STATE OF CALIFORNIA

CALIFORNIA LAW REVISION COMMISSION

RECOMMENDATION AND STUDY

relating to

Notice to Shareholders of Sale of Corporate Assets

January 1959

LETTER OF TRANSMITTAL

To His Excellency Edmund G. Brown
Governor of California
and to the Members of the Legislature

The California Law Revision Commission was authorized by Resolution Chapter 207 of the Statutes of 1955 to make a study to determine whether Sections 2201 and 3901 of the Corporations Code should be made uniform with respect to notice to stockholders before all or substantially all of the assets of a corporation may be sold. The Commission herewith submits its recommendation relating to this subject and the study prepared by its staff.

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John R. McDonough, Jr.
Executive Secretary

January 1959

TABLE OF CONTENTS

RECOMMENDATION OF THE CALIFORNIA LAW REVISION COMMISSION

Relating to Notice to Shareholders of Sale of Corporate Assets

Section 3901 of the California Corporations Code permits the board of directors of a corporation to sell, lease, convey, exchange, transfer or otherwise dispose of all or substantially all of the corporation's property and assets "with the approval of the principal terms of the transaction and the nature and amount of the consideration by vote or written consent of shareholders entitled to exercise a majority of the voting power of the corporation." Section 2201 of the Corporations Code provides that when such a transaction is to be voted upon at a shareholders' meeting all shareholders must be given written notice thereof even though routine notice of meetings has been dispensed with. The Corporations Code contains no express requirement that such notice be given to shareholders when a sale of corporate assets is made with the written consent of a majority of the voting shares.

The Law Revision Commission was authorized by the Legislature to make a study to determine (1) whether a requirement that all shareholders must be given notice before a sale of corporate assets is approved by written consent might be implied from the provisions of the Corporations Code or has been established by court decision and (2) if not, whether there is adequate reason for having a requirement that notice be given to all of the shareholders when a sale of corporate assets is approved at a shareholders' meeting but not when it is approved by the written consent of the requisite number of shareholders.

As the Commission's staff study, *infra*, shows, it is clear from the legislative history of Section 3901 that notice need not be given to shareholders generally when a sale of corporate assets is approved by the written consent of a majority. A provision requiring such notice was enacted in 1931 but was repealed in 1933. Professor Henry W. Ballantine who worked with the State Bar Committee which proposed the 1933 amendment states that the requirement raised a question as to the validity of the sale if the prescribed notices were not given and that the requirement did not seem to be necessary.

The Commission believes that a requirement that notice be given to all shareholders before all or substantially all of a corporation's assets are sold or otherwise disposed of with the written consent of the majority shareholders should not be enacted. The self-interest of the majority and their fiduciary duty to the minority provide reasonably adequate protection for the interests of the latter. Moreover, a requirement that all shareholders be given formal notice might in some cases seriously handicap a corporation in effecting such a transaction because of the delay or publicity involved. Yet a sale of all or substantially all of its assets may be the only way either to save a corporation from disaster or to realize upon its assets for the greatest benefit of all

of its shareholders. The Commission recommends, therefore, that no change be made in this respect in the Corporations Code.

However, a matter warranting legislative action has come to the attention of the Commission in the course of making this study. As the staff study, *infra*, shows, a recent California decision adopted the widely-accepted view that common law and statutory rules prohibiting or regulating the sale of all or substantially all of a corporation's assets should not be applied to a corporation the very purpose of which is to sell such assets—e.g., a corporation organized to buy and sell real property. In the case of such a corporation a sale of all or substantially all of the corporate assets is a sale in the ordinary course of business and hence within the discretion of management. Yet neither Section 2201 nor Section 3901 of the Corporations Code provides expressly for this situation. It is recommended, therefore, that both sections be amended to except from their provisions a sale of all or substantially all of a corporation's assets made in the usual and regular course of business. If this is done Section 3904 should be amended to provide that the certificate of the secretary or assistant secretary of the corporation stating that a sale of corporate assets is made in the usual and regular course of business shall be prima facie evidence of that fact and conclusive evidence thereof in favor of any innocent purchaser or encumbrancer for value.

The Commission's recommendation would be effectuated by the enactment of the following measure:*

An act to amend Sections 2201, 3901 and 3904 of the Corporations Code, relating to the sale of all or substantially all of the property and assets of a corporation.

The people of the State of California do enact as follows:

SECTION 1. Section 2201 of the Corporations Code is amended to read:

2201. At the annual meeting directors shall be elected, reports of the affairs of the corporation shall be considered, and any other business may be transacted which is within the powers of the shareholders, except that action shall not be taken on any of the following proposals unless written notice of the general nature of the business or proposal has been given as in case of a special meeting, even though notice of regular or annual meetings is otherwise dispensed with:

(a) A proposal to sell, lease, convey, exchange, transfer, or otherwise dispose of all or substantially all of the property or assets of the corporation except *in the usual and regular course of its business or* under Section 3900.

* Matter in italics would be added to the present law.

(b) A proposal to merge or consolidate with another corporation, domestic or foreign.

(c) A proposal to reduce the stated capital of the corporation.

(d) A proposal to amend the articles, except to extend the term of the corporate existence.

(e) A proposal to wind up and dissolve the corporation.

(f) A proposal to adopt a plan of distribution of shares, securities, or any consideration other than money in the process of winding up.

SEC. 2. Section 3901 of the Corporations Code is amended to read:

3901. A corporation shall not sell, lease, convey, exchange, transfer, or otherwise dispose of all or substantially all of its property and assets except in accordance with one of the following subdivisions:

(a) Under Section 3900.

(b) *In the usual and regular course of its business.*

(c) Under authority of a resolution of its board of directors and with the approval of the principal terms of the transaction and the nature and amount of the consideration by vote or written consent of shareholders entitled to exercise a majority of the voting power of the corporation.

However, the articles may require for such approval the vote or consent of a larger proportion of the shareholders or the separate vote of a majority or a larger proportion of any class or classes of shareholders.

SEC. 3. Section 3904 of the Corporations Code is amended to read:

3904. Any deed or instrument conveying or otherwise transferring any assets of a corporation may have annexed to it the certificate of the secretary or an assistant secretary of the corporation, setting forth the resolution of the board of directors and (a) stating that the property described in said deed, instrument or conveyance is less than substantially all of the assets of the corporation, if such be the case, or (b) *stating that the conveyance or transfer is made in the usual and regular course of business, if such be the case, or (c)* if such property constitutes all or substantially all of the assets of the corporation *and the conveyance or transfer is not made in the usual and regular course of business,* stating the fact of approval thereof by the vote or written consent of the shareholders pursuant to this article. Such certificate is prima facie evidence of the existence of the facts authorizing such conveyance or other transfer of the assets and conclusive evidence in favor of any innocent purchaser or encumbrancer for value.

A STUDY RELATING TO NOTICE TO SHAREHOLDERS OF A SALE OF ALL OR SUSBTANTIALLY ALL OF THE ASSETS OF A CORPORATION*

Sections 2201 and 3901 of the Corporations Code are inconsistent with respect to the requirement of notice to the shareholders of a corporation of an impending sale of all or substantially all of the corporate property. Section 2201 provides that a proposal to sell or otherwise dispose of such property may not be acted upon at a shareholders' meeting unless written notice thereof is sent to each shareholder, even though routine notice of regular or annual meetings has been dispensed with.[1] However, Section 3901 which provides, *inter alia*, that a corporation may sell or otherwise dispose of all or substantially all of its property or assets with the written consent of a majority of the shareholders,[2] does not in terms require that all shareholders be notified of such a sale. Moreover, as will be shown below, the legislative history of Section 3901 makes it clear that no such notice is required.

This study is concerned with two questions: whether there is any substantial reason for this difference between Sections 2201 and 3901 and, if not, whether either should be revised. Before the question of notice to shareholders of a sale of all or substantially all of a corporation's assets is discussed, however, the power of a corporation to engage in such a transaction will be briefly considered.

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* This study was made by the Staff of the Law Revision Commission.

[1] Section 2201 of the Corporations Code provides:

> At the annual meeting directors shall be elected, reports of the affairs of the corporation shall be considered, and any other business may be transacted which is within the powers of the shareholders, except that action shall not be taken on any of the following proposals unless written notice of the general nature of the business or proposal has been given as in case of a special meeting, even though notice of regular or annual meetings is otherwise dispensed with:
>
> (a) A proposal to sell, lease, convey, exchange, transfer, or otherwise dispose of all or substantially all of the property or assets of the corporation except under Section 3900.
>
> (b) A proposal to merge or consolidate with another corporation, domestic or foreign.
>
> (c) A proposal to reduce the stated capital of the corporation.
>
> (d) A proposal to amend the articles, except to extend the term of the corporate existence.
>
> (e) A proposal to wind up and dissolve the corporation.
>
> (f) A proposal to adopt a plan of distribution of shares, securities, or any consideration other than money in the process of winding up.

[2] Section 3901 of the Corporations Code provides:

> A corporation shall not sell, lease, convey, exchange, transfer, or otherwise dispose of all or substantially all of its property and assets except in accordance with one of the following subdivisions:
>
> (a) Under Section 3900.
>
> (b) Under authority of a resolution of its board of directors and with the approval of the principal terms of the transaction and the nature and amount of the consideration by vote or written consent of shareholders entitled to exercise a majority of the voting power of the corporation.
>
> However, the articles may require for such approval the vote or consent of a larger proportion of the shareholders or the separate vote of a majority or a larger proportion of any class or classes of shareholders.

POWER TO SELL ALL OR SUBSTANTIALLY ALL OF THE ASSETS OF A CORPORATION—COMMON LAW AND MODERN STATUTES

Common Law

The common law rule was that a corporation could not be dissolved without the unanimous consent of its members. Nor, in the absence of a provision in the corporate charter or by-laws, could there be a sale of all or substantially all of the assets of a solvent corporation without the unanimous consent of the shareholders since this was considered to be a step towards dissolution.[3] This doctrine evolved on the theory that there is an implied contract among the shareholders of a corporation that it will continue to exist and to carry out the business purposes as set forth in the corporate charter.[4]

This common law rule empowered one or a minority of shareholders to thwart proposed sales which would be in the best interest of the corporation and most of its shareholders. Because of this it was soon qualified by judicially-created exceptions. First, a number of cases held that the directors or a majority of shareholders could authorize the dissolution of a corporation or the sale of all or substantially all of its assets without the vote or assent of all of the shareholders when the corporation was insolvent[5] (as used herein majority of shareholders means those entitled to exercise a majority of the voting power of the corporation). The courts later extended this rule, holding that the majority could act without consent of the minority when the prospect of achieving the chartered purposes had diminished because of financial difficulties.[6]

Another judicially-created exception to the common law rule requiring the unanimous consent of the shareholders to the sale of all or substantially all of the assets of a corporation was developed to cover the situation where the very purpose of the corporation was to sell such assets—e.g., a corporation organized for the sole purpose of managing and disposing of the property of a decedent's estate[7] or a corporation created to buy and sell land.[8] Thus, a distinction was taken at common law between a sale of corporate assets which was made in the usual and regular course of the corporate business and one which was not. In the case of the former, consent of the shareholders was not required.[9] California follows this distinction. In *Jeppi* v. *Brockman Holding Co.*,[10] which involved the question whether failure to obtain

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[3] BALLANTINE, CORPORATIONS § 231 (rev. ed. 1946); 4 THOMPSON, CORPORATIONS § 2561 (3d ed. 1927); 8 COOK, CORPORATIONS § 670 (8th ed. 1923).

[4] Lake Ontario Bank v. Onondaga Bank, 7 Hun 549 (N.Y. Sup. Ct. 1876); Town v. Bank of River Raisin, 2 Doug. 530, 546 (Mich. 1847); Revere v. Boston Copper Co., 32 Mass. (15 Pick.) 351 (1834); see also Geddes v. Anaconda Mining Co., 254 U.S. 590, 596 (1921) (dictum); BALLANTINE, *op. cit. supra* note 3, § 231; 8 COOK, *op. cit. supra* note 3, § 669.

[5] Oskaloosa Savings Bank v. Mahaska County State Bank, 205 Iowa 1251, 219 N.W. 530 (1928); see also BALLANTINE, *op. cit. supra* note 3, § 231; 4 THOMPSON, *op. cit. supra* note 3, § 2498; 8 COOK, *op. cit. supra* note 3, § 670; UNITED STATES SECURITIES AND EXCHANGE COMMISSION REPORT, Part VII, at 676 (1938).

[6] Bowditch v. Jackson Co., 76 N.H. 351, 82 Atl. 1014 (1912); Paterson v. Shattuck Arizona Copper Co., 186 Minn. 611, 244 N.W. 281 (1932); see also 6a FLETCHER, CYCLOPEDIA CORPORATIONS § 2947 (perm. ed. 1950).

[7] Jeppi v. Brockman Holding Co., 34 Cal.2d 11, 206 P.2d 847 (1949); see also Keck Enterprises v. Braunschweiger, 103 F. Supp. 925 (S.D. Cal. 1952); Thayer v. Valley Bank, 35 Ariz. 238, 276 Pac. 526 (1929); Annot., *Sale of Corporate Assets*, 9 A.L.R.2d 1306, 1312 (1950).

[8] Hendren v. Neeper, 279 Mo. 125, 213 S.W. 839 (1919).

[9] BALLANTINE, *op. cit. supra* note 3, § 42; 2 FLETCHER, *op. cit. supra* note 6, § 518; Annot., *Corporations—Sale of Property*, 5 A.L.R. 930 (1920).

[10] 34 Cal.2d 11, 206 P.2d 847 (1949).

the consent of the majority of shareholders to a contract to sell substantially all of a corporation's property invalidated the contract of sale, the Supreme Court held that Section 3901 of the Corporations Code was not applicable and that the transaction was not ultra vires because the sale was one made in the furtherance of the business for which the corporation was organized. The court stated:

> The provisions of the statute should not be applied solely upon the basis of the quantity of the property; the test which determines the question of the necessity for consent of the stockholders is, "whether the sale is in the regular course of the business of the corporation and in furtherance of the express objects of its existence, or something outside the normal and regular course of the business . . . the only purpose, for the organization of the corporation . . . was a sale in the regular course of its business . . . ."[11]

Statutes

By 1953 all but six states had enacted statutes relating to the sale of all or substantially all of the assets of a corporation.[12] These statutes may be classified as follows:

1. Seven jurisdictions had enacted statutes which provided that the directors must have authorization by a vote of a stated proportion of the shareholders obtained at a regular or special meeting to make a sale not in the usual and regular course of business.[13] Five of these jurisdictions expressly provided that no consent is needed for a sale in the usual course of business;[14] the other two jurisdictions had no express statutory provisions relating to such sales.[15]

2. Twenty-four other jurisdictions[16] permitted a sale of all or substantially all of the assets of a corporation with the approval of the majority of shareholders obtained at a regular or special meeting. These statutes do not differentiate between a sale made in the usual and regular course of business and a sale not so made. It is not clear whether the courts in these jurisdictions would require the shareholders' approval of the former.[17]

3. At least ten jurisdictions, including California, provided that the directors could be authorized by a majority or specified proportion of shareholders to sell all or substantially all of the corporate assets, such authority to be given either by (1) an affirmative vote at a general

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[11] *Id.* at 16, 206 P.2d at 350.

[12] Source of the comparative analysis of the statutes is from CORPORATION MANUAL (54th ed., Parker & Smith 1953).

[13] Illinois, Missouri, North Carolina, Ohio, Pennsylvania, Wisconsin, Virginia. See note 12 *supra*. All of these jurisdictions require that when a sale not in the usual and regular course of business is contemplated the vote must be taken at a regular meeting in which notice had been sent apprising the shareholder that such a transaction was to be considered at the regular meeting or at a special meeting duly called for that purpose.

[14] Illinois, North Carolina, Pennsylvania, Wisconsin, Virginia. See note 12 *supra*. Wisconsin has a provision specifically exempting corporations organized to deal in property as well as a provision relating to a sale in the usual course of business. WISC. STAT. § 180.70(3) (1957).

[15] Missouri, Ohio. See note 12 *supra*.

[16] Alabama, Colorado, Connecticut, District of Columbia, Georgia, Hawaii, Idaho, Indiana, Kansas, Kentucky, Maryland, Montana, New Hampshire, New Mexico, New York, North Dakota, Oklahoma, Oregon, Rhode Island, South Carolina, South Dakota, Tennessee, Vermont, Washington. See note 12 *supra*.

[17] A New York court upheld a sale by a corporation engaged in the real estate business making no attempt to proceed in accordance with the statute. Greenpoint Coal Docks v. Newton Creek Realty Corp., 5 Misc.2d 812, 91 N.Y.S.2d 466 (Sup. Ct. 1949).

or special meeting or (2) by written consent.[18] The general provisions of these statutes are essentially similar to those of the Delaware statute which provides in part:

> Every corporation . . . may at any meeting of its board of directors, sell, lease or exchange all of its property and assets, . . . as its board of directors deems expedient and for the best interests of the corporation, when and as authorized by the affirmative vote of the holders of a majority of the stock issued and outstanding having voting power given at a stockholders' meeting duly called for that purpose, or when authorized by the written consent of the holders of a majority of the voting stock . . . .[19]

NOTICE OF SALE OF ALL OR SUBSTANTIALLY ALL OF THE ASSETS OF A CORPORATION

General Considerations

One of the questions which arises in any situation in which a corporation is empowered by charter, by-law, statute or decision to sell all or substantially all of its assets is whether all of the shareholders must be given notice of such a sale before it is made. On this question the answer seems clear in three situations: (1) if the charter or a by-law has a provision one way or the other it will govern; (2) when approval of the shareholders is required to be given at a special or regular meeting they have to be given notice of the sale in the notice of the meeting;[20] and (3) in California and some other jurisdictions[21] notice to shareholders is not required when a sale of all or substantially all of a corporation's assets is made in the usual course of the business of a corporation because the consent of the shareholders to such a sale is not necessary. The precise question with which this study is concerned may, therefore, be narrowly stated: when a corporation is authorized by statute to sell all or substantially all of its assets, other than in the usual and regular course of business, with the written consent of less than all of its shareholders must those shareholders whose consent is not necessary be given notice of the proposed sale?

No decision has been found on the question whether under such a statute notice of an impending sale must be given to shareholders other than those whose consent is required. However, two of these states have dealt with the matter by statute. In 1951 Michigan amended its statute which is similar to Section 3901 to require that after a proposed sale of all or substantially all of the corporate assets has been approved by the written consent of the required proportion of shareholders the directors mail notice of such consent to all shareholders of record.[22]

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[18] CAL. CORP. CODE § 3901. Alaska, Arkansas, Delaware, Florida, Michigan, Minnesota, Nebraska, Nevada, New Jersey, West Virginia. See note 12 *supra*.

[19] DEL. CODE ANN. tit. 8, § 271 (1953). A report to the Securities and Exchange Commission stated that these statutes, including Section 3901 of the California Corporations Code, are not clear as to whether, when such a sale is made with the written consent of the required proportion of shareholders, such consent has to be filed at a shareholders' meeting to be effective. UNITED STATES SECURITIES AND EXCHANGE REPORT, Part VII, at 570 (1938).

[20] The statutes providing for the approval of the sale at a special or regular meeting require notice to the shareholders regarding the proposed sale. CORPORATION MANUAL, *passim* (54th ed., Parker & Smith 1953).

[21] See notes 7 and 18 *supra*.

[22] MICH. COMP. LAWS § 450.57 (Mason Supp. 1952).

New Jersey has also provided that notice of such consent shall be given to shareholders of record regardless of whether or not they are entitled to vote on the proposal.[23]

California Law

On its face Section 3901 of the Corporations Code appears to present the question whether it is necessary to notify all shareholders of an impending sale of all or substantially all of a corporation's assets when the approval therefor is obtained through the written consent of a majority of the shareholders. But this is a case in which appearances are deceiving for two reasons. In the first place, the question is narrower than it would appear to be by virtue of the following considerations:

1. As has been noted, the question does not arise in the case of a sale of corporate assets in the ordinary course of business.[24] The directors can make such a sale without obtaining the approval of the shareholders and *a fortiori* without notifying them.

2. The question does not arise in connection with a sale of all or substantially all of a corporation's assets in the course of effectuating a merger or consolidation for there are specific statutory provisions setting out the procedural requirements for such a transaction which require that notice thereof be given to all shareholders unless such notice has been waived.[25] Here notice is required to apprise the shareholders of the proposed transaction and to give them the opportunity to withdraw and receive payment for their shares.[26]

3. The question does not arise when the sale of all or substantially all of the corporation's assets is proposed by the directors in connection with a voluntary liquidation or dissolution of the corporation for there is a statute which specifically requires that notice of the commencement of the proceeding be given to all shareholders in such cases.[27]

In the second place, the legislative history of Section 3901 makes it clear that notice to shareholders is not required when approval of the sale is obtained by written consent. Section 3901 was enacted along with many other provisions following a six year study of California corporation laws by the State Bar Committee on Corporation Law during the years 1927 to 1933. This Committee, whose draftsman was Professor Henry W. Ballantine of the School of Law of the University of California, studied the Uniform Business Corporation Act, the Ohio General Corporation Act of 1927 and the statutes of Delaware, Nevada and other states before proposing legislation.[28] In the legislative years of 1929, 1931 and 1933 many fundamental changes were made in California corporation law on the recommendation of this Committee.

In its original form what is now Section 3901 of the Corporations Code was Section 361a of the Civil Code, enacted in 1903, which pro-

[23] N.J. STAT. ANN. § 14:3-5 (1939).
[24] See pp. G-10-11 *supra*.
[25] CAL. CORP. CODE § 4107.
[26] *Id.* § 4123.
[27] *Id.* § 4605.
[28] See BALLANTINE, CALIFORNIA CORPORATION LAWS 21 (1932); BALLANTINE, CALIFORNIA CORPORATION AMENDMENTS, preface (1929); Ballantine, *Amendments of the California General Corporation Law (1933)*, 8 CAL. B.J. 136 (1933); Ballantine, *Questions of Policy in Drafting a Modern Corporation Law*, 19 CALIF. L. REV. 465 (1931).

vided that no sale of corporate property would be valid without first obtaining the vote or expressed or written consent of two-thirds of the shareholders at a meeting called for that purpose.[29] In 1931 Section 343 of the Civil Code was enacted which contained the former Section 361a but with certain fundamental changes. Section 343 as enacted required approval of a directors' resolution to sell all or substantially all of the corporation's assets by vote or written approval by a majority of the shareholders and a *written notice of the resolution authorizing the same had to be mailed to every shareholder* whether entitled to vote or not within five days after the adoption of the resolution.[30] Professor Ballantine stated in his comment relating to this section that the requirement of written notice was for the purpose of giving the non-voting shareholders the opportunity to raise objections to the transaction in those instances when no meeting was called and the transaction was authorized by the written consent of the shareholders rather than by vote at a meeting.[31] This section was subsequently revised in 1933 to eliminate the requirement of notice to the shareholders.[32] Professor Ballantine's explanation of this revision was that the requirement of notice raised a question as to the validity of a sale of corporate assets if notice had not been given, and a requirement of notice seemed to be unnecessary.[33] In 1947 Section 343 of the Civil Code was repealed and a similar provision was enacted as Corporations Code Section 3901.[34] There were no substantive revisions to the statute at that time nor have there been any subsequent revisions.

QUESTIONS PRESENTED

From the foregoing analysis it is clear that when a sale of corporate assets is approved by a vote of shareholders at a regular or special shareholders' meeting all shareholders must be given "written notice of the general nature of the business proposal" prior to the meeting. On the other hand, when such a sale is approved by the written consent of the holders of a majority of voting shares, no information concerning the transaction need be given shareholders other than those who approve the transaction. Is this difference justified?

It may be helpful in answering this question to consider the two different purposes which a notice provision may be thought to serve. One purpose is to alert each shareholder to the fact that such relatively drastic corporate action is contemplated, thus affording him an opportunity to take such steps to prevent the action as he may be advised—e.g., attempting to persuade other shareholders not to consent, attending a shareholders' meeting to protest, or, possibly, bringing a legal action to stop the contemplated action. Section 2201 assures that each shareholder will have such notice and opportunity to act before a sale of corporate assets is approved at a shareholders' meeting. Under Section 3901, on the other hand, a sale of assets can be approved by the written consent of a majority of shareholders without the minority even being aware that it is under consideration.

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[29] Cal. Stat. 1903, c. CCLXXI, p. 396.
[30] Cal. Stat. 1931, c. 862, p. 1801.
[31] BALLANTINE, CALIFORNIA CORPORATION LAWS 323 (1932).
[32] Cal. Stat. 1933, c. 533, § 48, p. 1384.
[33] BALLANTINE AND STERLING, CALIFORNIA CORPORATION LAWS 136 (Supp. 1933).
[34] Cal. Stat. 1947, c. 1038, pp. 2375, 2440.

The other purpose which a notice requirement serves is to assure that at least those shareholders who *approve* a sale of corporate assets are made aware of what they are being asked to approve and are afforded an opportunity to consider the wisdom of the contemplated action. If one considers Sections 2201 and 3901 of the Corporations Code alone, this purpose appears to be adequately achieved at the present time in this State. Section 3901 appears to assure such notice and opportunity to those shareholders who give written consent to such a sale. While there is no explicit requirement that each shareholder whose consent is solicited be informed of the principal terms of the transaction and the nature and amount of the consideration, such a requirement can readily be implied from Section 3901. In any event, the very solicitation of his written consent affords the shareholder an opportunity to investigate and to ponder the matter before he assents. Similarly, notice and opportunity to investigate appear to be given to assenting shareholders by Section 2201 when a sale of corporate assets is to be approved at a shareholders' meeting.

But this analysis of the matter leaves out of account Section 2225 of the Corporations Code which provides that every person entitled to vote or execute consents may do so through one or more agents authorized by a written proxy, and Section 2217 which provides that written consents with respect to any shares may be given by a proxy holder. There is no requirement under California law that a person soliciting a proxy disclose to the shareholder what kinds of corporate action are contemplated or how the proxy holder will vote the shares on any question which may arise.[35] Thus, under Sections 2225 and 2217 one may use a shareholder's proxy to approve a sale of corporate assets, either by voting his shares in favor thereof at a shareholders' meeting or by giving written consent thereto on behalf of those shares, without informing the shareholder that such corporate action is contemplated, much less giving him any specific information concerning the terms of the proposed transaction. Of course, Section 2201 affords considerable assurance that the shareholder will be put on notice when a sale is approved by vote at a shareholders' meeting because it requires that all shareholders (including those who have given proxies) be given notice that the matter is to be taken up at the meeting. If a shareholder who has given a proxy bothers to read such a notice he can prevent his shares from being registered in favor of the sale either by revoking the proxy pursuant to Section 2226 or by attending the meeting and electing to vote in person pursuant to Section 2228 of the Corporations Code. However, no protection is afforded a shareholder against having his shares registered in favor of a sale of corporate assets without his knowledge, much less his personal assent, when a sale of corporate

[35] For California corporations subject to the jurisdiction of the Federal Securities and Exchange Commission this is, of course, not true. Section 14A of the Rules and Regulations of the Commission provides for the procedure, form and contents of proxy statements for corporations registered with the Commission. This statement must include information on matters to be acted upon at the meeting. The proxy statement must also give the shareholder the opportunity to indicate how his shares are to be voted on each matter listed and must state how the proxy will vote if no instructions are given by the shareholder. Thus the shareholder is protected in that he is aware of the business that is to be brought before the meeting and how his shares will be voted by his authorization of a proxy. S.E.C. RULES AND REGS. UNDER THE SECURITIES EXCHANGE ACT OF 1934, at 35,43 (1958).

assets is approved by written consent given by one to whom he has given a proxy.

POSSIBLE LEGISLATIVE ACTION

Any legislative action which is taken with respect to notice to shareholders of a sale of all or substantially all of a corporation's assets will depend, of course, on what objectives are desired to be achieved. Statutory provisions on this subject might be designed either to provide notice to nonassenting shareholders, to assure that those whose shares are registered in favor of such action are adequately informed about it in advance, or to achieve both of these objectives. Various possibilities with respect to legislative action are suggested below.

Legislation for the Protection of Nonassenting Shareholders

It is arguable that although minority shareholders should neither be able to dictate corporate policy nor prevent the majority from acting for what it regards as the best interest of the corporation, they should have the right to compel the majority to act honestly and within the general purposes of the corporate charter and that in order to do so minority shareholders must be given advance notice of action as drastic as that of selling all or substantially all of the corporation's assets. The general trend in corporation law has been to give broader powers to the majority to determine corporate policy but to afford some protection to the minority against action which would drastically alter the nature or purposes of the corporation. In many jurisdictions a compromise has been reached by the enactment of statutes conferring on the dissenters from such action the right to sell their stock to the corporation at its fair value. Such statutes generally provide that shareholders must be given notice of the proposed transaction. They may then file written objections to the transaction with the corporation within a specified number of days, making a demand for payment of the fair value of their stock if the transaction is consummated. If there is a disagreement as to the value of the stock, either the corporation or the shareholder can have the value of the stock ascertained.[36] The corporation must then buy the stock at the appraised value. California has such a statute in Section 4123 of the Corporations Code;[37] it applies, however, only to cases of consolidation and merger.

[36] Either by court action, ORE. REV. STAT. § 57.516 (1957-58); MO. REV. STAT. § 351.405 (1949); or by three disinterested persons, N.H. REV. STAT. ANN. § 294:77 (1956); MONT. REV. CODES ANN. tit. 15, § 15-913 (1947).

[37] Michigan has a similar provision, MICH. COMP. LAWS § 450.44 (1948). Michigan, however, does provide that a shareholder could request a withdrawal of his demand for payment. If the directors consent to this request he is then entitled to any rights which he would otherwise have had during the time when his demand for payment was in effect. These statutes are unusual in that they provide that the dissenting shareholder who is entitled to sell his shares to the corporation is precluded from resorting to any other remedy in equity or law. The latter provision has been criticized on the ground that "no majority, however large, should be permitted to run rough shod over the minority, however small, by illegal action or legal action carried out by illegal means." Lattin, *Remedies of Dissenting Stockholders Under Appraisal Statutes*, 45 HARV. L. REV. 233, 245 (1931). And dissenting stockholders should not be deprived of those remedies which are ordinarily available in the event of irregular or illegal action by the majority merely because a special statutory remedy is given them. STEVENS, CORPORATIONS 595 (Hornbook Series 2d ed. 1949). On the other hand, in commenting on Section 4123, Professor Ballantine took the position that the remedy given by the statute should be made exclusive thus precluding minority stockholders from blocking necessary changes and hampering business. Ballantine, *Questions of Policy in Drafting a Modern Corporation Law*, 19 CALIF. L. REV. 465, 482 (1931).

By virtue of Section 2201 minority shareholders are presently given adequate notice of a sale of corporate assets which receives the requisite shareholder approval through a vote at a shareholders' meeting. They are not given such notice when a sale of assets is approved by the written consent of the majority. If notice to all shareholders in this situation is thought desirable it could be provided by adding a new Section 3901.1 to the Corporations Code, to read:

> 3901.1. If a transfer or disposition of corporate assets authorized by paragraph (b) of Section 3901 is to be approved by the written consent of shareholders, the corporation shall mail to each shareholder at his address appearing on the books of the corporation, or given by him to the corporation for the purpose of notice, or if no such address appears or is given, at the place where the principal office of the corporation is located, a statement of the principal terms of the transaction and the nature and amount of the consideration.

Such a provision could be made directory rather than mandatory by adding the following sentence thereto:

> However, failure to give such notice does not invalidate the transfer or disposition.

Giving all shareholders notice of a proposed sale of corporate assets would, of course, provide a measure of protection to those who are opposed to such action. They can attempt to enlist sufficient shareholder support to defeat the proposed sale or, if they be so advised, bring a legal action to prevent it. But in many cases these efforts will fail. This presents the question whether a shareholder should have some further remedy when the corporation undertakes drastic action from which he dissents. If this question is answered in the affirmative, such a remedy could be provided by giving the dissenter a right to require the corporation to purchase his shares at their fair value. This could be done by enacting a new Section 4300.1 of the Corporations Code, to read:

> 4300.1. In the event that a corporation has sold, leased, conveyed, exchanged, transferred or otherwise disposed of all or substantially all of its property and assets pursuant to Section 3901 of this code, any holder of voting or nonvoting shares who has not by vote or written consent approved the principal terms of the transaction and the nature and amount of the consideration may, by complying with this article, require the corporation of which he is a shareholder to purchase his dissenting shares and to pay him their fair market value. The market value shall be determined as of the day before the action of the shareholders approving the transaction was taken or completed, excluding any appreciation or depreciation in consequence of the proposed transaction.

Legislation To Provide Adequate Notice to Assenting Shareholders

It is pointed out above that while Sections 2201 and 3901 appear to provide notice to those shareholders who assent to a sale of all or substantially all of a corporation's assets, such shareholders may not in fact

receive adequate notice when the sale is approved by persons holding their proxies, particularly when the proxy holder gives written consent to the transaction. The problem of assuring adequate notice to "assenting" shareholders in this situation could be met by enacting a new Section 2225.5 of the Corporations Code, to read:

> 2225.5. If a proxy is solicited with the intention that the holder thereof will give approval by vote or written consent to a transfer or disposition authorized by paragraph (b) of Section 3901 of this code, the person soliciting the proxy shall give the person from whom it is solicited written notice of such intention, which shall disclose the principal terms of the transaction and the nature and amount of the consideration.
>
> If a person holding a proxy not so solicited intends to give approval by vote or written consent to such a transfer or disposition he shall, before giving such approval, mail to the person from whom the proxy was obtained at his address appearing on the books of the corporation, or given by him to the corporation for the purpose of notice, or if no such address appears or is given, at the place where the principal office of the corporation is located, a written notice of such intention, which shall disclose the principal terms and the nature and amount of the consideration.

Such a provision could be made directory rather than mandatory by adding the following sentence thereto:

> Failure to give either of the notices required herein or the giving of a defective notice does not of itself invalidate the transfer or disposition.

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