

First Supplement to Memorandum 2000-69

Uniform Unincorporated Nonprofit Association Act (Comments of State Bar and Discussion of Issues)

On July 18, 2000, R. Bradbury Clark of the State Bar Nonprofit Organizations Committee (“the Committee”) wrote to express the Committee’s interest in this study and to recommend that the Commission carefully consider: (1) the extent to which any changes to the law of unincorporated association should apply to both for-profit and nonprofit associations, and (2) whether it would be appropriate to add default rules governing the organization, governance, and termination of unincorporated associations. See First Supplement to Memorandum 2000-44. The staff asked Mr. Clark for further detail regarding the Committee’s suggestions. We have received a letter from Mr. Clark, writing on behalf of himself and members of his committee, addressing these points and others (attached). Key points in the letter are discussed below.

SCOPE OF STUDY

In its initial analysis of the Uniform Act and California law, the staff recommended against wholesale enactment of the Uniform Act. The Uniform Act is not a comprehensive scheme for regulation of unincorporated associations, addressing only a small number of important issues. Many of those issues are already addressed by existing California law. The staff felt that enactment of the Uniform Act as a whole would be disruptive, without offering any obvious benefit over existing law. Instead, the staff recommended review of existing law to identify marginal improvements that could be made.

The Committee encourages the Commission to take a more ambitious approach, proposing the creation of a comprehensive set of statutes governing unincorporated associations (see Exhibit pp. 1-2):

We believe that the Commission has and must seize the excellent opportunity this project provides to make a much needed and extremely important revision of California law.

California statutory law as to unincorporated associations is fragmentary and confusing, really just a patchwork of a few

provisions, mostly in the Corporations Code and the Code of Civil Procedure. that law badly needs revision for clarity and cohesion — not to say consistency — and major expansion to fill existing gaps.

The need and opportunity are important. Despite the large number of these organizations of widely varying purposes and make-up, our experience is that very few persons — participants, lawyers and courts included — have a meaningful understanding of the governing rules (such as they are) as to formation; organization; governance; management; dissolution; and liability of members, managers and associations; to mention only some aspects. Those rules are now embodied in the few fragments of statutory coverage and in judicial decisions scattered over many years and it is not surprising that they are so poorly understood.

Most other widely used forms of organization have detailed governing laws that cover these aspects, e.g., business corporations, nonprofit corporations, consumer cooperative corporations, general and limited partnerships and limited liability companies. These other laws provide quite comprehensive rules on the above and related matters. Some of their provisions are mandatory. Also, however, and of great importance to organizational flexibility, many can be changed by agreement or provide “default” rules that can be adopted by inaction or that apply if an organization has simply failed to cover a particular matter. Those who operate through unincorporated associations deserve the same treatment.

The Uniform Unincorporated Association Act (“Uniform Act”) could have but does not fill that need. It does have some provisions that could be used, along with some existing California provisions, to create a comprehensive law that would fill that need.

...

We support the Commission’s undertaking of this project. We urge it to seize its opportunity to sponsor a much needed expansion of California law to fill a vacuum and provide statutory support to the widely used unincorporated association like that provided other types of private organizations. We also stand ready to provide whatever help we can to the Commission in this task.

As an organizational matter, the staff sees no problem with the creation of a comprehensive statute governing unincorporated associations. In fact, most of the statutes governing unincorporated associations are already clustered together in a contiguous series in the Corporations Code. It would be a simple matter to reorganize them into a more accessible scheme.

However, the Committee’s proposal goes beyond improving the *organization* of the statutes. They would like to see provisions added to create default governance rules and protections from liability for association members and

officers, and would like those rules to apply to all unincorporated associations that are not subject to other statutory schemes. The Committee's proposals are discussed below.

DEFINITIONS

Integral to the Committee's proposal are the proposed definitions of "association," "member," and "constitution." The Committee's proposed governance provisions would rely heavily on these defined terms.

The staff agrees that existing definitions should be improved. Clear and broadly applicable definitions would help eliminate repetitive and awkward definitional language that exists in many of the unincorporated association statutes. See, e.g., Corp. Code § 20001 ("any unincorporated society or association, and every lodge or branch of any such society or association, and any labor organization").

The Committee's proposed definitions are discussed briefly below:

"Association"

"Association" would be defined broadly:

"Association" means an association or organization or agreement of two or more persons that (1) is not or does not establish a corporation, a general or limited or limited liability partnership, a limited liability company, [trust?] or other organization formed under any statute of this state or other jurisdiction other than this or a similar act and (2) is formed to carry on a lawful activity as specified in its constitution.

See Exhibit p. 9. In other words, an "association" is any unincorporated organization (with a lawful purpose) that is not formed pursuant to another statute.

The staff sees a few potential problems with this definition:

- (1) The definition appears to include common law for-profit associations (i.e., a joint venture, joint stock company, or business trust). It may be inappropriate to apply the same rules to such entities as are applied to nonprofit associations (e.g., liability limitations).
- (2) Use of the term "association" to define "association" is circular.
- (3) The term "agreement" is perhaps too open-ended. Many agreements to carry out lawful activities are not intended to create separate legal entities. Perhaps, the problem of determining which

agreements create separate entities could be addressed by incorporating Professor Hone's suggestion that an association must "operate under a common name." See Memorandum 2000-44 at p. 6. Operation under a common name would indicate a subjective intention to form a group, rather than a simple agreement between individuals to perform some activity together.

For the most part these are technical problems that can probably be resolved by further refinement of the drafting.

"Member"

The Committee would define "member" as follows:

"Member" of an association means, at any time, a person whom the association's constitution provides is a member of it, who by affirmative act or conduct has accepted membership and whose membership has not terminated by expiration, cancellation or resignation. Unless otherwise provided in an association's constitution, a person is a member of it if that person has rights to vote for or select the association's manager(s) or managing body or (2) in the absence of designated manager(s) or managing body, has the right under the association's constitution to participate in its management, or (3) has the right under the association's constitution to vote on changes to the constitution or on dissolution of the association.

See Exhibit p. 9. The intent is to defer to the association's constitution "unless the constitution does not cover membership explicitly." *Id.* This seems like a reasonable approach.

"Constitution"

The Committee would define "constitution" as follows:

"'Constitution' means the organizational documentation or, in the absence of such documentation, the governing understanding or agreement (whether written or oral) pursuant to which an association is formed or under which it operates, as such documentation, understanding or agreement is in effect or amended from time to time."

See Exhibit p. 10. Inclusion of an oral agreement in the definition is consistent with the Committee's desire to establish a comprehensive statute, applicable by default to all organizations that are not subject to other law. The Commission should consider whether recognition of an oral constitution could create problems.

GOVERNANCE

Under existing law, there are no statutes governing the creation, governance, or dissolution of an unincorporated association. The Committee believes that these matters should be left to the organization's constitution if addressed by the constitution. In the absence of a constitutional provision, the Committee believes that certain default rules should apply. The Committee's letter includes a brief outline of the proposed governance provisions, which can also serve as an outline of a comprehensive unincorporated associations law. See Exhibit pp. 5-8.

The staff has a general concern about the proposed approach: what is the consequence if an unincorporated association fails to abide by an applicable default governance rule? For example, the Committee proposes a default quorum requirement of some percentage of those with voting rights [one-third]. See Exhibit p. 6. Suppose that an informally organized association routinely meets and makes decisions with fewer members than the number required by the default quorum rule. It's "constitution" is silent as to quorum requirements. Are the association's actions valid? If the association decides to enter into a contract, without the required number of voting members, would the contract be valid? Care must be taken to ensure that default governance rules do not create problems for associations that are unaware of them.

Despite the staff's concern, there would be cases where default governance provisions would be useful. For example, the staff previously proposed development of a rule governing disposition of association property on dissolution of the association. Under the proposed rule, the matter would be governed by the association's constitution, if it contains an applicable provision. If it does not, then default rules would apply to determine whether the property can be distributed to members or must be dedicated to some purpose similar to that of the dissolved association. See Exhibit p. 8 for a similar proposal by the Committee. This type of rule would be very helpful for resolving disputes over the disposition of association property.

The Commission should consider adding default governance provisions to existing law, keeping in mind any adverse consequences that might result from failure to abide by the default rules.

LIABILITY

Under existing law, the contract and tort liability of members of an unincorporated association is governed by common law agency principles, as modified by certain statutory limits. See the main memorandum for a discussion of these laws. The Committee proposes statutory liability rules for members and managers of an unincorporated association. These are discussed below:

Members

The Committee proposes providing members of an unincorporated association with the same liability protection afforded members of a limited liability company (LLC):

As to members, the Limited Liability Company Act handles their liability in a direct way. Members of an LLC are not liable for its obligations except (1) for liability based on alter ego concepts, (2) if a corporate shareholder would be liable for an obligation of the corporation, (3) liability for personal participation in a tortious act, (4) if the member agrees to be liable, and (5) to return a distribution of property if necessary to protect creditors. This general exculpation and its exceptions would accord with normal expectations of participants and of claimants against an association who have dealt with or been harmed by it.

See Exhibit p. 10; Corp. Code § 17101 (liability of LLC member). In the short period the staff has had to consider this proposal, it has identified a few issues:

- (1) In an informally organized organization, how would one establish that an association was a member's alter ego? For example, commingling of personal funds and association funds may be a common practice in small organizations that lack the resources to establish separate financial systems.
- (2) Under the Committee's proposal, the limitation on member liability for contracts would be broader. Under existing agency principles, a member would apparently be liable where the member expressly authorizes creation of a contract. A member might also be liable on the basis of implied ratification of a contract, if the member knowingly accepts the benefit of the contract. Under the Committee's proposal, the member would not be liable in either case.
- (3) Is general exculpation consistent with most parties' expectations when dealing with an unincorporated association? An LLC is a registered entity, which identifies itself as an LLC, and which is required to "carry insurance or provide an undertaking to the same

extent and in the same amounts as is required by any law, rule, or regulation of this state that would be applicable to the limited liability company ... were it a corporation.” Corp. Code § 17101(d). An unincorporated association can be a thoroughly informal organization with no written governing documents, is not required to identify itself as having limited liability, and is not required to carry insurance. Would it be fair to insulate the members of an unincorporated association from liability to the same extent as members of an LLC?

Managers

The Committee proposes applying LLC principles to the liability of the managers of an unincorporated association:

It provides managers/officers are not personally liable solely by reason of being a manager/officer. This leaves open the reasonably well developed law that a person who directly commits or participates in a wrong may be personally liable for that personal action. A good many unincorporated associations will have officers and managers, who ought to have protection from liability akin to that in other entity-like organizations.

See Exhibit p. 11; Corp. Code § 17158 (liability of managers and officers of LLC).

Tentatively, the staff agrees that a manager or officer should not be liable solely as a consequence of being a manager or officer. This is consistent with agency law, under which an agent is not generally liable for a contract entered into on behalf of the principal, or for a principal’s tort of which the agent is innocent. See 2 B. Witkin, Summary of Cal. L. Agency §§ 145, at 141, 151, at 145 (9th ed. 1987).

CONCLUSION

The staff appreciates the thoughtful and creative work that the Committee has put into its proposals. They deserve careful consideration. The staff also welcomes the Committee’s offer to provide additional assistance to the Commission. This supplement has only addressed the principal suggestions made by the Committee in its letter. With respect to those suggestions, the staff makes the following general recommendations:

- (1) *Comprehensive approach.* The staff recommends that the Commission approach this project from the perspective of developing a comprehensive “Unincorporated Associations Act.” The organization of existing provisions of the Corporations Code could

be improved with little effort. Considering how infrequently these statutes are cited, it is unlikely that there would be any opposition based on concerns about disrupting the existing system (and section numbering). Decisions regarding which types of provisions should be added to existing law can be made as the relevant substantive issues are considered in the course of this study.

- (2) *Definitions.* The staff recommends that existing definitions be revised and their application clarified. Conforming changes should be made to the unincorporated association statutes to clear out duplicative definitional language. The Commission may wish to provisionally adopt the definitions proposed by the Committee, as a starting point for discussion by interested parties. Special attention should be paid to how inclusive the definition of “association” should be and whether including oral agreements in the definition of “constitution” will cause problems.
- (3) *Governance provisions.* The staff has no general objection to creating default governance provisions. However, careful consideration will need to be given to the consequences of failing to abide by a default rule. This will require further elaboration and analysis of the specific proposals for consideration by the Commission.
- (4) *Liability of members and managers.* The Committee’s proposed limitation on the liability of members raises some serious issues and should be the subject of further analysis and consideration. The proposed limitation on the liability of managers and officers appears reasonable, but should also be the subject of further analysis.

If the Commissions agrees with the general recommendations set out above, the staff will prepare a skeletal draft of a Unincorporated Associations Act and begin analysis of the possible components of that act, for the Commission’s consideration.

Respectfully submitted,

Brian Hebert
Staff Counsel



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Re: Uniform Unincorporated Association Act

Ladies and Gentlemen:

INTRODUCTION

I am writing as a member of the Nonprofit Organizations Committee ("Committee") of the Business Law Section of the State Bar of California and on behalf of Committee members whose practice includes "unincorporated associations"¹ about the above Commission Project. We believe that the Commission has and must seize the excellent opportunity this project provides to make a much needed and extremely important revision of California law.

California statutory law as to unincorporated associations is fragmentary and confusing, really just a patchwork of a few provisions, mostly in the Corporations Code and the Code of Civil Procedure. That law badly needs revision for clarity and cohesion – not to say internal consistency – and major expansion to fill existing gaps.

The need and opportunity are important. Despite the large number of these organizations of widely varying purposes and make-up, our experience is that very few persons -- participants, lawyers and courts included -- have a meaningful understanding of the governing rules (such as they are) as to formation; organization; governance; management; dissolution; and liability of members, managers and associations; to mention only some aspects. Those rules are now

¹ The comments and suggestions in this letter are those of the writer and members of the Committee. They represent the general views of the Committee, but do not represent positions of the overall Business Law Section or the State Bar, which have taken no position on these matters.

embodied in the few fragments of statutory coverage and in judicial decisions scattered over many years and it is not surprising that they are so poorly understood.

Most other widely used forms of organization have detailed governing laws that cover these aspects, e.g., business corporations, nonprofit corporations, consumer cooperative corporations, general and limited partnerships and limited liability companies. These other laws provide quite comprehensive rules on the above and related matters. Some of their provisions are mandatory. Also, however, and of great importance to organizational flexibility, many can be changed by agreement or provide "default" rules that can be adopted by inaction or that apply if an organization has simply failed to cover a particular matter. Those who operate through unincorporated associations deserve the same treatment.

The Uniform Unincorporated Association Act ("Uniform Act") could have but does not fill that need. It does have some provisions that could be used, along with some existing California provisions, to create a comprehensive law that would fill that need.

In what follows, this letter will:

1. Discuss aspects of the Uniform Act.
2. Respond to the two questions that the Commission asked R. Bradbury Clark: what "for profit" associations should be covered and what statutory governance provisions are needed? Governance provisions are so important and so pervasive that the response to the latter question has to include an outline of minimally but adequate comprehensive statutory provisions for unincorporated associations.
3. Make suggestions as to key definitions and liability of members and managers of unincorporated associations.
4. Comment on the Commission's decisions as reported in the minutes of its July meeting.
5. Comment on Mr. Hebert's study B-500 (Memorandum 2000-69) dated September 22, 2000 in a preliminary way.

THE UNIFORM ACT

The Uniform Act does not purport to provide coverage comparable to even a scaled down and minimal general corporation, partnership or limited liability act. Many provisions those acts contain would not be necessary in an unincorporated association act if (as seems acceptable) no required public filings are contemplated and the act is designed simply to enable associations to organize, exist and dissolve; to provide "default" rules for those organized without constitutions of good scope; and to provide for rights and liabilities of associations and their participants among themselves and vis-à-vis third parties.

Many of the shortcomings of the Uniform Act were pointed out while it was still being drafted and later after it had been promulgated. See, for example, the letter from this Committee to Messrs. Lieman and Ruud dated July 20, 1991, distributed to the Commission sometime ago.

Despite what we see as its major shortcoming, the Uniform Act includes some material that could be used in a more comprehensive and adequate statute. The following are brief notes as to this:

- Section 1 - (Definitions) See below in this letter.
- Section 2 - (Supplemental General Provisions . . .) Any problem? (I haven't thought of any).
- Section 3 - (Territorial Application) May need more thought.
 - check with real estate specialists, title insurance companies, etc.
 - accompanying law needs to provide adequate provisions as to governance, authorizations, etc., for this provision to be really useful.
 - does it need some requirement for filing (as opposed to permission to file) if an association is to own real property? Corp. Code § 24003 already provides for permissive filing of a statement with Secretary of State.
- Section 4 - (Real and Personal Property; Nonprofit Association as Legatee, etc.) See comments on Section 3; should Section 3 be combined with 4(a)?
- Section 5 - (Statement of Authority as to Real Property) Needs thought and probably different details. Consider adapting Corp C. § 16303 – partnership general statement of authority. Any other provision for statements (Cf. Corp. C. §§ 16304, 16704, 16805) desirable?
- Section 6 - (Liability in Tort and Contract) See separate coverage below.
- Sections 7, 8,
11, 12, 13 - (Various provisions relating to litigation) Would need coordination with existing California statutes re litigation.
- Section 9 - (Disposition of Personal Property of Inactive Nonprofit Association) Needs to be replaced by more detailed provisions on dissolution, merger, etc. See below.
- Section 10 - (Appointment of Agents, Service of Process) Revise to be similar to other Corporations Code provisions (e.g., Corp. C. §§ 1502(b), 1503).
- Section 11 - (Claim not abated, etc.) Needs integration with other provisions of enlarged Act.

Section 12 - (Venue) See above; also this would probably need default provision to apply where an association has no officer.

Sections 14 –
20 (Various general provisions) Would be dealt with in enlarged act in much the same way.

THE COMMISSION'S REQUESTS FOR INFORMATION

The Commission asked for information on two matters.

Coverage of For Profit Associations

First, what for profit associations should be covered? My suggestion should have been phrased to refer to coverage of associations other than “nonprofit” associations.

California statutory provisions that refer to “unincorporated associations” by that description (i.e., other than the statutes governing partnerships, limited liability companies, etc.) are not now limited to “nonprofit associations”. See Parts 1 and 5 of Division 3 of the Corporations Code, especially § 24000, quoted on page 2 of Mr. Hebert’s Memorandum 2000-69. See also various provisions of the Code of Civil Procedure, whose inclusion of unincorporated associations is not limited to “nonprofit” associations (See list of sections on page 5 of Staff Recommendations attached to Mr. Hebert’s Memorandum). A few provisions are limited to what they call “nonprofit associations”. See Corp. Code § 21000; this section limits its definition of “nonprofit association” to associations of “natural persons” for various stated purposes but includes “other purposes not that of pecuniary profit”. That phrase leaves open inclusion of associations for unclassified purposes, including purposes which could be for profit other than pecuniary. It leaves out associations with members that are not natural persons.

Efforts to define “nonprofit” as applied to unincorporated bodies have proved frustrating and more often than not have been abandoned. The drafters of the California Nonprofit Corporation Law did so. The Uniform Partnership Act’s definition of partnership uses the phrase “association to carry on a business for profit”, without defining “association”, “business” or “for profit”. Presumably, for example, an association of two or more persons to carry on a business without a profit motive would not be a partnership. There are many such businesses, as demonstrated by those that are incorporated as “nonprofit” corporations. Similar businesses can be and are carried on without incorporation. These and many other types of unincorporated activities that are not clearly “nonprofit” or “not for profit” would not be partnerships and seem entitled to statutory recognition by an appropriately comprehensive statute.

Some examples of organizations that are not covered by other statutory schemes but are, at least not clearly, not “non profit “ because they are designed to carry on a business, or provide valuable benefits to their members that sometimes are tangible and sometimes intangible but are not a “business [carried on] for profit”, follow:

1. As already noted, most unincorporated activities that would be mutual benefit corporations if incorporated.
2. Trustees that manage property or engage in commerce, such as a trust managing property or a business trust.
3. Some bar or professional organizations (the American Bar Association was unincorporated until a few years ago).
4. Some joint ventures.
5. Couples who register with the Secretary of State under Division 3 of the Corporations Code.
6. Some fraternal orders, lodges or societies. Corporations Code §§ 21300-21310 cover some of those but only as to use and protection of their insignia.
7. A garden or agricultural club that operates a plot of ground to grow crops for its participants or an unincorporated organization that cooperatively pools skills or produces or sells goods, in each case for the benefit of its members or proprietors. These might not make a pecuniary profit, but their members or proprietors can and often do use them in their own economic activities.

Because of the huge variety of purposes and forms of unincorporated human activity, the above list could go on, but the examples demonstrate the need for better statutory support than California now does, or the Uniform Act would, provide.

Accordingly, California's unincorporated association law should not only include many "default" rules as to associations it covers but it also should itself be a default law, picking up such associations not formed under or governed by some other law.

Governance Provisions

Second, governance provisions should be part of California's statutory unincorporated association law. A brief outline of minimal but adequate governance provisions follows. Because of their pervasiveness in such an act, this outline actually is also a brief outline of that overall act.

Definitional

- Define member, association, constitution, person, manager and perhaps other terms as dictated by detailed drafting. These terms are key underpinnings not only of governance provisions but also of most other parts of the act.
- See below (pages 9 and 10) as to definitions of association, member and constitution.

- Some definitions in current law or the Uniform Act could be used or adopted.

Formation [and continuation]

- Formation – effective upon execution of organization documentation, or entering into governing understanding or agreement (whether written or oral), which in either case become association's constitution.
- Continuation – as provided in constitution² or, if not provided, until purpose accomplished and association dissolved or discontinued (see below).
- Name: any requirement for name if no real estate owned?
- Permit identifying public filings with Secretary of State and possibly with County Recorders.

Status and Powers

- Confirm status as entity.
- Powers are as provided in constitution or if not provided, those of a natural person to carry out association's purposes.

Members

- Admission as provided by constitution or, if not provided, default rules in definition of "member" apply. See pages 9 and 10 below.
- Rights as provided in constitution or, to the extent not inconsistent with it:
 - 1 vote per member on matters subject to member vote.
 - no proxies.
 - Equal rights to participate in management akin to those of partner under UPA.
- Meetings as provided in constitution or, if not provided:
 - call by greater of [1 member] or [___% of members].
 - quorum [one-third] of voting power.
 - procedure:

² The repetition of "as provided . . ." in these materials would be replaced in the Act by a section like Corp. Code § 16103 of UPA, which provides that relations between partners and the partnership are governed by partnership agreement except for a few mandatory provisions specified in that Act.

- members present select presiding officer.
- follow fair-minded procedures for efficient dispatch of business.
- action by majority of quorum is action by members.
- business:
 - selection of managers if association has managers.
 - operational matters if members manage association.
 - changes in constitution.
 - merger (if allowed).
 - dissolution.
 - other as provided in notice.
- Action without meeting as provided in constitution or if not provided, by writing executed by greater of a majority of quorum or larger number acting.
 - Anything that could be done at a meeting.
- Liability – see below (pages 10 and 11)
- Termination – as provided in constitution, or if not provided:
 - automatic – failure to exercise voting rights for [one year][other?] after notice of one or more voting events or failure to reaffirm membership for one year after [receipt][giving] of request to do so.
 - automatic – expiration of term if term specified.
 - resignation by member.

Management

- By all members (see above), some of members or non-members, each as provided in constitution or, if not provided, by members (see above).

Amendments to Constitution

- As provided in constitution or, if not provided, by (1) [majority] [other] of (2) [all members] [some number or percentage of members], (3) [voting at meeting with quorum present] [consenting in writing to amendment].

Merger and Business Combination

- Most California business and nonprofit entities may merge with each other if the law under which they are organized authorizes such a merger.
- Unincorporated associations are not now authorized to merge but there seems to be no reason not to authorize them to do so.
- If authorized, merger approval would require same approval as described for amendments to constitution.

Dissolution/Discontinuance

When – as provided in constitution or upon approval of members.

Approval – Same as for amendments to constitution.

Procedures – wind up any remaining affairs as provided in constitution or, if not provided, by members, or their appointed agents, who shall:

- provide for any obligations of organization (required whether or not specified in constitution).
- distribute any remaining assets ratably among members.
- provide for custodian of records for [10 years], to be available for inspection by members and former managers.

Discontinuance – If activities of association have been discontinued or abandoned for [three years] [other] any member shall have power, in concert with any other members who desire to participate, to wind up its efforts, provide for its obligations and distribute remaining property in accordance with any charitable purposes, applicable trust purpose or the constitution of the association or, if none applicable, to remaining members pro rata.

Other provisions

Various implementing provisions would also be required. See, e.g., sections 3, 14-20 of Uniform Act and general provisions of other acts in Corporations Code.

To extent not subsumed in other provisions of the law, existing statutory provisions for particular kinds of associations could be preserved (e.g., Corp. Code § 21200 et. seq. re medical associations).

DEFINITION OF ASSOCIATION, MEMBER AND CONSTITUTION

These three definitions are so important to a good unincorporated association act that they are singled out for special attention here.

Definition of "Association"

Uniform Act § 1(2) defines a "nonprofit association" as "an unincorporated organization consisting of [two] or more members joined by mutual consent for a common, nonprofit purpose. However, joint tenancy, tenancy in common, or tenancy by the entireties does not by itself establish a nonprofit association, even if the co-owners share use of the property for a nonprofit purpose."

A better definition, consonant with suggestions in this letter, would be:

"Association" means an association or organization or agreement of two or more persons that (1) is not or does not establish a corporation, a general or limited or limited liability partnership, a limited liability company, [trust?] or other organization formed under any statute of this state or other jurisdiction other than this or a similar act and (2) is formed to carry on a lawful activity as specified in its constitution.

The Uniform Act definition seems to beg the question by its use of the word "organization", while the suggested one is generic enough to pick up the myriad of forms that a "default" law for these organizations should. The suggested definition also leaves out any references to nonprofit but excludes organizations covered by the laws that govern other common unincorporated groups. The suggested definition would also replace the several inconsistent (or, charitably, just different) definitions now in California law.

Definition of "Member"

Uniform Act § 1(1) defines a "member" as "a person who, under the rules or practices of a nonprofit association, may participate in selection of persons authorized to manage the affairs of the nonprofit association or in the development of policies of the nonprofit association."

A better definition, consonant with suggestions in this letter, is:

"Member" of an association means, at any time, a person whom the association's constitution provides is a member of it, who by affirmative act or conduct has accepted membership and whose membership has not terminated by expiration, cancellation or resignation. Unless otherwise provided in an association's constitution, a person is a member of it if that person has rights to vote for or select the association's manager(s) or managing body or (2) in the absence of designated manager(s) or managing body, has the right under the association's constitution to participate in its management, or (3) has the

right under the association's constitution to vote on changes to the constitution or on dissolution of the association.”

The suggested definition defers primarily to the association's constitution without specifying any mandatory or exclusive rights required for membership or that bestow membership unless the constitution does not cover membership explicitly. It also avoids the ambiguity of the word “participate” in the Uniform Act's definition.

A governance provision should provide a default rule as to a member's rights in the absence of provision by the association.

Definition of “Constitution”

Neither the Uniform Act nor California law covers this important and pervasive definition. It is needed and should read:

“‘Constitution’ means the organizational documentation or, in the absence of such documentation, the governing understanding or agreement (whether written or oral) pursuant to which an association is formed or under which it operates, as such documentation, understanding or agreement is in effect or amended from time to time.”

LIABILITY OF MEMBERS AND MANAGERS

This subject has been addressed by courts over the years in ways often reversed by legislation. See pages 8-15 of Mr. Hebert's Memorandum 2000-69. The result, often resulting from and improved by legislation sponsored by the Commission, is still a patchwork. It also leaves most participants in unincorporated associations in a vulnerable position they neither expect nor want. That position, we believe, is one that claimants and creditors also do not ordinarily expect in dealing with an organization. Accordingly, we feel the California statutory provisions for unincorporated associations should treat participants in them like participants in limited liability companies. In doing so, the statute should treat members and managers separately.

Liability of Members

As to members, the Limited Liability Company Act handles their liability in a direct way. Members of an LLC are not liable for its obligations except (1) for liability based on alter ego concepts, (2) if a corporate shareholder would be liable for an obligation of the corporation, (3) liability for personal participation in a tortious act, (4) if the member agrees to be liable, and (5) to return a distribution of property if necessary to protect creditors. This general exculpation and its exceptions would accord with normal expectations of participants and of claimants against an association who have dealt with or been harmed by it.

Using this approach would not only meet expectations, but also would help courts in an area that is ill defined now and certainly not illuminated by Uniform Act Section 6. The phrase in that Section, "is authorized to participate in the management of the affairs of the nonprofit association", leaves totally open what liabilities arise if a person exercises the authority (exercise could range from voting for managers/directors or electing officers, to actual personal participation in an alleged wrong).

Liability of Managers, Officers, Directors, Trustees, Etc.

The Uniform Act does not deal with the liability of these persons, unless § 6 does so in its generality/vagueness. California statutory law also does not. Using the LLC Act approach resolves this gap. It provides managers/officers are not personally liable solely by reason of being a manager/officer. This leaves open the reasonably well developed law that a person who directly commits or participates in a wrong may be personally liable for that personal action. A good many unincorporated associations will have officers and managers, who ought to have protection from liability akin to that in other entity-like organizations.

COMMENTS ON COMMISSION DECISIONS REPORTED ON PP. 3-4 OF MINUTES OF ITS JULY 20-21, 2000 MEETING

We have belated, but we hope helpful, comments on the decisions reported in the Minutes of the Commission's July 2000 Meeting.

An overall comment is to urge the Commission to add a decision to sponsor an adequately comprehensive statute for unincorporated associations, as urged elsewhere in this letter, and to modify its other decisions to fit that program. Beyond that we have the following comments:

- (1), (4), (5), (8), (11), (13). No comment on these decisions at this time.
- (2) See elsewhere in this letter.
- (3) Suggest analysis include (as may already be planned) consideration of elimination of the restriction.
- (6) Adequate governance provisions would deal with this matter. A properly drafted adaptation of Corp. Code § 7214 (presumption of authorization if document executed as provided in section) would be useful.
- (7) This should be left to an association's constitution (see definition herein) or if not covered there to adequate statutory default provisions on dissolution, discontinuance and distributions.
- (10) Agreed.

- (12) Section 24007 should be part of an overall unincorporated associations act and may benefit from minor revision depending on content of act.

COMMENTS ON MEMORANDUM 2000-69

We did not become aware of this memorandum until Monday, September 24, 2000, and have only been able to give it a first reading.

The memorandum appears to do a good job in short compass of responding to the Commission's earlier requests for study and analyses and for specified drafts of legislation.

The Commission did not ask, and the Memorandum does not cover, whether the Uniform Act should be enacted (the Commission's specific decisions do imply a negative conclusion as to this).

Similarly, the Commission did not ask, and the Memorandum does not cover, whether an adequately comprehensive statute should be enacted covering formation, governance, dissolution and necessary related provisions as to unincorporated associations. It will be no surprise to the Commission that we feel it should make such a decision. If it does, we and other Committee members will make ourselves available to provide requested assistance to flesh out the suggestions elsewhere in this letter.

CONCLUSION

We support the Commission's undertaking of this project. We urge it to seize its opportunity to sponsor a much needed expansion of California law to fill a vacuum and provide statutory support to the widely used unincorporated association like that provided other types of private organizations. We also stand ready to provide whatever help we can to the Commission in this task.

Respectfully submitted,

R. Bradbury Clark
for himself, Lisa A. Runquist,
Gregory E. Siegler and other members
of the Committee.

RBC:bas