

Memorandum 76-70

Subject: Study 77.330 - Nonprofit Corporations (Conforming Changes--
Cooperative and Mutual Corporations)

This memorandum considers the subject of cooperative corporations and proposes several conforming changes. Attached as Exhibit I is a copy of the Cooperative Corporation Law, Part 2 (commencing with Section 12200) of Division 3 of Title 1 of the Corporations Code. Also attached is a draft of conforming changes suggested by the staff.

I. COOPERATIVE CORPORATIONS

Background

Nature of cooperative corporations. Cooperative corporations are a distinct form of organization. A cooperative corporation may be organized with shares or with memberships or both. The shareholders or members characteristically have a common interest in marketing or purchasing products, and the corporation is democratically controlled (i.e., frequently one vote per shareholder or member), may pay interest on investments in a limited amount (five or eight percent in California), and may return net profits to the members in the form of limited dividends per share or membership on the basis of their participation in the activities of the cooperative. See U.S. Bureau of Labor Statistics, Dep't of Labor, Bull. No. 1211, Consumer Cooperatives 2 (1957).

Cooperatives resemble nonprofit corporations in that they are frequently membership organizations and the cooperative does not seek a profit for itself. Hence, Section 54033 of the Food and Agricultural Code states that agricultural cooperatives are "'nonprofit', since they are not organized to make profit for themselves, as such, or for their members, as such, but only for their members as producers." For a similar section, see Corp. Code § 13203 (fish marketing cooperatives). Despite these statutory exhortations, it is generally understood that cooperatives are a variety of business entity. See, e.g., Jensen, et. al., Report of Part of the Committee on Classification and Terminology, 1949, in Cooperative Corporate Association Law--1950, at 75-76 (American Institute of Cooperation 1950), Jaenke, Cooperatives: The Clear Alternative, in Proceedings of the National Symposium on Cooperatives and

the Law 2-3 (Madison, Wisc., April 23-25, 1974); Couper, Organizing Cooperatives, in California Farm & Ranch Law § 11.1 (Cal. Cont. Ed. Bar 1967). New York and Pennsylvania, which both have enacted modern non-profit corporation laws, placed cooperatives under the business corporation law or corporation for profit law rather than under the nonprofit corporation law.

Cooperatives may be exempt from income taxes. Section 521 of the Internal Revenue Code of 1954 provides an exemption for farmers' cooperative organizations. One qualification for the exemption is that organizations having capital stock may not pay dividends exceeding the state's legal rate of interest or eight percent, whichever is greater. Exemptions are also provided for certain credit unions, cooperative banks, mutual savings banks, and mutual insurance companies. Int. Rev. Code of 1954, § 501(c)(14), (15).

California statutes. California has three significant statutes pursuant to which cooperatives may be formed:

1. Cooperative corporations. Corporations Code Sections 12200-12956 (a copy of these provisions is attached as Exhibit I), Part 2 of Division 3 of Title 1, relates to cooperative corporations "composed of ultimate producers or consumers, or both, organized for the purpose of conducting any lawful business primarily for the mutual benefit of its shareholders." This law will be referred to in this memorandum as the Cooperative Corporation Law.

2. Fish marketing cooperatives. The Fish Marketing Act, Corporations Code Sections 13200-13356 (Part 3, Division 3, Title 1), provides for the organization of "associations" of persons engaged in the production of fishery products.

3. Agricultural cooperatives. Food and Agricultural Code Sections 54001-54294 (Chapter 1, Division 20) provides for the formation of "associations" of producers of farm products. The chapter is entitled "nonprofit cooperative associations"; this memorandum will refer to such corporations as agricultural cooperatives.

These bodies of law are largely self-sufficient; however, they each incorporate portions of other laws. The Agricultural Cooperative Law and the Fish Marketing Act incorporate only the General Corporation Law.

The Cooperative Corporation Law incorporates both the General Corporation Law and the General Nonprofit Corporation Law. Of course, where each of these special laws contains provisions that vary from the provisions found in the general laws, the special provisions prevail.

While there are many similar or identical provisions in the three cooperative corporation laws, each has its unique provisions. Accordingly, it is difficult to generalize when it comes to describing the detailed provisions governing cooperative corporations. The state of the law is all the more confusing when the enactment of the new General Corporation Law and the prospective enactment of a new General Nonprofit Corporation Law are taken into account. The extent of necessary or advisable conforming revisions to be included in the Commission's recommendation is a difficult and complex matter to decide.

Ideally, the entire subject of cooperative corporations should receive separate study. Of course, that is not a topic specifically included on the Commission's agenda and would be a substantial and important undertaking. However, we should do something about the Cooperative Corporation Law inasmuch as it incorporates the existing General Nonprofit Corporation Law, which we plan to repeal. It is arguable that the Commission study should cover the other major cooperative laws since they declare by statute that they are of a nonprofit nature.

Staff Recommendations

Agricultural cooperatives and fish marketing cooperatives. The staff recommends that the laws relating to agricultural cooperatives and fish marketing cooperatives be left alone since they do not incorporate the General Nonprofit Corporation Law. This means that they will continue to operate under their own law and, to the extent incorporated or generally applicable, they will be governed by the old General Corporation Law in effect on December 31, 1976. See Assembly Bill 2349, § 43.5, proposing to amend Cal. Stats. 1975, Ch. 682, § 16; Assembly Bill 2849, § 1.3, proposing to amend Corp. Code § 102, as enacted by Cal. Stats. 1975, Ch. 682, § 7 (operative Jan. 1, 1977). (We would also leave Civil Code Sections 653aa and 653ee untouched. These sections, leftovers from the 1923 act that was codified in the Agricultural Code in 1933, are almost identical to Sections 54031 and 54032 of the Food and Agricultural Code.)

Cooperative corporations under Corporations Code. The decision regarding cooperative corporations under Part 2 of Division 3 of Title 1 of the Corporations Code is more complicated. Section 12205 provides that Division 2 (the General Nonprofit Corporation Law) applies to cooperative corporations formed under Part 2 absent a conflicting provision in Part 2. Section 12206 provides for an amendment of articles in the manner provided in the General Corporation Law by a corporation desiring to be governed by Part 2. Section 12900 provides that a cooperative corporation may amend its articles in the manner prescribed by the General Corporation Law. The remainder of Part 2 does not incorporate any other law. The existing General Nonprofit Corporation Law refers over to the General Corporation Law, thus picking up provisions applicable to cooperative corporations that have shareholders. This feature of the old General Corporation Law will be eliminated in the new law, which will apply only to membership corporations.

Other than a complete revision of this area of the law, the staff notes the following alternative dispositions of the Cooperative Corporation Law:

1. Leave cooperative corporations under the old General Nonprofit Corporation Law. The obvious drawbacks of this alternative are that two nonprofit corporation laws remain in force for different types of corporations and that practitioners have to retain old codes. One goal of the staff is to repeal the existing General Nonprofit Corporation Law and to have no corporation thereafter subject to the repealed statute. This alternative would defeat that goal. The benefits of this alternative are that the law governing cooperative corporations remains the same and that any unforeseen or undesirable consequences of putting them under a different body of law are avoided. There will accordingly be some impetus for those interested in cooperative corporations to revise the law in order to avoid the need to refer to the repealed statute.

2. Put cooperative corporations under the existing General Corporation Law. This alternative, like the first, would require the retention of old codes after the new General Corporation Law goes into effect. It may have some undesirable consequences as well. However, it should be remembered that, although cooperative corporations are now under the existing General Nonprofit Corporation Law, Section 9002 of

the General Nonprofit Corporation Law incorporates the provisions of the General Corporation Law. Hence, in many respects, cooperative corporations are now governed by the General Corporation Law. To directly incorporate the existing General Corporation Law would continue this feature and make the Cooperative Corporation Law consistent with the Agricultural Cooperative Law and the Fish Marketing Act, both of which incorporate the old General Corporation Law. The existing General Nonprofit Corporation Law would cease to have any force.

3. Put cooperative corporations under the new General Corporation Law.

(a) Without making any technical revisions. If one believes that all cooperative corporations should be governed by the business corporation laws and that the new General Corporation Law is an improvement over the old law, this alternative has considerable appeal. However, the mere substitution of a reference to the new General Corporation Law might have unanticipated consequences. Does it make sense to put cooperative corporations under the new General Corporation Law without making technical amendments in the Cooperative Corporation Law to conform it to the new law to the extent that the unique provisions in the Cooperative Corporation Law are merely reflections of provisions the old General Corporation Law that were not retained and are not important to cooperative corporations?

(b) With technical revisions. The problem with proceeding through the Cooperative Corporation Law at this stage in an attempt to conform it to the new General Corporation Law is that it would be a substantial undertaking to determine what changes should be made. For example, Section 12400 requires five or more incorporators--Section 200 requires only one; Section 12401 requires the articles to state the names and addresses of the subscribers for shares--no such provision appears in the new law; Section 12402 requires the articles to state the par value of shares if they have any--Section 205 has a different rule; Section 12600 permits a majority of shareholders to remove directors--Section 303 provides much more complex rules.

4. Put cooperative corporations without shares under the new General Nonprofit Corporation Law and cooperative corporations with shares under the new General Corporation Law. This alternative too

would be a substantial undertaking, an undertaking that would be even more difficult than alternative 3(b).

The staff seeks guidance from the Commission before proceeding further on this matter.

Electrical cooperatives. The provisions in the Public Utilities Code relating to electrical cooperatives, Sections 2781-2783 (as added by Cal. Stats. 1975, Ch. 451, § 1--different sections with the same numbers were enacted at the same session), merely recognize the existence of such corporations "organized for the purposes of transmitting or distributing electricity exclusively to its stockholders or members at cost" and provide certain exceptions from the regulatory authority of the Public Utilities Commission. No amendment is needed.

II. MUTUAL CORPORATIONS

Background

The term "cooperative corporation" is imprecise. In the first part of this memorandum, it was used to describe corporations organized under Part 2 of Division 3 of Title 1 of the Corporations Code. However, features which distinguish these cooperatives are also characteristic of corporations organized on a mutual basis--typically financial, insurance, and utility companies. See U.S. Bureau of Labor Statistics, Dep't of Labor, Bull. No. 1211, Consumer Cooperatives, passim (1957).

As indicated in the background discussion in the first part of this memorandum, tax exemptions may be available to certain types of mutual companies, including credit unions.

We have found the following references to mutual companies in California statutes:

1. Mutual water companies are provided for in Civil Code Section 330.24, Corporations Code Sections 502(a) and 708(d) (in the new General Corporation Law), and Public Utilities Code Sections 2702, 2705, and 2725 et seq.

2. Mutual savings and loan associations are recognized in Financial Code Section 5502 which provides that the word "mutual" shall not be used in the name of any association organized after 1931 unless it is organized without stock. However, the law relating to borrowers' mutual

savings and loan associations, Financial Code Sections 10000-10609, was repealed in 1971. The information we obtained from the Department of Savings and Loan is that it has been a very long time since they have received any applications for the formation of mutual savings and loan associations but that, if an application were received, they would have to evaluate it on an individual basis. In any event, Financial Code Section 5500 provides that associations have the "powers and privileges provided by the General Corporation Law" except where the Savings and Loan Association Law is inconsistent.

3. Credit unions (Fin. Code §§ 14000-16000) are described by Section 14000 as "cooperative" corporations "organized for the purposes of promoting thrift among its members and creating a source of credit for them at legal rates of interest for provident purposes." However, the Cooperative Corporation Law (Corp. Code § 12200 et seq.) is not incorporated by reference. Two sections refer to the General Corporation Law. See Sections 14200 (credit unions incorporated under Credit Union Law in the same manner as corporations under the General Corporation Law except as otherwise provided), 14807 (credit union has general powers conferred upon corporations by the General Corporation Law unless restricted).

4. Mutual insurers include general mutual insurers (Ins. Code § 4010 et seq.), county mutual fire insurers (Ins. Code § 5050 et seq.), county mutual fire reinsurers (Ins. Code § 7080 et seq.), and general mutual life and disability insurers (Ins. Code § 10442). Apparently, these mutual insurers are governed for certain purposes by the General Corporation Law. See Ins. Code §§ 1140 (except as otherwise provided, incorporated insurers subject to provisions of the general corporation law), 4012 (Section 1140 applies to general mutual insurers except that provisions of "Corporation Law referring to shareholders or members shall be applied as though such provisions referred to the policyholders or members of a mutual"), 4090 (merger provisions of General Corporation Law, § 4300 et seq., not applicable to merger of mutual insurers), 5053 (county mutual fire insurers file articles in conformity with Corp. Code § 303), 5080 (county mutual fire insurers have "usual powers" and are subject to "usual duties" of corporations), 7040 (merger of county

mutual fire insurers notwithstanding Corp. Code § 3602), 7046 (transformation to general mutual insurer notwithstanding Corp. Code § 3602), 7083 (articles of county mutual fire reinsurer acknowledged as required by the "general corporation law"), 8011 ("usual powers," "usual duties"), 10442 (domestic mutual life or disability insurer governed by Division 1 of Title 1 of the Corporations Code), and 11529 (filing articles pursuant to Corp. Code § 3670 et seq. in acquisition of stock in conversion of reserve insurer with capital stock to mutual insurer).

5. Fraternal insurers include fraternal fire insurers (Ins. Code § 9080 et seq.), fraternal benefit societies (Ins. Code § 10970 et seq.), and firemen's, policemen's, or peace officers' benefit and relief associations (Ins. Code § 11400 et seq.). These corporations or associations are mutual in nature and are declared to be nonprofit or charitable. See Fin. Code §§ 9081, 9090 (fraternal fire insurers bind themselves to contribute to each other's loss by fire), 9096 (fraternal fire insurers declared to be charitable and benevolent institutions exempt from taxes), 10990 (fraternal benefit society is conducted solely for benefit of its members and not for profit), and 10993 (fraternal benefit society declared to be charitable and benevolent institution exempt from taxes); see also Fin. Code §§ 11400 (purpose of benefit and relief associations), 11402 (incorporated benefit and relief associations may not issue shares of stock), and 11406 (benefits only to members and beneficiaries).

Staff Recommendations

The provisions concerning mutual water companies in the Civil Code should be relocated in the part of the Public Utilities Code where it deals with water companies. (See the attached draft of conforming changes.)

No amendments are needed to deal with mutual savings and loan associations, credit unions, or mutual insurers since they are governed either by their particular laws or the General Corporation Law. Needed amendments should be made by the persons affected by these laws or by those in charge of amending the General Corporation Law.

The law relating to fraternal insurers does not specifically incorporate the General Nonprofit Corporation Law; the general nature of

these insurers and the cross-references contained in the annotated code indicate that they would be governed, where appropriate, by the law relating to nonprofit corporations. The staff does not recommend that we attempt to clarify this situation.

Respectfully submitted,

Stan G. Ulrich
Staff Counsel

EXHIBIT I

Title 1 of Part 2 of Division 3 of Corporations Code §§ 12200-12956

§ 12200. Definitions; construction. Unless the context otherwise requires, the definitions and general provisions set forth in this chapter govern the construction of this part.

§ 12201. Cooperative corporation. A "cooperative corporation" means a corporation composed of ultimate producers or consumers, or both, organized for the purpose of conducting any lawful business primarily for the mutual benefit of its shareholders who may be natural or legal persons, and the earnings, savings, or benefits of which are used for the general welfare of the shareholders or patrons or are distributed in the form of cash, stock, evidences of indebtedness, goods, or services, proportionately and equitably among the persons for which it does business upon the basis of the amount of their transactions or participation in production, or both. However, any such corporation may pay out of its net surplus earnings, savings, or benefits, not to exceed 5 percent interest upon its capital stock.

§ 12202. Cooperative corporation; central organization. "Cooperative corporation" includes any central organization composed wholly or in part of cooperative corporations.

§ 12203. Corporation synonyms. "Corporation," "company," "association," "exchange," "society," "league" and "union" are synonymous.

§ 12204. Share; shareholder. "Share" means a share of stock or a membership share, and includes "membership." "Shareholder" means either a holder of a share of stock or a member.

§ 12205. Application of general nonprofit corporation law. The provisions of Division 2 of Title 1¹ of this code, relating to nonprofit corporations, apply to cooperative corporations formed under this part, except where such provisions are in conflict with those of this part. Corporations formed under this part have and enjoy all rights, powers, and privileges granted generally to corporations by the laws of this State, except as may be inconsistent with the provisions of this part.

§ 12206. Bringing corporation under provisions of part; amendment of articles. Any corporation organized under any other law of this State may bring itself under the provisions of this part by amending its articles of incorporation in the manner proscribed by the General Corporation Law¹ to conform to the provisions of this part. Whenever any corporation has amended its articles of incorporation to conform to the provisions of this part, it shall be deemed to be then organized and existing under, and entitled to the benefit of, and subject to the provisions of, this part for all purposes as fully as though originally organized under this part.

§ 12400. Formation; number of incorporators; purpose. Five or more persons may form a cooperative corporation for any lawful purpose by filing articles of incorporation with the Secretary of State.

§ 12401. Articles; required provisions. The articles of incorporation shall contain:

- (a) The name of the corporation.
- (b) The purposes for which it is formed.
- (c) The county in this State in which the principal office for the transaction of the business of the corporation is located.
- (d) The number of its directors, which shall be not less than 5 nor more than 25.
- (e) The names and post-office addresses of the directors, who shall serve until the first annual meeting.
- (f) The names and post-office addresses of the subscribers for shares and a statement of the number of shares which each agrees to take in the corporation.

§ 12402. Statement of shares and memberships. The articles shall also state either or both of the following:

- (a) The total number of shares which the corporation is authorized to issue and (1) the aggregate par value, if any, of all shares, and the par value of each share, or (2) that all shares are to be without par value.
- (b) The number and kind of memberships and the cost thereof.

§ 12403. Statement of number of shares permitted per shareholder and initial capital. The articles shall also state any limitation on the number of shares permitted to be owned or held or voted by any one shareholder at any one time, and the amount of capital with which the association will begin business.

§ 12404. Classes of shares; statement of par value and preferences, privileges, and restrictions; authority of board to change. If the corporation is authorized to issue more than one class of shares, the articles shall state the total number of shares which the corporation is authorized to issue and the aggregate par value of all shares that are to have a par value, and (a) the number of shares of each class that are to have a par value, and the par value of each share of each such class, and (b) the number of shares of each class that are to be without par value, and the articles shall state the preferences, privileges, and restrictions granted to or imposed upon the respective classes of shares or the holders thereof. In lieu of a statement of the dividend rate, the conversion rights, voting rights, the redemption price, or the liquidation preferences of any class, the articles may authorize the board of directors, within the limits and restrictions stated therein, to fix the dividend rate, the conversion rights, voting rights, the redemption price, or the liquidation preferences of any wholly unissued class of shares, or all or any of them.

Except as specified in the articles, no distinction shall exist between classes of shares or the holders thereof.

§ 12405. Voting rights in central organization. The articles of incorporation of a central organization which has been formed or exists under the provisions of this part may provide that each cooperative corporation which is a shareholder thereof is entitled to cast one or more additional votes in the affairs of the central organization for any stipulated number of voting members in the cooperative corporation, or for any stipulated volume of business done by the cooperative corporation with the central organization, or for both.

§ 12406. Corporate name; inclusion of cooperative. The names of all corporations formed under this part shall include "cooperative." No corporation shall be formed under this part unless there is affixed or prefixed to its name some word or abbreviation which will indicate that it is a corporation, as distinguished from a natural per-

§ 12450. Adoption before doing business. Before proceeding to do business the shareholders shall adopt by-laws not inconsistent with the provisions of this part.

§ 12451. Permissible provisions. The by-laws of a cooperative corporation may provide for:

- (a) The management of the property.
- (b) The regulation of the affairs.
- (c) Transfer of the shares.

- (d) The purchase of shares as authorized.
- (e) Calling of meetings of shareholders.
- (f) Election of directors.
- (g) The number of shareholders necessary to constitute a quorum.
- (h) The method of returning and distributing net savings or earnings.
- (i) Such other rules and regulations as the directors deem necessary for the proper management of the business of the corporation.

§ 12452. Purchase of shares. The by-laws of a cooperative corporation may provide for the purchase of shares held by any shareholder who fails to patronize the corporation during the preceding corporate year to an amount prescribed in the by-laws.

§ 12453. Formation of districts; district meetings; election of delegates; vote of delegates. A cooperative corporation covering an area which in the opinion of the shareholders is too large for their convenient assembling may provide in its by-laws for the formation of districts and the holding of district meetings which may elect one or more delegates to represent their districts in annual and special meetings of the corporation in a manner to be specified in the by-laws. The vote of such delegates shall be the vote of all the shareholders appearing upon the books of the corporation as residing in their respective districts, on all questions not covered by ballots submitted to all shareholders.

§ 12600. Management of corporation by board; election of directors; term of office; removal. Every cooperative corporation shall be managed by a board of directors. The directors shall be elected by the shareholders at such time and for such terms not exceeding three years as the by-laws may prescribe, and shall hold office until their successors are elected and enter upon the discharge of their duties.

A majority of all the shareholders, at any regular or special meeting duly called, may remove any director for cause, and fill the vacancy.

§ 12601. Officers; election by directors

The officers of every cooperative corporation shall be a president, one or more vice presidents, who shall be directors, and a secretary and a treasurer, who need not be directors, all of whom shall be elected annually by the directors. One person may hold the office of secretary and treasurer. If the corporation employs a manager who is not a director, the directors may also elect him vice president. (As amended Stats. 1937, c. 276, p. 626, § 2.)

§ 12700. Special meeting at request of shareholders. Upon written request of at least 20 percent of the shareholders, the secretary shall call a special meeting of the shareholders for the purpose to which the request relates.

§ 12701. Quorum

At any meeting of the shareholders, the presence in person of 250 holders of shares having voting rights, or such lesser number of such persons as shall equal 5 percent of all of the holders of such shares, constitutes a quorum for the transaction of business, unless the by-laws require a greater number or percentage. (Amended Stats.1957, c. 1-119, p. 2774, § 1.)

§ 12702. Voting rights. Any holder of shares having voting rights is entitled to cast one vote and no more, regardless of the number of shares or memberships held by him, except as provided in Section 12405.

§ 12703. Proxies. There shall be no voting by proxy, except as provided in Section 12453.

§ 12704. Voting by absent shareholders. At any meeting of the shareholders the written vote of an absent shareholder, signed by him, shall be received and counted if (a) he has been previously notified, in writing, of the exact motion, resolution, or nomination upon which the vote is taken, and (b) a copy of the motion, resolution, or nomination has been forwarded with, and attached by him to, the written vote.

§ 12705. Referendum. The secretary shall cause a referendum vote to be taken by mail upon any action or recommendation proposed in writing by 20 percent of the shareholders of the corporation.

§ 12800. Promotion expenses; limitation on payment. None of the funds of any corporation organized under this part shall be used nor shall any shares of stock or memberships of such corporation be used in payment of any promotion of the corporation for commission, salaries, or expenses of any kind whatsoever, in excess of 10 percent of the paid-up capital stock. However, this section does not authorize any act prohibited by any provision of the corporation laws of this State placing restrictions upon the issue of stock, certificates of interest, or other securities, or upon the payment of promotion expenses or compensation for promotion.

§ 12801. Stock certificates; issuance when fully paid. Certificates of stock shall not be issued to any subscriber until fully paid.

§ 12802. Purchase of business of another; payment in shares or memberships; approval by shareholders. When a cooperative corporation purchases the business of any other association, corporation, or person, it may pay for the purchase wholly or partly by the issue of shares of its capital stock or memberships to an amount which at par value would equal the fair market value of the business purchased, or wholly or partly in goods and services equal to the fair market value of the business purchased, or by any combination of shares, memberships, goods, and services to that amount.

No such purchase shall be made until the proposal therefor has been submitted by the directors to a meeting of the shareholders duly convened, with notice of the proposed action, and with an itemized statement of assets and liabilities of the business proposed to be purchased which shall include the value of the good will, patents, and other intangible assets as a separate item, and the proposal has been ratified by a majority vote of the shareholders.

§ 12803. Purchase of own shares or memberships. The corporation has the right to purchase, at book value as conclusively determined by the directors, any of its shares or memberships offered for transfer, or the stock or membership of any deceased shareholder.

§ 12804. Investment in shares or memberships of other corporations. The corporation may, by a majority vote of the shareholders, invest not to exceed 25 percent of its capital, in the capital stock, shares, or memberships of any other corporation.

§ 12805. Reserve funds and dividends

(a) **Surplus-savings and earnings; reserve fund; dividend.** The directors shall apportion any net surplus-savings and earnings by first setting aside at least 10 percent thereof for a reserve fund until the reserve fund equals 30 percent of the paid-up shares, and thereafter the directors may continue to set aside 10 percent of the net surplus-savings for a reserve fund. The directors may then declare a dividend upon the paid-up shares at a yearly rate not to exceed 5 percent. No such dividend shall be cumulative.

(b) **Educational fund.** The directors may then set aside such an amount of the remaining surplus-savings or earnings as may be provided in the by-laws as an educational fund to be used in teaching cooperation.

(c) **Dividends to patrons; use of surplus-savings for general welfare.** The directors may distribute all remaining surplus-savings or earnings uniformly to patrons of the corporation who are shareholders, and in the discretion of the corporation, they may also distribute uniform surplus-savings to patrons who are not shareholders, based in amount upon the volume of business transacted with the corporation by such patrons. The rate of such distribution, and the ratio of savings returns to shareholders and nonshareholders shall be determined by resolution of the directors. However, surplus-savings or earnings shall not be distributed to nonshareholder patrons unless at least 50 percent of such amount is applied toward purchase of shares in the corporation.

Alternatively, the corporation may employ a part or all of such surplus-savings for its general welfare.

(d) **Form of dividends.** Any savings returns or dividends declared under this section may be in the form of stock or memberships in whole or in part.

§ 12900. Application of general corporation law

Any co-operative corporation organized or existing under this part may amend its articles of incorporation in the manner prescribed by the General Corporation Law. (As amended Stats. 1939, c. 1540, p. 3867, § 1.)

§ 12950. Unauthorized use of cooperative in name

Except as otherwise expressly provided in this chapter, no person, firm, individual, partnership, trust, domestic corporation, foreign corporation, or association shall adopt or use the word " * * * cooperative" or any abbreviation or derivation thereof, or any word similar thereto, as part of the name or designation under which he does business in this state, nor conduct business or represent that business is conducted * * * cooperatively, unless incorporated as provided in this

part or as a nonprofit * * * cooperative association under * * * Chapter 1 of Division 29 of the Agricultural Code or under some other law of this state entitling him so to do; provided, however, that the foregoing prohibition shall be inapplicable to any housing cooperative, the financing of which is insured or guaranteed by the United States of America, one of its instrumentalities, or agencies, and which is certified by the Commissioner of the Federal Housing Administration as a consumer * * * cooperative.

§ 12951. Use of cooperative in name; cooperative organizations using name before September 19, 1939. A domestic or foreign corporation or association which did business in this State under a name or designation including the word "cooperative" prior to September 19, 1939, and which conducts business on a cooperative basis substantially as set forth in this part, may continue to do business under that name or designation.

§ 12952. Use of cooperative in name; noncooperative organizations using name before September 19, 1939. Any person, firm, individual, partnership, trust, domestic corporation, foreign corporation, or association which did business in this State under a name or designation including the word "cooperative" prior to September 19, 1939, but which does not conduct business substantially as set forth in this part, may continue to do business under that name or designation if the words "not organized under the law relating to cooperative corporations" are always placed immediately after the name or designation wherever it is used.

§ 12953. Foreign corporations; use of cooperative in name. Any foreign corporation, organized under and complying with the cooperative law of the State or other jurisdiction of its creation, may use the term "cooperative" in this State if it has complied with the laws of this State applicable to foreign corporations, in so far as those laws are applicable to it, and if it is doing business on a cooperative basis, as defined in this part.

§ 12954. Unauthorized business. It is unlawful for any corporation formed under this part to carry on business contrary to or outside of the purpose for which it is formed. (Stats.1947, c. 1038,

§ 12955. Injunction. Any person, firm, partnership, trust, domestic corporation, foreign corporation, or association may be enjoined from violating the provisions of Section 12950 or Section 12954 or from issuing, selling, offering for sale, negotiating, advertising or distributing stocks, notes, bonds, certificates or evidences of indebtedness, or other securities, issued by him or concerning his business or affairs in violation of this part, at the instance of any citizen or official agency of this State.

§ 12956. Penalty for violation; misdemeanor. Any person, firm, partnership, trustee, association or corporation violating any of the provisions of Section 12950 or Section 12954 is guilty of a misdemeanor, punishable by a fine of not more than five hundred dollars (\$500), or by imprisonment for not more than one year, or by both such fine and imprisonment.

CONFORMING REVISIONS IN THE LAWS RELATING
TO MUTUAL WATER COMPANIES

Civil Code § 330.24 (repealed)

SEC. [1]. Section 330.24 of the Civil Code is repealed.

~~330.24. Any corporation organized for or engaged in the business of selling, distributing, supplying or delivering water for irrigation purposes, or for domestic use, may provide in its articles or by-laws that water shall be sold, distributed, supplied or delivered only to owners of its shares and that such shares shall be appurtenant to certain lands when the same are described in the certificate issued therefor; and when such certificate is so issued and a certified copy of such articles or by-laws recorded in the office of the county recorder in the county where such lands are situated the shares of stock shall become appurtenant to the said lands and shall only be transferred therewith, except after sale or forfeiture for delinquent assessments thereon as provided in Section 331 of this title. Notwithstanding such provision in its articles or by-laws, any such corporation may sell water to the State, or any department or agency thereof, or to any school district, or to any public agency, or, to any other mutual water company or, during any emergency resulting from fire or other disaster involving danger to public health or safety, to any person at the same rates as to holders of shares of such corporations; and provided further, that any such corporation may enter into a contract with a county fire protection district to furnish water to fire hydrants and for fire suppression or fire-prevention purposes at a flat rate per hydrant or other connection.~~

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~~In the event lands to which any such stock is appurtenant are owned or purchased by the State, or any department or agency thereof, or any school district, or public agency, such stock shall be canceled by the secretary, but shall be reissued to any person later acquiring title to such land from the state department, agency, or school district, or public agency.~~

Comment. Section 330.24 is continued as Public Utilities Code Section 2713.

045/167

Civil Code § 330.25 (repealed)

SEC. [2]. Section 330.25 of the Civil Code is repealed.

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~~330.25. Any corporation, including a nonprofit corporation organized for or engaged in the business of developing, distributing, supplying, or delivering water for irrigation or domestic use or both, may provide in its articles, or may amend its articles to provide, that its only purpose shall be to develop, distribute, supply, or deliver water for irrigation or domestic use or both to its members or shareholders, at actual cost plus necessary expenses.~~

The amendment of the articles may be accomplished by:

- (a) The passage by a three-fourths vote of the members of the board of directors of the corporation of a resolution adopting as the purpose of the corporation the purpose set forth in this section.

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~~(b) The signing, verification, and filing in the manner prescribed~~
in Section 362b of a certificate setting forth the resolution and the
manner of its adoption.
Such corporation shall not distribute any gains, profits, or divi-
~~dends to its members or shareholders except upon the dissolution of the~~
~~corporation.~~

Comment. Section 330.25 is continued as Public Utilities Code Sec-
tion 2714.

045/168

Civil Code § 330.26 (repealed)

SEC. [3]. Section 330.26 of the Civil Code is repealed.

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~~330.26. Whenever the owner of real property to which water stock~~
by the terms of the certificate thereof is attached or appurtenant at
the time of conveyance, by properly executed conveyance, transfers to
another the real property with the appurtenances belonging to the prop-
erty, or whenever title to the property passes by execution sale, or by
foreclosure or probate proceedings, the secretary of the water company
which issued the stock shall, upon exhibition to him of a deed of the
land duly recorded, or the necessary court order duly recorded, issue to
the grantee named in the conveyance a new certificate of stock for the
~~number of shares attached or appurtenant to the land as shown by the~~

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~~books and records of the company. The secretary of the water company shall enter the name of the grantee upon the books of the company as the owner of the shares of stock and shall cancel on the books the number of former shares of stock so attached or appurtenant to the land though the lands stands in the name of the grantor or of any previous owner of the land, or of any other person.~~

Comment. Section 330.26 is continued as Public Utilities Code Section 2715.

Civil Code § 331 (repealed)

SEC. [4]. Section 331 of the Civil Code [as amended by Assembly Bill 2849, Section 1] is repealed.

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~~331. (1) Nonstock corporations may levy dues or assessments or both upon their members, if such authority is conferred either by the articles or by their by-laws, and subject to any limitations therein contained. Such dues or assessments or both may be levied upon all classes of membership alike, or in different amounts or proportions or upon a different basis upon different classes of membership and memberships of one or more classes may be made exempt from either dues or assessments or both, in the manner and to the extent provided either in the articles or the by-laws.~~

~~The amount of the levy and method of collection of such dues or~~
assessments or both may be fixed in the articles or by-laws, or the
articles or by-laws may authorize the board of directors to fix the
amount thereof from time to time, and make them payable at such times or
intervals, and upon such notice, and by such methods of collection as
the directors may prescribe. They may be made enforceable by action or
by forfeiture of membership, or both, upon reasonable notice.

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(2) Any corporation organized for or engaged in the business of
selling, distributing, supplying or delivering water for irrigation pur-
poses or domestic use, and not as a public utility, may levy assessments
upon its shares, whether or not fully paid, unless otherwise provided in
its articles or by-laws. If any shares of any such corporation which
have been made appurtenant to any land as provided in this code, become
delinquent in the payment of assessments, the right to receive water or
dividends thereon may be denied, and they may be sold and transferred
without said lands as if not appurtenant thereto, and the purchaser
shall acquire the right to receive water as provided in the articles or
~~by-laws of the corporation, or they may be forfeited to the corporation.~~

Comment. Subdivision (1) of Section 331 is superseded by Corpora-
tions Code Section 3500. Subdivision (2) is continued as Public Utili-
ties Code Section 2716.

Corporations Code § 602 (amended)

SEC. [5]. Section 602 of the Corporations Code is amended to read:

602. (a) Unless otherwise provided in the articles, a majority of the shares entitled to vote, represented in person or by proxy, shall constitute a quorum at a meeting of shareholders, but in no event shall a quorum consist of less than one-third ~~(or, in the case of a mutual water company, 29 percent)~~ of the shares entitled to vote at the meeting or, except in the case of a close corporation, of more than a majority of the shares entitled to vote at the meeting. If a quorum is present, the affirmative vote of the majority of the shares represented at the meeting and entitled to vote on any matter shall be the act of the shareholders, unless the vote of a greater number or voting by classes is required by this division or the articles and except as provided in subdivision (b).

(b) The shareholders present at a duly called or held meeting at which a quorum is present may continue to transact business until adjournment notwithstanding the withdrawal of enough shareholders to leave less than a quorum, if any action taken (other than adjournment) is approved by at least a majority of the shares required to constitute a quorum.

(c) In the absence of a quorum, any meeting of shareholders may be adjourned from time to time by the vote of a majority of the shares represented either in person or by proxy, but no other business may be transacted, except as provided in subdivision (b).

Comment. Subdivision (a) of Section 602 is amended to delete the reference to mutual water companies. The substance of the deleted language is continued in Public Utilities Code Section 2717.

Corporations Code § 703 (amended)

SEC. [6]. Section 703 of the Corporations Code is amended to read:

703. (a) Every shareholder complying with subdivision (b) and entitled to vote at any election of directors may cumulate such shareholder's votes and give one candidate a number of votes equal to the number of directors to be elected multiplied by the number of votes to which the shareholder's shares are entitled, or distribute the shareholder's votes on the same principle among as many candidates as the shareholder thinks fit.

(b) No shareholder shall be entitled to cumulate votes (i.e., cast for any one or more candidates a number of votes greater than the number of the shareholder's shares) unless such candidate or candidates' names have been placed in nomination prior to the voting and the shareholder has given notice at the meeting prior to the voting of the shareholder's intention to cumulate the shareholder's votes. If any one shareholder has given such notice, all shareholders may cumulate their votes for candidates in nomination.

(c) In any election of directors, the candidates receiving the highest number of votes of the shares entitled to be voted for them up to the number of directors to be elected by such shares are elected.

~~(d) Subdivision (a) applies to the shareholders of any mutual water company organized or existing for the purpose of delivering water to its shareholders at cost on lands located within the boundaries of one or more reclamation districts now or hereafter legally existing in this state and created by or formed under the provisions of any~~

~~statute of this state, but does not otherwise apply to the shareholders of mutual water companies unless their articles or bylaws so provide.~~

~~(e)~~ (d) Elections for directors need not be by ballot unless a shareholder demands election by ballot at the meeting and before the voting begins or unless the bylaws so require.

Comment. Section 708 is amended to delete the reference to mutual water companies. The substance of subdivision (d) is continued as Public Utilities Code Section 2718.

368/263

Pub. Util. Code § 2713

Public Utilities Code § 2713 (added)

SEC. [7]. Section 2713 is added to the Public Utilities Code, to read:

2713. Any corporation organized for or engaged in the business of selling, distributing, supplying or delivering water for irrigation purposes, or for domestic use, may provide in its articles or bylaws that water shall be sold, distributed, supplied or delivered only to owners of its shares and that such shares shall be appurtenant to certain lands when the same are described in the certificate issued therefor; and when such certificate is so issued and a certified copy of such articles or bylaws recorded in the office of the county recorder in the county where such lands are situated the shares of stock shall become appurtenant to the said lands and shall only be transferred therewith,

except after sale or forfeiture for delinquent assessments thereon as provided in Section 2716. Notwithstanding such provision in its articles or bylaws, any such corporation may sell water to the state, or any department or agency thereof, or to any school district, or to any public agency, or, to any other mutual water company or, during any emergency resulting from fire or other disaster involving danger to public health or safety, to any person at the same rates as to holders of shares of such corporations; and provided further, that any such corporation may enter into a contract with a county fire protection district to furnish water to fire hydrants and for fire suppression or fire prevention purposes at a flat rate per hydrant or other connection. In the event lands to which any such stock is appurtenant are owned or purchased by the state, or any department or agency thereof, or any school district, or public agency, such stock shall be canceled by the secretary, but shall be reissued to any person later acquiring title to such land from the state department, agency, or school district, or public agency.

Comment. Section 2713 is substantively identical to former Civil Code Section 330.24.

368/261

Pub. Util Code § 2714

Public Utilities Code § 2714 (added)

SEC. [8]. Section 2714 is added to the Public Utilities Code, to read:

2714. (a) Any corporation, including a nonprofit corporation orga-

nized for or engaged in the business of developing, distributing, supplying, or delivering water for irrigation or domestic use or both, may provide in its articles, or may amend its articles to provide, that its only purpose shall be to develop, distribute, supply, or deliver water for irrigation or domestic use or both to its members or shareholders, at actual cost plus necessary expenses.

(b) The amendment of the articles may be accomplished by:

(1) The passage by a three-fourths vote of the members of the board of directors of the corporation of a resolution adopting as the purpose of the corporation the purpose set forth in this section.

(2) The signing, verification, and filing in the manner prescribed in Chapter 9 (commencing with Section 900) of the General Corporation Law or Chapter 9 (commencing with Section 5910) of the General Nonprofit Corporation Law, whichever is applicable, of a certificate setting forth the resolution and the manner of its adoption.

(c) Such corporation shall not distribute any gains, profits, or dividends to its members or shareholders except upon the dissolution of the corporation.

Comment. Section 2714 is the same in substance as former Civil Code Section 330.25. Subdivision (b)(2) provides that the signing, verification, and filing of the certificate of amendment shall be accomplished in the manner provided by the General Corporation Law or the General Nonprofit Corporation Law, depending on which provisions normally apply to the water company amending its articles.

Public Utilities Code § 2715 (added)

SEC. [9]. Section 2715 is added to the Public Utilities Code, to read:

2715. Whenever the owner of real property to which water stock by the terms of the certificate thereof is attached or appurtenant at the time of conveyance, by properly executed conveyance, transfers to another the real property with the appurtenances belonging to the property, or whenever title to the property passes by execution sale, or by foreclosure or probate proceedings, the secretary of the water company which issued the stock shall, upon exhibition to him of a deed of the land duly recorded, or the necessary court order duly recorded, issue to the grantee named in the conveyance a new certificate of stock for the number of shares attached or appurtenant to the land as shown by the books and records of the company. The secretary of the water company shall enter the name of the grantee upon the books of the company as the owner of the shares of stock and shall cancel on the books the number of former shares of stock so attached or appurtenant to the land though the lands stands in the name of the grantor or of any previous owner of the land, or of any other person.

Comment. Section 2715 is identical to former Civil Code Section 330.26.

Public Utilities Code § 2716 (added)

SEC. [10]. Section 2716 is added to the Public Utilities Code, to read:

2716. Any corporation organized for or engaged in the business of selling, distributing, supplying or delivering water for irrigation purposes or domestic use, and not as a public utility, may levy assessments upon its shares, whether or not fully paid, unless otherwise provided in its articles or bylaws. If any shares of any such corporation which have been made appurtenant to any land as provided in Section 2713, become delinquent in the payment of assessments, the right to receive water or dividends thereon may be denied, and they may be sold and transferred without said lands as if not appurtenant thereto, and the purchaser shall acquire the right to receive water as provided in the articles or bylaws of the corporation, or they may be forfeited to the corporation.

Comment. Section 2716 is substantively identical to subdivision (2) of former Civil Code Section 331.

Public Utilities Code § 2717 (added)

SEC. [11]. Section 2717 is added to the Public Utilities Code, to read:

2717. A quorum at a meeting of shareholders of a mutual water company may not consist of less than 20 percent of the shares entitled to vote at the meeting.

Comment. Section 2717 continues the substance of a portion of subdivision (a) of Section 602 of the Corporations Code.

4460

Public Utilities Code § 2718 (added)

SEC. [12]. Section 2718 is added to the Public Utilities Code, to read:

2718. Subdivision (a) of Section 708 of the Corporations Code, relating to cumulative voting, applies to the shareholders of any mutual water company organized or existing for the purpose of delivering water to its shareholders at cost on lands located within the boundaries of one or more reclamation districts now or hereafter legally existing in this state and created by or formed under the provisions of any statute of this state but does not otherwise apply to the shareholders of mutual water companies unless their articles or bylaws so provide.

Comment. Section 2718 is substantively identical to former subdivision (d) of Section 708 of the Corporations Code.