

Memorandum 90-77

Subject: Study L-646 - Exercise of Stock Voting Rights by Trustees

We have received an inquiry by telephone about a potential conflict between Corporations Code Section 704, concerning voting of stock by fiduciaries, and Probate Code Section 15620, concerning actions by trustees under the Trust Law. The Trust Law provides as follows: "Unless otherwise provided in the trust instrument, a power vested in two or more trustees may only be exercised by their unanimous action." This has been the law at least since 1872 (see former Civ. Code § 2268).

Corporations Code Section 704 provides its own default rules where shares stand of record in the names of two or more persons, unless "the secretary of the corporation is given written notice to the contrary and is furnished with a copy of the instrument or order appointing them or creating the relationship" providing a different rule. In the absence of such notice, Section 704 provides that:

- (1) If only one votes, such act binds all.
- (2) If more than one vote, the act of the majority so voting binds all.
- (3) If more than one vote, but the vote is evenly split, each faction may vote proportionately.

It is reasonable to suppose that a corporate secretary will follow Corporations Code Section 704, regardless of the Trust Law rule and will not be concerned with any special rules in the trust unless given notice as provided in Section 704. However, there may be some doubt about what to do if a trustee gives notice of the contents of the statute. In other words, if the trust is governed by the unanimous vote rule, why should the corporate secretary be able to ignore that rule when so informed. Presumably, if the trust instrument provided (needlessly) for unanimity, perhaps even by referring to the statutory rule in Probate Code Section 15620, the literal terms of Corporations

Code Section 704 can be satisfied by filing the trust instrument with the corporate secretary.

Is There a Problem in Need of a Solution?

The staff does not know whether the inconsistency between these two statutes has caused any real problems in practice. Where trustees have failed to abide by the applicable trust law or the terms of the trust instrument, the trustees might be liable in a proceeding for breach of trust or a petition to remove a trustee who, for example, voted the stock without the necessary authority. The action of a rogue trustee who votes stock may be relied upon by the corporate secretary, under the terms of the Corporations Code and also under Probate Code Section 18100 which protects third persons who rely on the actions of a trustee without actual knowledge that the trustee is exceeding its powers. Accordingly, the Commission may not want to give any further consideration to this question.

Possible Statutory Remedies

If the Commission decides to seek a resolution of this statutory conflict, there are several possible approaches. (1) Corporations Code Section 704 could be revised to require corporate secretaries to follow the unanimity rule in the Trust Law unless notice of a different rule is given. (2) Corporations Code Section 704 could be revised to provide for giving notice to the corporate secretary that the trust is subject to the statutory unanimity rule. (3) The direction of the statutory default rule in the Trust Law could be reversed to provide for majority rule, unless the trust instrument provides otherwise, which would be consistent with the default rule applicable to personal representatives under Probate Code Section 9630.

If a solution is desired, the staff recommends the approach of revising the Corporations Code to permit effective notice to the corporate secretary of the fact that the trust is subject to the default statutory unanimity rule. This could be accomplished as follows:

Corp. Code § 704. Shares in names of more than one person

704. If shares stand of record in the names of two or more persons, whether fiduciaries, members of a partnership,

joint tenants, tenants in common, husband and wife as community property, tenants by the entirety, voting trustees, persons entitled to vote under a shareholder voting agreement or otherwise, or if two or more persons (including proxyholders) have the same fiduciary relationship respecting the same shares, unless the secretary of the corporation is given written notice to the contrary and is furnished with a copy of the instrument or order appointing them or creating the relationship wherein it is so provided, or a copy of a statute governing the manner of voting and a statement that the statute governs the vote in the matter, their acts with respect to voting shall have the following effect:

- (1) If only one votes, such act binds all;
- (2) If more than one vote, the act of the majority so voting binds all;
- (3) If more than one vote, but the vote is evenly split on any particular matter, each faction may vote the securities in question proportionately.

If the instrument so filed or the registration of the shares shows that any such tenancy is held in unequal interests, a majority or even split for the purpose of this section shall be a majority or even split in interest.

Comment. The first paragraph of Section 704 is amended to recognize that a different rule for voting shares may be provided by statute, as well as an instrument or court order. See Prob. Code § 15620 (cotrustees act unanimously unless trust provides otherwise).

Note that, as drafted, this revision would apply potentially to more than the Trust Law.

We would not reverse the default unanimity rule in the Trust Law. This was discussed and approved in the existing form when the Commission revised the Trust Law, and it would not make sense to change it at this point just to resolve the conflict with the Corporations Code. In any event, revising the default rule could only apply prospectively, and the problem, such as it is, would continue to exist for years to come.

Respectfully submitted,

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