

## Memorandum 76-7

Subject: Study 77.20 - Nonprofit Corporations (Organization--Name, Purposes, and Formation)

Introduction

At the November, 1975 meeting, the Commission requested (1) a rough outline of the Nonprofit Corporation Law and (2) some general background on the variety of nonprofit corporations, their nature, numbers, and statutes controlling them. The rough outline is at the front of the attached draft sections.

Nonprofit corporations lend themselves easily to a general categorization as either membership (serving the needs of its members) or charitable (serving a broad or indefinite segment of the public). A slightly more sophisticated general breakdown is that of Oleck, Nonprofit Corporations, Organizations, and Associations § 10 (3d ed.):

1. Charitable organizations. These include religious, educational, hospital, library, civic organizations, and the like.
2. Social organizations. These include clubs, mutual benefit societies, fraternal orders, and the like. Not included are "clubs" such as nightclubs, Christmas clubs, limited edition clubs, or one-man clubs.
3. Political organizations. These include political party organizations, propaganda organizations, and committees to aid the candidacy of a political hopeful or the adoption of certain legislation.
4. Trade associations. These include labor unions, boards of trade and chambers of commerce, manufacturers' or employers' associations, and the like.
5. Mixed business-non-profit organizations. These are the newest type, typified by the New York not-for-profit corporations for business operations, such as for urban housing development and the like, or the New Jersey limited-dividend public housing corporations.
6. Governmental organizations. These include all governmental and municipal organizations, such as municipal corporations (those of cities, towns, villages, counties, and road and water districts), and administrative bodies such as the Civil Aeronautics Board, the Tennessee Valley Authority, the New York Port Authority, and the Commodity Credit Corporation. Most of these are established and operated pursuant to express legislative provisions.

The California statutes specifically refer to many types of nonprofit corporations, including:

- Religious, charitable, social, educational, cemetery (Corp. Code § 9200)
- Medical or health services (Corp. Code § 9201)
- Optometric services (Corp. Code § 9201.1)
- Legal services (Corp. Code § 9201.2)
- Society, library, school, college, club, church, charitable trust, chamber of commerce (Corp. Code § 9202)
- Subordinate body of national association, lodge, order, beneficial association, fraternal or beneficial society, labor union, foundation, federation (Corp. Code § 9203)
- Corporation sole (Corp. Code §§ 10000-10015)
- Charitable or eleemosynary corporation (Corp. Code §§ 10200-10208)
- Common trust fund (Corp. Code § 10250)
- Humane society (Corp. Code §§ 10400-10406)
- Port and terminal protection and development (Corp. Code §§ 10700-10703)
- Chamber of commerce, board of trade, mechanics institute (Corp. Code §§ 12000-12006)
- Cooperative corporation (Corp. Code §§ 12200-12956)
- California Job Development Corporation (Corp. Code §§ 14000-14122)
- Homeowners association (Bus. & Prof. Code § 11003.1)
- Water distributing company (Civil Code § 330.25)
- Library (Educ. Code §§ 28701-28712)
- Educational institution of collegiate grade (Educ. Code §§ 29001-29022)

In addition, Internal Revenue Code Section 501(c) and Revenue and Taxation Code Sections 23701a-23701s specify numerous types of nonprofit corporations that may qualify for tax exemption. These include corporations formed for the following purposes:

Religious

Charitable, which includes

- relief of the poor and distressed or underprivileged
- advancement of religion, education, or science
- erection or maintenance of public buildings, monuments, or works
- lessening of the burdens of government
- promotion of social welfare
- lessening neighborhood tensions
- eliminating prejudice and discrimination
- defending human and civil rights secured by law
- combating community deterioration and juvenile delinquency
- promotion of health
- legal assistance
- pollution control

Scientific

Testing for public safety

Literary

Educational, which includes  
 primary and secondary school, college, or professional or trade  
 school  
 organization presenting public discussion groups, forums, panels,  
 lectures, or other programs  
 instruction by correspondence through radio or television.  
 museums, zoos, planetariums, symphony orchestras  
 Prevention of cruelty to children or animals  
 Business leagues, chambers of commerce, real estate boards, boards of  
 trade, professional football leagues  
 Civic leagues  
 Benevolent life insurance associations, mutual ditch or irrigation  
 companies, mutual or cooperative telephone companies  
 Mutual insurance companies  
 Credit unions  
 Title holding companies  
 Social clubs  
 Fraternal beneficiary societies  
 Cemetery companies  
 Labor, agricultural, or horticultural organizations  
 Religious and apostolic organizations  
 Local associations of employees  
 Voluntary employees' beneficiary associations  
 Local teachers' retirement fund associations  
 Supplemental unemployment benefit trusts  
 Qualified pension, profit-sharing and stock bonus plans

It is impossible to estimate the numbers of nonprofit corporations that exist in California or elsewhere. Oleck reports that the general proportion of business to nonprofit corporations throughout the United States is two to one, and that, in 1974, Ohio carried 40,000 nonprofit corporation charters on its active files. "Nobody knows the exact number of nonprofit organizations in this country. No doubt there are **hundreds of thousands**. And almost every American belongs to, or works in or with, dozens of them in his lifetime."

[Oleck, Nonprofit Corporations § 1.]

#### Corporate Name

General limitation on choice of name. The restrictions on corporate names in the General Corporation Law--that the name may not mislead the public or resemble another corporate name so closely as to tend to deceive--are applicable to nonprofit corporations. See general discussion in American Auto. Ass'n

v. American Auto. Owners Ass'n, 216 Cal. 125, 13 P.2d 707 (1932) and Most Worshipful Hiram etc. v. Most Worshipful Sons etc., 94 Cal. App.2d 25, 210 P.2d 34 (1949). In addition, a nonprofit corporation may not have a name that resembles the name of an unincorporated association so closely as to tend to deceive. Law v. Crist, 41 Cal. App.2d 862, 107 P.2d 953 (1941).

These provisions should be continued in the new General Nonprofit Corporation Law. But the staff believes it should be made clear that a nonprofit corporation cannot take the name of a business corporation and vice versa. This will require an amendment of the General Corporation Law.

"Bank" or "trust" in name. Section 201(a) of the General Corporation Law provides that the Secretary of State shall not file articles which set forth a name in which "bank," "trust," "trustee," or related words appear unless the certificate of approval of the Superintendent of Banks is attached. While this provision would not appear to apply to nonprofit corporations, a nonprofit corporation is permitted to organize for "any lawful purpose," and the Secretary of State has stated that this provision applies to both business and nonprofit corporations. See Corporations Check List, pp. 5, 11 (1973-74 rev.); see also California Nonprofit Corporations § 2.3 (Cal. Cont. Ed. Bar). This provision too should be continued in the General Nonprofit Corporation Law.

Misleading use of "charitable" name. The Commission has previously requested the staff to give consideration to whether a nonprofit corporation that is not charitable should be permitted to use a name that gives it the appearance of a charitable corporation. The staff believes that such a requirement would be difficult to police and, moreover, that it would be unnecessary--there are already adequate protections in the law against noncharitable corporations masquerading as charities. See, e.g., Penal Code § 532d

(fraudulent solicitation for charitable, religious, or eleemosynary purpose) and Bus. & Prof. Code §§ 17510-17510.7 (charitable solicitations by organizations that do not have charitable tax exempt status under federal and state law).

#### Purposes

Statement of specific and primary purposes. At the November 1975 meeting, the Commission determined to delete from existing law the requirement that the nonprofit corporation state in its articles the "specific and primary" purposes for which it is formed. This has been done in the attached draft. See Section 5250.

Further research on this point reveals that, prior to 1949, Corporations Code Section 9300 required only a statement of the "purposes" of the nonprofit corporation. This provision was revised, as part of a general improvement of the Corporations Code sponsored by the Secretary of State in 1949, to require the statement of "specific and primary purposes." At the same time, the sentence was added that "This requirement shall not be deemed to preclude a statement of general purposes or powers or to restrict the right of the corporation to engage in any other lawful activity."

It was erroneously stated at the November 1975 meeting that the CEB nonprofit corporations book attributes this amendment to the need of private foundations which solicit and receive funds and distribute them to other charities. The CEB book merely points out that the articles must state the specific and primary purposes for which the nonprofit corporation is formed, and that this does not preclude a statement of general purposes or powers and does not restrict the right to engage in other lawful activity. The comment about private foundations relates only to the sample corporate purposes clause

that happens to be illustrated in the book. See California Nonprofit Corporations § 2.10 (Cal. Cont. Ed. Bar 1969).

The principal objective of the 1949 amendment was to facilitate classification of corporations and to assist the Secretary of State in determining whether there is a likelihood of deception in the choice of corporate names. See The Work of the 1949 California Legislature, 23 So. Cal. L. Rev. 1 (1949).

In light of this background, the Commission may wish to reconsider its decision to repeal the requirement of a statement of specific and primary purposes. The staff notes, however, that a comparable provision was repealed in the General Corporation Law revision, apparently without objection by the Secretary of State. It may be that the need for this provision is no longer felt to be as great as it was in 1949.

Statement in articles that nonprofit corporation may not make distributions to members. At the November 1975 meeting, the Commission determined to require a statement in the articles that the nonprofit corporation cannot make distributions to members except to the extent provided in the General Nonprofit Corporation Law. Further research reveals that the nonprofit corporation law required such a statement in the articles until 1949, when it was replaced by the requirement that the articles state only that the corporation is organized under the General Nonprofit Corporation Law. Thus, a grandfather clause excusing compliance with this requirement for existing corporations need only do so for those formed between 1949 and the enactment of the new act.

Corporations for special purposes. The General Nonprofit Corporation Law contains several provisions relating to nonprofit corporations formed for special purposes. See Sections 9201 (medical services corporations), 9201.1 (optometrical services corporations), 9201.2 (legal services corporations),

9202 (incorporation of unincorporated associations), and 9203 (incorporation of subordinate bodies of head or national associations). Each of these sections contains special provisions that vary somewhat from the general provisions relating to nonprofit corporations.

The staff proposes to compile these special provisions outside the General Nonprofit Corporation Law with the subjects to which they specifically relate. The effect of this recompilation will be to assure that the General Nonprofit Corporation Law retains its general character unencumbered by special provisions which are not of general application.

#### Formation

The General Nonprofit Corporation Law provisions relating to formation of a corporation generally parallel those of the General Corporation Law. The staff plans to adopt the new General Corporation Law in this regard with the exceptions discussed below.

Incorporators. Section 9200 provides that a nonprofit corporation may be formed by "three or more persons." The General Corporation Law (Section 200(a)) provides for one incorporator, as do the ABA-ALI Model Nonprofit Corporation Act § 28 and the New York Not-for-Profit Corporation Law § 401.

The Commission has previously determined to delete the requirement of incorporators altogether because it serves no useful purpose in the modern nonprofit corporation. Traditionally, the incorporator was the person responsible if the corporation was inadequately capitalized; however, this has little relevance to the nonprofit corporation situation.

Under the Commission's proposal, with no incorporators, the first directors fulfill the functions traditionally assumed by incorporators. It should be noted that the new General Corporation Law takes the opposite approach, minimizing the role of first directors and increasing the role of incorporators.

County where principal office is located. Section 9300 requires that the articles of incorporation set forth "The County in this State where the principal office for the transaction of the business of the corporation is located." The new General Corporation Law eliminates a comparable requirement for business corporations because (1) it seems to imply that the principal office for the transaction of business be in California thus precluding incorporation of an out-of-state business, and (2) the principal office may change from time to time, so there is little point in preserving its initial address in the articles.

The new General Corporation Law substitutes for the requirement of designation of a county the requirement of the designation of an initial agent for service of process. The staff suggests that the required designation of a county for nonprofit corporations should likewise be omitted. The question whether it should be replaced by a required designation of an initial agent for service of process the staff reserves for future consideration in connection with the service of process provisions.

Execution of articles. Section 9304(a) requires the first directors, and permits other incorporators, to sign the articles of incorporation. All signatures must be personally acknowledged before an officer qualified to observe acknowledgments. The Commission has previously determined to limit the signers to first directors, and to eliminate the acknowledgment requirement. The General Corporation Law (Section 200(b)) requires signing and acknowledgment by both first directors and incorporators; however, the acknowledgment requirement is limited to a declaration in writing, signed by the persons executing it, "that they are such persons." Section 149(b).

Filing of articles. Section 9304.5 requires filing of articles with both the Secretary of State and the office of the county clerk of the county in which the nonprofit corporation is to have its principal office and in the office of



the county clerk of each county in which the nonprofit corporation acquires ownership of any real property. The Commission has previously determined to delete the requirements of filing with the county clerk having discerned no useful purpose of such filing. This corresponds with the approach of the General Corporation Law.

Corporate existence. Section 9304.5 provides that the corporate existence of a nonprofit corporation is perpetual unless otherwise expressly provided by law. The Commission has previously approved the concept of permitting the nonprofit corporation to limit its duration. The General Corporation Law has also adopted this approach.

Respectfully submitted,

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Tentative Rough Outline

GENERAL NONPROFIT CORPORATION LAW

Chapter 1. General Provisions and Definitions (§ 5000)

Article 1. General Provisions

Article 2. Definitions

Chapter 2. Organization and Bylaws (§ 5200)

Article 1. Purposes

Article 2. Formation

Article 3. Powers

Article 4. Corporate Name

Article 5. Articles of Incorporation

Article 6. Bylaws

Chapter 3. Directors and Management (§ 5300)

Article 1. Board of Directors

Article 2. Officers

Chapter 4. Members and Membership Certificates (§ 5400)

Chapter 5. Corporate Finances (§ 5500)

Article 1. General Provisions

Article 2. Trust Property

Article 3. Common Trust Funds

Chapter 6. Members' Meetings and Consents (§ 5600)

Chapter 7. Voting of Memberships (§ 5700)

Chapter 8. Members' Derivative Action (§ 5800)

Chapter 9. Amendment of Articles (§ 5900)

Article 1. Purposes

Article 2. Adoption and Approval

Article 3. Certificates of Amendment

Article 4. Extension of Corporate Existence

Article 5. Restatement of Articles

Chapter 10. Sales of Assets (§ 6000)

Chapter 11. Merger (§ 6100)

Article 1. Procedure and Effect

Article 2. Dissenting Members

Chapter 12. Reorganizations (§ 6200)

Chapter 13. Dissenters' Rights (§ 6300)

Chapter 14. Bankruptcy Reorganizations and Arrangements (§ 6400)

Chapter 15. Records and Reports (§ 6500)

Article 1. Books and Records

Article 2. Annual Report

Article 3. Statement of Identification of Corporate Officers;

Designation of Agent for Service

Chapter 16. Rights of Inspection (§ 6600)

Chapter 17. Service of Process (§ 6700)

Chapter 18. Involuntary Dissolution (§ 6800)

Article 1. Proceedings by Directors or Members

Article 2. Proceedings by State

Chapter 19. Voluntary Dissolution (§ 6900)

Chapter 20. General Provisions Relating to Dissolution (§§ 7000)

Article 1. Winding Up

Article 2. Directors

Article 3. Distribution of Assets

Article 4. Orders, Certificates, and Decrees of Winding Up and  
Dissolution

Article 5. Continuation After Dissolution

Chapter 21. Foreign Nonprofit Corporations (§ 7100)

Chapter 22. Crimes and Penalties (§ 7200)

Chapter 23. Transition Provisions (§ 7300)

Chapter 1. General Provisions and Definitions

§ 5000. Short title

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§ 5110. Application of general provisions

§ 5111. Scope of division

§ 5115. Filing by Secretary of State

§ 5116. Delayed effective date of instruments

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Article 2. Definitions

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§ 5122. Articles

§ 5124. Corporation

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§ 5128. Nonprofit corporation

Chapter 2. Organization and Bylaws

Article 1. Purposes

§ 5210. Any lawful purpose other than distribution of dividends

Article 2. Formation

§ 5220. Nonprofit corporation formed by executing and filing articles

§ 5221. Execution of articles

§ 5222. Filing of articles

Article 3. Powers

§ 5235. Power to engage in business activity

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Article 4. Corporate Name

§ 5240. Reservation of corporate name

§ 5241. Name which is likely to mislead or tends to deceive

§ 5242. Agreement to use name that is substantially the same

§ 5243. Name in which "bank," "trust," or related terms appear

§ 5244. Enjoining name violations

Article 5. Articles of Incorporation

§ 5250. Required contents of articles

DIVISION 2. GENERAL NONPROFIT CORPORATION LAW

CHAPTER 1. GENERAL PROVISIONS AND DEFINITIONS

§ 5000. Short title

5000. This division shall be known and may be cited as the General Nonprofit Corporation Law.

Comment. Section 5000 continues former Section 9000. For a comparable provision, see Section 100(a)(General Corporation Law).

Article 1. General Provisions§ 5110. Application of general provisions

5110. Unless the provision or the context otherwise requires, these general provisions govern the construction of this division.

Comment. Section 5110 is new; for comparable provisions, see Sections 5 (Corporations Code) and 101 (General Corporation Law).



§ 5111. Scope of division

5111. (a) Subject to the provisions of Chapter 23 (transition provisions), the provisions of this division apply to every nonprofit corporation now existing or hereafter formed unless the nonprofit corporation is expressly exempted from the operation thereof, or there is a special provision applicable to the nonprofit corporation inconsistent with the provisions of this division, in which case the special provision prevails.

Comment. Section 5111 supersedes former Section 9001; for a comparable provision, see Section 102 (General Corporation Law).

Subdivision (a) continues former Section 9001. For special provisions applicable to nonprofit corporations, see, e.g., Bus. & Prof. Code §§ 700-701 (medical services) and 6185 (legal services); Corp. Code §§ 20004 (incorporation of unincorporated association) and 20005 (incorporation of subordinate body).

Note. With each change in the law that the new General Nonprofit Corporation Law makes, the Commission must consider its effect on existing corporations and whether compliance is required. This section and Section 5126 ("nonprofit corporation" defined) are related.

§ 5115. Filing by Secretary of State

5115. (a) Upon receipt of any instrument by the Secretary of State for filing pursuant to this division, if it conforms to law, it shall be filed by, and in the office of, the Secretary of State and the date of filing endorsed thereon.

(b) The Secretary of State shall file a document as of any requested future date, including a Saturday, Sunday, or legal holiday, if the document is received in the Secretary of State's office at least one business day prior to the requested date of filing.

(c) The date of filing shall be the date the instrument is received by the Secretary of State unless withheld from filing for a period of time pursuant to a request by the party submitting it for filing.

Comment. Section 5115 is new; for comparable provisions, see Section 110(a) (General Corporation Law).

§ 5116. Delayed effective date of instruments

5116. (a) Any instrument filed with respect to a nonprofit corporation (other than original articles) may specify that the instrument is to become effective no more than 90 days after the filing date. If no revocation certificate is filed, the instrument becomes effective on the date specified.

(b) An instrument filed with a delayed effective date may be prevented from becoming effective by a certificate filed on or before the specified effective date, which states that, by appropriate corporate action, the instrument has been revoked and is null and void. The revocation certificate shall be executed in the same manner as the original instrument except that, in the case of a merger agreement, the certificate need only be executed on behalf of one of the constituent nonprofit corporations.

Comment. Section 5116 is new; for a comparable provision, see Section 110(c) (General Corporation Law).

§ 5117. Instruments conforming to law

5117. (a) If the Secretary of State determines that an instrument submitted for filing or otherwise submitted does not conform to law and returns it to the person submitting it, the instrument may be resubmitted accompanied by a written opinion of the member of the State Bar of California submitting the instrument, or representing the person submitting it, to the effect that the specific provision of the instrument objected to by the Secretary of State does conform to law and stating the points and authorities upon which the opinion is based. The Secretary of State shall rely, with respect to any disputed point of law (other than the application of Article 4 (commencing with Section 5240) of Chapter 2 and of Sections [2101] and [2106]), upon such written opinion in determining whether the instrument conforms to law.

(b) An instrument does not fail to conform to law because it is not accompanied by the full filing fee if the unpaid portion of such fee does not exceed the limits established by the policy of the Secretary of State for extending credit in such cases.

Comment. Section 5117 is new; for comparable provisions, see Section 110(b), (c).

Note. The references to Sections 2101 and 2106 are corporate name provisions for foreign corporations, a matter the staff has not yet reviewed.

Article 2. Definitions§ 5120. Application of definitions

5120. Unless the provision or context otherwise requires, these definitions govern the construction of this division.

Comment. Section 5120 is new; for comparable provisions, see Sections 5 (Corporations Code) and 101 (General Corporation Law). Unless otherwise provided in this division, the definitions in the general provisions of the Corporations Code are applicable. See, e.g., Sections 14-18.

§ 5122. Articles

5122. "Articles" includes the articles of incorporation, amendments thereto, amended articles, and restated articles.

Comment. Section 5122 continues a provision applicable to non-profit corporations by former Section 102 through former Section 9002. For a comparable provision, see Section 154 (General Corporation Law).

Note. The question whether this section should include certificates of incorporation, certificates of determination, and agreements of merger is deferred.

§ 5124. Corporation

5124. "Corporation" means corporation as that term is defined in the General Corporation Law.

Comment. Section 5124 is new. "Corporation" is defined in the General Corporation Law to mean a corporation organized under the General Corporation Law or a business corporation organized under a predecessor general law or created by act of the Legislature prior to enactment of a general corporation law. See Section 162 (General Corporation Law).

§ 5126. Filed

5126. "Filed," unless otherwise expressly provided, means filed in the Office of the Secretary of State.

Comment. Section 5126 is new; for a comparable provision, see Section 169 (General Corporation Law).



§ 5128. Nonprofit corporation

5128. "Nonprofit corporation" means a corporation organized under this division or under any predecessor general or special nonprofit corporation law, or by any act of the Legislature creating a private nonprofit corporation prior to the enactment of a general nonprofit incorporation statute.

Comment. Section 5128 is new; for a comparable definition of "corporation" see Section 162 (General Corporation Law).

Note. The staff has not yet investigated the extent to which the new statute can or should be applied to preexisting nonprofit corporations or to foreign nonprofit corporations. This section and Section 5111 (scope of division) are related.

## CHAPTER 2. ORGANIZATION AND BYLAWS

Article 1. Purposes§ 5210. Any lawful purpose other than distribution of dividends

5210. Subject to the laws and regulations applicable to the particular class of nonprofit corporation or line of activity, a nonprofit corporation may be formed for any lawful purposes other than the distribution of gains, profits, or dividends to members.

Comment. Section 5210 continues the substance of a portion of the first sentence of former Section 9200. Section 5210 permits incorporation for such purposes as religious, charitable, social, educational, cemetery, or for rendering services, but does not limit incorporation to these purposes. The requirement of former Section 9200 that the corporate purposes be ones for which individuals lawfully may associate themselves is not continued; it is unnecessary in light of the general limitation of Section 5210 that the nonprofit corporation be formed only for lawful purposes.

Under Section 5210, a nonprofit corporation may not be formed with the intent to distribute the proceeds of its operations to members, whether periodically or upon dissolution. The articles of a nonprofit corporation must preclude such distribution except to the extent provided in this division. See Section 5250. It should be noted, however, that this restriction does not prohibit a nonprofit corporation from operating a business or from making profits thereon. See Section 5235(a) (power to engage in business activity). Any profits must be applied to the lawful corporate purposes (Section 5235(b)) and may not be distributed to members except to the extent permitted by Section 5236.

The introductory portion of Section 5210 recognizes that there may be limitations on the purposes for which particular types of nonprofit corporations may be formed. See, e.g., Bus. & Prof. Code §§ 700-701 (medical services corporations) and 6185 (legal services corporations). It should also be noted that a nonprofit corporation may be formed, subject to Section 5210, for the purpose of incorporating an unincorporated association (Corp. Code § 20004) or subordinate body (Corp. Code § 20005).

Article 2. Formation§ 5220. Nonprofit corporation formed by executing and filing articles

5220. A nonprofit corporation may be formed under this division by executing and filing articles of incorporation.

Comment. Section 5220 supersedes a portion of former Section 9200 which provided that a nonprofit corporation may be formed by three or more persons. Section 5220 deletes the concept of incorporators, who perform no necessary function. First directors execute and file the articles and are fully empowered to govern the affairs of the nonprofit corporation until the selection of their successors. See Sections 5221 (execution of articles) and 5250 (required contents of articles).

§ 5221. Execution of articles

5221. Each person named in the articles of incorporation to act in the capacity of a first director shall personally sign the articles.

Comment. Section 5221 supersedes former Section 9304(a). Under Section 5221, "other persons desiring to associate with" the first directors are no longer permitted to sign the articles. Section 5221 also eliminates the acknowledgment requirements of former Section 9304(a) since they served no useful purpose. For an exception to the provision of Section 5221, see Sections 20004 (incorporation of unincorporated association) and 20005 (incorporation of subordinate body).

§ 5222. Filing of articles

5222. The corporate existence begins upon the filing of the articles and continues perpetually unless otherwise expressly provided by law or in the articles.

Comment. Section 5222 supersedes former Section 9304.5; for a comparable provision, see Section 200(c) (General Corporation Law). Section 5222 eliminates the requirement that articles be filed with the county clerk of the county in which the nonprofit corporation is to have its principal office. See Section 5124 ("filed" means filed with Secretary of State). For the duty of the Secretary of State to file and endorse the date of filing on the articles, see Section 5115.

Section 5222, unlike former Section 9304.5, authorizes the nonprofit corporation to limit in the articles the term of its existence.

Article 3. Powers§ 5235. Power to engage in business activity

5235. (a) Subject to any limitations contained in the articles and applicable laws, a nonprofit corporation may engage in business activity.

(b) Any gain or profit that results from business activity of a nonprofit corporation shall be applied only to the purposes for which the nonprofit corporation is formed.

Comment. Section 5235 is new.

Subdivision (a) supersedes the portion of the second sentence of former Section 9200 which provided that "carrying on business at a profit as an incident to the main purposes of the corporation" is not forbidden. Subdivision (a) makes clear that a corporation may carry on a business for profit whether or not the business is "incident" to its main purposes. See People ex rel. Groman v. Sinai Temple, 20 Cal. App.3d 614, 99 Cal. Rptr. 603 (1971). For a comparable provision, see Section 206 (General Corporation Law). One major limitation on the business activity of nonprofit corporations is found in subdivision (b).

Subdivision (b) requires that any gains or profits of the business be applied to the purposes of the nonprofit corporation. It should be noted that a nonprofit corporation may not have as a purpose the distribution of gains, profits, or dividends to members. Section 5210. Nor may a nonprofit corporation distribute any such gains, profits, or dividends to members. Section 5236.

§ 5236. Distributions to members prohibited

5236. (a) A nonprofit corporation shall not distribute any gains, profits, or dividends as such to members.

(b) Notwithstanding subdivision (a), a nonprofit corporation may, subject to any limitations in the articles or bylaws, do any of the following, none of which shall be deemed to be a distribution of gains, profits, or dividends:

- (1) Pay compensation to members for services rendered.
- (2) Confer benefits upon members in conformity with the purposes for which it is formed.
- (3) Make distributions to members upon dissolution or winding up to the extent permitted by this division.

Comment. Section 5236 is new; for a comparable provision, see the last portion of Section 26 of the ALI-ABA Model Non-Profit Corporation Act.

Subdivision (a) continues a limitation formerly found in the second sentence of Section 9200. A nonprofit corporation may not be formed for profit-distribution purposes (Section 5210), and this limitation must be stated in the articles. Section 5250. While subdivision (a) continues the limitation of former law that profits, gains, or dividends may not be distributed "as such," this limitation is subject to the provisions of subdivision (b).

Subdivision (b) lists major areas of withdrawal of corporate proceeds which do not violate the prohibition of subdivision (a). Paragraph (1) is new; compensation may be limited or precluded in the articles or bylaws. Paragraph (2) supersedes the portion of former Section 9200 permitting the formation of a nonprofit corporation for the purpose of rendering services. It makes clear that a nonprofit corporation may provide benefits to its members without violating the prohibition against distributions of gains, profits, or dividends as such. This codifies case law. People ex rel. Groman v. Sinai Temple, 20 Cal. App.3d 614, 99 Cal. Rptr. 603 (1971) (discount on price of cemetery land to members of nonprofit corporation is proper). Paragraph (3) continues portions of former Section 9200 permitting distributions on dissolution. For limitations on such distributions, see Sections 7030-7038.

Article 4. Corporate Name§ 5240. Reservation of corporate name

5240. (a) Any applicant may, upon payment of the fee prescribed therefor in the Government Code, obtain from the Secretary of State a certificate of reservation of any name not prohibited by Section 5241 and, upon the issuance of the certificate, the name stated therein shall be reserved for a period of 60 days.

(b) The Secretary of State shall not issue certificates reserving the same name for two or more consecutive 60-day periods to the same applicant or for the use or benefit of the same nonprofit corporation; nor shall consecutive reservations be made by or for the use or benefit of the same nonprofit corporation of names so similar as to fall within the prohibitions of Section 5241.

Comment. Section 5240 continues provisions applicable to nonprofit corporations by former Section 310 through former Section 9002. For a comparable provision, see Section 201(c). The fee for a certificate of reservation of corporate name is four dollars. Govt. Code § 12199.



§ 5241. Name which is likely to mislead or tends to deceive

5241. The Secretary of State shall not file articles which set forth a name which is likely to mislead the public or which is the same as, or resembles so closely as to tend to deceive, any of the following:

(a) The name of a domestic corporation or nonprofit corporation.

(b) The name of a foreign corporation or association which is authorized to transact intrastate business or has registered its name pursuant to Section 2101.

(c) A name which a foreign corporation or association has assumed under subdivision (b) of Section 2106.

(d) A name which will become the record name of a domestic or foreign corporation or nonprofit corporation upon the effective date of a filed corporate instrument where there is a delayed effective date pursuant to subdivision (c) of Section 110 or pursuant to Section 5116.

(e) A name which is under reservation for another corporation or nonprofit corporation.

Comment. Section 5241 continues provisions applicable to nonprofit corporations by former Section 310 through former Section 9002. For a comparable provision, see Section 201(b).

In addition to the prohibitions contained in Section 5241, there may be other applicable name limitations in other statutes. See, e.g., Section 12950 (use of word "cooperative"); Fin. Code § 5501 (building and loan and savings and loan associations); 36 U.S.C. § 379 (use of words "Olympic" or "Olympiad").

Note. This section has not been adjusted to account for foreign nonprofit corporations and associations. Conforming changes have not been made in Section 201.

§ 5242. Agreement to use name that is substantially the same

5242. Notwithstanding Section 5241, a nonprofit corporation may adopt a name that is substantially the same as the name of (1) an existing domestic corporation or nonprofit corporation or (2) a foreign corporation or association which is authorized to transact intrastate business or has registered its name pursuant to Section 2101 upon proof of consent by such domestic corporation or nonprofit corporation or foreign corporation or association and a finding by the Secretary of State that, under the circumstances, the public is not likely to be misled.

Comment. Section 5242 is new; for a comparable provision; see Section 201(b) (General Corporation Law).

Note. This section has not been adjusted to account for foreign nonprofit corporations and associations.

§ 5243. Name in which "bank," "trust," or related terms appear

5243. The Secretary of State shall not file articles setting forth a name in which "bank," "trust," "trustee," or related words appear unless the certificate of approval of the Superintendent of Banks is attached thereto.

Comment. Section 5243 continues provisions applicable to nonprofit corporations by former Section 309 through former Section 9002. For a comparable provision, see Section 201(a) (General Corporation Law).

§ 5244. Enjoining name violations

5244. The use by a nonprofit corporation of a name in violation of this article may be enjoined notwithstanding the filing of its articles by the Secretary of State.

Comment. Section 5244 continues a provision applicable to nonprofit corporations by former Section 310 through former Section 9002. For a comparable provision, see the second paragraph of Section 201(b) (General Corporation Law). It should be noted that a nonprofit corporation may not use a name that is deceptively similar to that of a domestic nonprofit association. Law v. Crist, 41 Cal. App.2d 862, 107 P.2d 953 (1941).

Article 5. Articles of Incorporation

§ 5250. Required contents of articles

5250. The articles of incorporation shall set forth:

(a) The name of the nonprofit corporation.

(b) The purposes for which the nonprofit corporation is organized.

This requirement shall not be deemed to preclude a statement of general purposes or powers or to restrict the right of the nonprofit corporation to engage in any other lawful activity.

(c) That the nonprofit corporation is organized pursuant to the General Nonprofit Corporation Law and that the nonprofit corporation shall not distribute gains, profits, or dividends to members except to the extent permitted in the General Nonprofit Corporation Law.

(d) The names and addresses of three or more persons who are to act in the capacity of first directors until the election of their successors. These persons may be given such titles as are deemed appropriate, but they shall be subject to all laws of this state relating to directors except as otherwise provided in this part.

Comment. Section 5250 supersedes former Section 9300; for a comparable provision, see Section 202 (General Corporation Law).

Subdivision (a) continues subdivision (a) of former Section 9300. For limitations on corporate names, see Article 4 (commencing with Section 5240).

Subdivision (b) eliminates the requirement of subdivision (b) of former Section 9300 of a statement of specific and primary purposes. It should be noted that a nonprofit corporation organized for charitable purposes must include a statement of specific and primary purposes. See Section \_\_\_\_\_. A nonprofit corporation may, but need not, include a statement of general purposes and powers. Absent such a general statement, subdivision (b) permits the nonprofit corporation to engage in any lawful activity, and Section 5230 confers full corporate powers.

Subdivision (c) continues subdivision (c) of former Section 9300 and adds the requirement that the articles state that the nonprofit corporation may not make distributions to members except as provided in this division. A nonprofit corporation may be formed for any lawful purpose other than to make such distributions (Section 5210), and such distributions are prohibited except to the extent provided in Section 5236.

Subdivision (d) continues the first two sentences of subdivision (e) of former Section 9300.

Note. The staff has not yet drafted the following provisions:

(1) Grandfather clause to excuse compliance with the required statement that no distributions are permissible for corporations organized between 1949 and the operative date of this act.

(2) Requirements for incorporation of charitable corporation.

(3) Laws relating to directors and exceptions for first directors named in the articles.

(4) Designation of initial agent for service of process.

CONFORMING AMENDMENTS--OUTLINE

Article 10. Nonprofit Corporations for Medical Services

Business & Professions Code § 700 (added)

Business & Professions Code § 701 (added)

Article 12. Nonprofit Corporations for Legal Services

Business & Professions Code § 6185 (added)

Corporations Code § 20004 (added)

Corporations Code § 20005 (added)

CONFORMING AMENDMENTSArticle 10. Nonprofit Corporations for Medical ServicesBusiness & Professions Code § 700 (added)

700. (a) A nonprofit corporation may be formed under the General Nonprofit Corporation Law for the purposes of defraying or assuming the cost of professional services of licentiates under any chapter of this division or of rendering any such services, but it may not engage directly or indirectly in the performance of the corporate purposes or objects unless all of the following requirements are met:

(1) At least one-fourth of all licentiates of the particular profession residing in California become members.

(2) Membership in the nonprofit corporation and an opportunity to render professional services upon a uniform basis are available to all licensed members of the particular profession.

(3) Voting by proxy and cumulative voting are prohibited.

(4) A certificate is issued to the nonprofit corporation by the particular professional board whose licentiates have become members, finding compliance with the requirements of subdivisions (1), (2), and (3).

(b) Any such nonprofit corporation shall be subject to supervision by the particular professional board under which its members are licensed and shall also be subject to Section \_\_\_\_\_ of the Corporations Code.



Comment. Section 700 continues former Corporations Code Section 9201.

Note. A new section number has yet to be assigned to Corporations Code Section 9505 (property subject to supervision by Attorney General).

Business & Professions Code § 701 (added)

701. Any nonprofit corporation formed under Section 700 which defrays or assumes some portion or all of the costs of refractions or eye appliances shall offer an equal opportunity to render professional services upon a uniform basis to all licentiates expressly authorized by law to render such services.

Comment. Section 701 continues former Corporations Code Section 9201.1.

Article 12. Nonprofit Corporations for Legal Services

Business & Professions Code § 6185 (added)

6185. (a) Nonprofit corporations may be formed under the General Nonprofit Corporation Law for the purposes of administering a system or systems of defraying the cost of professional services of attorneys, but any such nonprofit corporation may not engage directly or indirectly in the performance of the corporate purposes or objects unless all of the following requirements are met:

(1) The attorneys furnishing professional services pursuant to such system or systems are acting in compliance with the Rules of Professional Conduct of the State Bar of California concerning such system or systems.

(2) Membership in the nonprofit corporation and an opportunity to render professional services upon a uniform basis are available to all active members of the State Bar of California.

(3) Voting by proxy and cumulative voting are prohibited.

(4) A certificate is issued to the nonprofit corporation by the State Bar of California finding compliance with the requirements of subdivisions (1), (2), and (3).

(b) Any such nonprofit corporation shall be subject to supervision by the State Bar of California and shall also be subject to Section \_\_\_\_\_ of the Corporations Code.

Comment. Section 6185 continues former Corporations Code Section 9201.2.

Note. A new section number has yet to be assigned to Corporations Code Section 9505 (property subject to supervision by Attorney General).

Corporations Code § 20004 (added)

20004. (a) A corporation may be formed under the General Nonprofit Corporation Law, subject to the requirements of this section, for the purpose of incorporating any existing unincorporated association or organization. As used in this section, "unincorporated association" includes but is not limited to society, library, school, college, club, church, trustees of a charitable trust, and chamber of commerce.

(b) The articles of incorporation shall set forth the name of the existing unincorporated association.

(c) The articles of incorporation shall be subscribed by the presiding officer or acting presiding officer and the secretary or clerk or similar officer of the association or by at least a majority of its governing board or body, and there shall be attached thereto the affidavit of the subscribing officers, board, or body that the association has duly authorized its incorporation and has authorized said officers, board, or body to execute the articles of incorporation.

(d) The members of the association shall be members of the non-profit corporation so created unless they file their dissent in writing with the secretary thereof.

Comment. Subdivision (a) of Section 20004 continues former Section 9202; subdivision (a) is subject to Section 5210 (proper corporate purposes). Subdivision (b) continues subdivision (f) of former Section 9300; subdivision (b) is in addition to the requirements of Section 5250 (required contents of articles). Subdivision (c) continues subdivision (b) of former Section 9304, with the exception of the acknowledgment requirement, which is omitted as unnecessary; subdivision (c) is an exception to the provisions of Section 5221 (execution of articles). Subdivision (d) continues former Section 9604.

Note. The staff has not yet devised an appraisal remedy for dissenting members of an unincorporated association.

Corporations Code § 20005 (added)

20005. (a) A corporation may be formed under the General Nonprofit Corporation Law, subject to the requirements of this section, for the purpose of incorporating any subordinate body instituted or created under the authority of any head or national association, lodge, order, beneficial association, fraternal or beneficial society, labor union, foundation, federation, or any other society, organization, or association. The fact that the head or national body is unincorporated does not prevent the incorporation of the subordinate body.

(b) The rules governing the incorporation and operation of unincorporated associations govern the incorporation of any subordinate body.

(c) The seal of the subordinate body shall be its corporate seal.

(d) Whenever the charter of a subordinate body incorporated pursuant to this section is surrendered to, taken away, or revoked by the head or national body granting it, the subordinate body shall dissolve. After paying its debts and obligations or making adequate provision therefor, the subordinate body may collect obligations owed to it and may sell property which is not designed for the exclusive use of the organization. The subordinate body shall then deliver any remaining property or obligations owed to it and any remaining proceeds of the sale of property to the head or national body to be disposed of in accordance with the laws of the head or national body.

Comment. Subdivisions (a)-(c) of Section 20005 continue former Section 9203; for the rules governing incorporation of unincorporated associations, see Section 20004. Subdivision (d) continues former Section 9802; it is an exception to the provisions of Sections 7030-7038 (distribution of assets on dissolution of nonprofit corporation).

APPENDIX

DIVISION 2. NONPROFIT CORPORATIONS

PART 1. GENERAL NONPROFIT CORPORATION LAW

CHAPTER 1. GENERAL PROVISIONS

Corporations Code § 9000 (repealed)

9000. This part shall be known and may be cited as the General Nonprofit Corporation Law.

Comment. Former Section 9000 is continued in Section 5000.

Corporations Code § 9001 (repealed)

9001. The provisions of this part apply to every nonprofit corporation now existing or hereafter formed, unless the corporation is expressly exempted from the operation thereof, or there is a special provision applicable to the corporation inconsistent with the provisions of this part, in which case the special provision prevails,

Comment. Section 9001 is continued in Section 5111.

Corporations Code § 9002 (repealed)

9002. The provisions of the General Corporation Law, Division 1 of this title, apply to corporations formed under this part, except as to matters specifically otherwise provided for in this part.

Comment. Section 9002 is not continued. The new General Nonprofit Corporation Law, Division 2 (commencing with Section 5000) of Title 1, provides a complete set of rules governing nonprofit corporations and does not incorporate by reference the General Corporation Law.



## CHAPTER 2. FORMATION AND BYLAWS

Article 1. PurposesCorporations Code § 9200 (repealed)

9200. A nonprofit corporation may be formed by three or more persons for any lawful purposes which do not contemplate the distribution of gains, profits, or dividends to the members thereof and for which individuals lawfully may associate themselves, such as religious, charitable, social, educational, or cemetery purposes, or for rendering services, subject to laws and regulations applicable to particular classes of nonprofit corporations or lines of activity. Carrying on business at a profit as an incident to the main purposes of the corporation and the distribution of assets to members on dissolution are not forbidden to nonprofit corporations, but no corporation formed or existing under this part shall distribute any gains, profits, or dividends to any of its members as such except upon dissolution or winding up.

Comment. The portion of the first sentence of former Section 9200 relating to the purposes for which a nonprofit corporation may be formed is superseded by Section 5210; the portion relating to the number of incorporators is superseded by Section 5220.

The portion of the second sentence of former Section 9200 permitting carrying on business at a profit is superseded by Section 5235; the portion precluding distributions to members of gains, profits, or dividends as such is continued in Section 5236(a); the portion permitting distribution of assets on dissolution or winding up is continued in Section 5236(b).

Corporations Code § 9201 (repealed)

9201. A nonprofit corporation may be formed under this part for the purposes of defraying or assuming the cost of professional services of licentiates under any chapter of Division 2 (commencing with Section 500) of the Business and Professions Code or of rendering any such services, but it may not engage directly or indirectly in the performance of the corporate purposes or objects unless all of the following requirements are met:

(a) At least one-fourth of all licentiates of the particular profession residing in California become members.

(b) Membership in the corporation and an opportunity to render professional services upon a uniform basis are available to all licensed members of the particular profession.

(c) Voting by proxy and cumulative voting are prohibited.

(d) A certificate is issued to the corporation by the particular professional board whose licentiates have become members, finding compliance with the requirements of subdivisions (a), (b), and (c).

Any such nonprofit corporation shall be subject to supervision by the particular professional board under which its members are licensed and shall also be subject to Section 9505.

Comment. Former Section 9201 is continued in Business and Professions Code Section 700.

Corporations Code § 9201.1 (repealed)

9201.1. Any nonprofit corporation formed under Section 9201 which defrays or assumes some portion or all of the costs of refractions or eye appliances shall offer an equal opportunity to render professional services upon a uniform basis to all licentiates expressly authorized by law to render such services.

Comment. Former Section 9201.1 is continued in Business and Professions Code Section 701.

Corporations Code § 9201.2 (repealed)

9201.2. Nonprofit corporations may be formed under this part for the purposes of administering a system or systems of defraying the cost of professional services of attorneys, but any such corporation may not engage directly or indirectly in the performance of the corporate purposes or objects unless all of the following requirements are met:

(a) The attorneys furnishing professional services pursuant to such system or systems are acting in compliance with the Rules of Professional Conduct of the State Bar of California concerning such system or systems.

(b) Membership in the corporation and an opportunity to render professional services upon a uniform basis are available to all active members of the State Bar.

(c) Voting by proxy and cumulative voting are prohibited.

(d) A certificate is issued to the corporation by the State Bar of California, finding compliance with the requirements of subdivisions (a), (b) and (c).

Any such nonprofit corporation shall be subject to supervision by the State Bar of California and shall also be subject to Section 9505.

Comment. Former Section 9201.2 is continued in Business and Professions Code Section 6185.

Corporations Code § 9202 (repealed)

9202. A nonprofit corporation may be formed for the purpose of incorporating any existing unincorporated association or organization. As used in this part "unincorporated association" includes but is not limited to society, library, school, college, club, church, trustees of a charitable trust, and chamber of commerce.

Comment. Former Section 9202 is continued in Section 20004(a).

Corporations Code § 9203 (repealed)

9203. A nonprofit corporation may be formed for the purpose of incorporating any subordinate body instituted or created under the authority of any head or national association, lodge, order, beneficial association, fraternal or beneficial society, labor union, foundation, federation, or any other society, organization, or association. The fact that the head or national body is unincorporated does not prevent the incorporation of the subordinate body.

The rules governing the incorporation and operation of unincorporated associations govern the incorporation of any subordinate body.

The seal of the subordinate body shall be its corporate seal.

Comment. Former Section 9203 is continued in Section 20005.

Article 2. Articles of IncorporationCorporations Code § 9300 (repealed)

9300. The articles of incorporation shall set forth:

(a) The name of the corporation.

(b) The specific and primary purposes for which it is formed.

This requirement shall not be deemed to preclude a statement of general purposes or powers or to restrict the right of the corporation to engage in any other lawful activity.

(c) That the corporation is organized pursuant to the General Nonprofit Corporation Law or pursuant to Part 1 of Division 2 of Title 1 of the Corporations Code.

(d) The county in this state where the principal office for the transaction of business of the corporation is located.

(e) The names and addresses of three or more persons who are to act in the capacity of directors until the selection of their successors. These persons may be given such titles as are deemed appropriate, but they shall be subject to all laws of this state relating to directors except as otherwise provided in this part. The number of persons so named constitutes the number of directors of the corporation, until changed by an amendment to the articles or, unless the articles otherwise provide, by a bylaw adopted by the members. However, the articles or, unless the articles provide otherwise, a bylaw duly adopted by the members, may state that the number of directors shall be not less than a stated minimum (which in no case shall be less than five) nor

more than a stated maximum (which in no case shall exceed such stated minimum by more than three); and in the event that the articles or bylaws permit such an indefinite number of directors, the exact number of directors shall be fixed, within the limits specified in the articles or bylaws, by a bylaw or amendment thereof duly adopted by the members or by the board of directors. In the event the articles provide for an indefinite number of directors, unless the articles provide otherwise, such indefinite number may be changed, or a definite number fixed without provision for an indefinite number, by a bylaw duly adopted by the members.

(f) If an existing unincorporated association is being incorporated, the name of the existing unincorporated association.

Comment. Section 9300 is superseded by Section 5250. Subdivision (a) is continued in Section 5250(a). Subdivision (b) is continued in Section 5250(b) with the exception of the "specific and primary purposes" requirement, which is not continued. Subdivision (c) is continued in Section 5252(c). Subdivision (d) is not continued. The first two sentences of subdivision (e) are continued in Section 5250(d); the remainder of subdivision (e) is continued in Section \_\_\_\_\_. Subdivision (f) is continued in Section 20004(b).



Corporations Code § 9304 (repealed)

9304. (a) Except in the case of the incorporation of an unincorporated association provided for in subdivision (b) hereof, each person named in the articles to act in the capacity of a first director shall, and any other person desiring to associate with those persons in the formation of the corporation may, personally sign the articles of incorporation. All signatures thereto shall be personally acknowledged before an officer designated by the laws of this State as one before whom an acknowledgment may be made. Any certificate of acknowledgment taken without the State shall be authenticated by the certificate of an officer having the requisite official knowledge of the qualification of the officer before whom the acknowledgment was made when taken before any officer other than a notary public or a judge or clerk of a court of record having an official seal.

(b) In the case of the incorporation of an unincorporated association, the articles of incorporation shall be subscribed and execution thereof personally acknowledged before an officer authorized to take acknowledgments by the presiding officer or acting presiding officer and the secretary or clerk or similar officer of the association or by at least a majority of its governing board or body, and there shall be attached thereto the affidavit of the subscribing officers, board or body that the association has duly authorized its incorporation and has authorized said officers, board or body to execute the articles of incorporation.

Comment. The first sentence of subdivision (a) of former Section 9304 is superseded by Section 5221; the second and third sentences are not continued. Subdivision (b) is continued in Section 20004(b) with the exception of the acknowledgment requirement which is not continued.

Corporations Code § 9304.5 (repealed)

9304.5. If the articles conform to law, the Secretary of State shall file them in his office and shall endorse the date of filing thereon. The corporate existence begins upon the filing of the articles and continues perpetually unless otherwise expressly provided by law.

A copy of the articles certified by the Secretary of State and bearing the endorsement of the date of filing in this office shall be filed in the office of the county clerk of the county in which the corporation is to have its principal office and in the office of the county clerk of each county in which the corporation acquires ownership of any real property.

Comment. The first sentence of former Section 9304.5 is continued in Section 5115. The second sentence is continued in Section 5222. The third sentence is not continued.

## CHAPTER 4. MEMBERS

Corporations Code § 9604 (repealed)

9604. If an unincorporated association is incorporated under this part, the members of the association shall be members of the corporation so created, unless they file their dissent in writing with the secretary thereof.

Comment. Former Section 9604 is continued in Section 20004(d).