6640 is the same in substance as the first sentence of Section 1602 (General Corporation Law).

§ 6641. Application of article

6641. This article applies to all of the following:

- (a) A domestic nonprofit corporation.
- (b) A foreign nonprofit corporation having its principal executive office in this state.
- (c) A foreign nonprofit corporation subject to Section [provision comparable to Section 2115].
- (d) Any other foreign nonprofit corporation with respect to such books, records, documents, and properties as are actually or customarily located in this state.

Comment. Section 6641 is similar to the second sentence of Section 1602 (General Corporation Law) except that Section 6641 gives the director a broader right of inspection with respect to foreign nonprofit corporations than Section 1602. Unlike Section 1602, in the case of a foreign corporation described in subdivision (b) or (c) of Section 6041, the director may inspect books, records, documents, and properties wherever they may be located. Compare Section 1602.

Article 5. Judicial Enforcement

§ 6650. Enforcement of right of inspection; appointment of inspectors or accountants

6650. (a) Upon refusal of, or noncompliance with, a proper demand for inspection, the superior court of the proper county or of the county in which any of the books, records, documents, or property is located may enforce the right of inspection provided in this chapter with just and proper conditions. When inspection is sought by a member pursuant to subdivision (c) of Section 6622 or Section 6630, such member has the burden of establishing that the inspection is for a proper purpose.

(b) The court may, for good cause shown, appoint one or more competent inspectors or accountants to audit the books and records and to investigate the property, funds, and affairs of the nonprofit corporation if such books, records, property, funds, and affairs are subject to inspection under this chapter. The court may direct such inspectors or accountants to report thereon in such manner as the court may direct.

(c) All officers and agents of the nonprofit corporation shall produce to the inspectors or accountants so appointed all books and documents subject to inspection which are in their custody or under their control under penalty of punishment for contempt of court for willful noncompliance.

(d) All expenses of the investigation or audit shall be defrayed by the applicant unless the court orders them to be paid or shared by the nonprofit corporation.

Comment. Section 6650 is based on Section 1603 (General Corporation Law). Section 6650 expands the venue of Section 1603 to include

the county where "any of the documents sought are located whether the nonprofit corporation is domestic or foreign. When inspection is sought by a member, the member has the burden of establishing the right to such inspection.

Under subdivision (b), the court's power to appoint inspectors or accountants is in addition to its other powers.

Subdivisions (c) and (d) are the same in substance as subdivisions (b) and (c), respectively, of Section 1603.

405/926

§ 6651

§ 6651. Recovery of reasonable expenses by member or director

6651. In any action or proceeding under this chapter, if the court finds the failure of the nonprofit corporation to comply with a proper demand thereunder was arbitrary and completely without justification, the court may award an amount sufficient to reimburse the member or director for the reasonable expenses, including reasonable attorney's fees, incurred in connection with such action or proceeding.

Comment. Section 6651 is based on Section 1604 (General Corporation Law). Section 6651 requires that the noncompliance by the nonprofit corporation be "arbitrary" and "completely" without justification but extends the right to recover reasonable expenses to directors who seek to enforce rights of inspection pursuant to Section 6640.

Policy Issue:

Is the standard "arbitrary and completely without justification" appropriate? Recommendation: Yes.