

First Supplement to Memorandum 76-7

Subject: Study 77.20 - Nonprofit Corporations (Organization--De Facto Corporations)

At common law, a de jure corporation could be formed only by complying with all technical statutory requirements of formation. Nonetheless, an organization in corporate form that was defectively incorporated could render itself immune from collateral attack on its existence through proof of de facto corporate existence, which required: (1) a statute under which the organization was purported to be incorporated, (2) a good faith attempt to organize under the statute, (3) reasonable compliance with the requirements of the statute, and (4) actual use of corporate powers. Likewise, such a de facto corporation is estopped to deny its existence when sued by a person who acted in reliance on the fact of its existence.

In California, legislation has made it largely unnecessary to resort to the common law doctrine of de facto corporations and corporations by estoppel where the organization has filed articles of incorporation. The following discussion of Section 313, which is continued in the new General Corporation Law as Section 209. and which is fully applicable to nonprofit corporations (see, e.g., Barber v. Irving, 226 Cal. App.2d 560, 38 Cal. Rptr. 142 (1964)), is drawn from 1 Ballantine & Sterling, California Corporation Laws §§ 40-41 (4th ed. 1975).

The act of the Secretary of State in filing the articles, even though done under an erroneous view of the legal requirements for incorporation, the availability of the name chosen, or the sufficiency of the articles or their execution, will be effective under statute to create a corporation good against all the world except against direct attack by the state in an action in the nature of quo warranto. It would be highly unjust to those who deal with

ostensible corporations to make it incumbent upon them to ascertain whether organizers have proceeded in strict or substantial conformity with all statutory requirements in the procedure of incorporation. It would be intolerable that corporations should be subject to attack as to their existence by those who deal with them on the ground of some omission, defect, or irregularity in their creation which has no relation to the merits of the case or the transaction in hand. An action by the Attorney General upon his own information or upon complaint by a private party may be brought against any corporation, either de jure or de facto, which usurps or unlawfully holds or exercises any franchise within the state.

The action in the nature of quo warranto is provided in Section 803 of the Code of Civil Procedure:

803. An action may be brought by the attorney-general, in the name of the people of this state, upon his own information, or upon a complaint of a private party, against any person who usurps, intrudes into, or unlawfully holds or exercises any public office, civil or military, or any franchise, or against any corporation, either de jure or de facto, which

usurps, intrudes into, or unlawfully holds or exercises any franchise, within this state. And the attorney-general must bring the action, whenever he has reason to believe that any such office or franchise has been usurped, intruded into, or unlawfully held or exercised by any person, or when he is directed to do so by the governor.

Even under this procedure for direct attack on corporate existence by the state, substantial compliance with the incorporation procedure will be a sufficient defense.

The staff believes that existing law on this subject is adequate and recommends that no changes be made. See the attached draft.

Respectfully submitted,

Nathaniel Sterling
Assistant Executive Secretary

§ 5223. Evidence of corporate formation and existence

5223. For all purposes other than an action in the nature of quo warranto, a copy of the articles of a nonprofit corporation duly certified by the Secretary of State is conclusive evidence of the formation of the corporation and prima facie evidence of its corporate existence.

Comment. Section 5223 continues provisions applicable to nonprofit corporations by former Section 813 through former Section 9002. See, e.g., Barber v. Irving, 226 Cal. App.2d 560, 38 Cal. Rptr. 142 (1964); see also Cavin Memorial Corp. v. Requa, 5 Cal. App.3d 345, 85 Cal. Rptr. 107 (1970). For a comparable provision, see Section 209 (General Corporation Law). For an action in the nature of quo warranto, see Section 803 of the Code of Civil Procedure.