



Mary Hanson



About the Business Advisor

The Business Advisor is written and published by Mary Hanson, a business attorney in Torrance, California.

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CORPORATE RECORDS: Annual Meetings

by Mary Hanson

California corporation law requires that corporations hold an annual meeting of the shareholders for the election of directors of the corporation.

Even a corporation comprised of one person as the sole shareholder and sole director needs to observe this formality to comply with the requirements of the California Corporations Code. Maintaining annual meeting minutes that evidence the yearly election of directors is an important part of maintaining the corporate shield from personal liability.

In addition to protecting the “corporate veil,” having annual meeting minutes available when requested by lenders, auditors, shareholders, or potential acquirers, or when subpoenaed in litigation, saves a corporation from delays, questions, challenges, and a range of potential problems.

Every incorporated business needs to make a point of “doing their annual minutes.” For a sole shareholder or a married couple operating an incorporated business, this is often a matter of acknowledging that the same directors and officers will continue for the next year and generating formal minutes that evidence the corporate approval of those actions.

Corporation law is very standard, so that one might reasonably assume that the requirements for holding meetings and approving corporate actions are always the same.

However, corporate requirements differ from state to state, and the requirements differ depending upon the action to be approved. In addition, corporations may adopt requirements more stringent than the requirements of applicable law.

Although the California Corporations Code requires only a meeting of shareholders, a meeting of the board of directors typically follows a corporation’s annual meeting of shareholders. The board of directors by law controls the business of the corporation and all corporate powers are exercised by or under the direction of the board. Shareholders can only vote on very few matters, with the vote to elect directors at the required annual meeting being a key right of shareholders. Since most corporate decisions are matters for the board under its authority to manage the activities of the corporation, meetings of boards of directors are important for the proper operation of a corporation.

Corporations that have a significant number of shareholders or deal with potentially contentious issues need to have procedures in place to assure that requirements regarding notice, quorum, and required approval are met and that the records maintained provide evidence of compliance with applicable requirements. The validity of actions taken at a meeting can be challenged if the meeting was not called and held in compliance with applicable corporate law.

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Annual Meetings of Shareholders

Notice of Meeting. California corporation law establishes the notice requirements for a valid meeting of shareholders. The notice requirements include that:

- written notice must be given not less than 10 or more than 60 days prior to the meeting – to each shareholder entitled to vote at the meeting;
- the written notice must contain the place, date, and hour of the meeting;
- the written notice must contain the names of the nominees intended to be presented by the board for election;
- certain matters, such as amendment of articles of incorporation, dissolution of the corporation, corporate reorganization, and matters in which there may be a conflict of interest between the corporation and a director must be stated in the notice; and
- the notice must be delivered in person or by first class mail (there are other alternatives that are too problematic to be desirable).

Corporations with few shareholders may skip the notice requirement if certain steps are taken. Shareholders may sign a “Waiver of Notice” approving the holding of the meeting whether or not they have received notice. Some small corporations have all shareholders sign a Waiver of Notice to avoid concerns about meeting legal requirements in the notices. Some small corporations only hold meetings if all shareholders can attend. Attendance at a meeting is also a waiver of notice.

Action by Written Consent. The California Corporations Code provides that any action the share-

holders may take at a meeting can be taken by a written consent, as long as that written consent receives the required number of votes. The election of directors by a written consent requires the unanimous vote of all shares entitled to vote. A California corporation is best advised to hold annual meetings of shareholders and keep minutes of annual meetings, utilizing a written consent only when a meeting cannot be held. Since the California Corporations Code requires an annual meeting of shareholders, the annual meeting is part of the observance of corporate formalities.

Quorum. For a valid meeting, a quorum must be present. Under California law the quorum requirement for a meeting of shareholders is a majority of the shares entitled to vote, represented in person or by proxy.

Voting. At a meeting of shareholders, each outstanding share is entitled to one vote, and a shareholder may vote all or a portion of his or her shares on any matter on which the shareholder is entitled to vote. At the shareholder level, percentage ownership determines the voting power of the shareholder.

Number of Shareholders. If a corporation has just one shareholder, any meeting of shareholders must be valid. If the shareholder does not attend the meeting, there is no meeting. His or her attendance at the meeting is a waiver of notice. The attendance of the 100% shareholder is always a quorum. Such a “meeting” can be as informal as the sole shareholder wishes. Nevertheless, it is important for a sole shareholder to maintain corporate minutes that evidence the election of directors at the annual meeting in order to maintain the corporate veil.

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The greater the number of shareholders, the greater the need to hold formal meetings and to take great care in complying with the legal requirements for valid meetings.

Meetings of the Board of Directors

Notice of Meeting. California corporation law establishes the notice requirements for a valid meeting of a board of directors. For most board meetings the key notice requirement is at least 4 days' notice if the notice is mailed or 48 hours' notice if the notice is delivered personally. The California Corporations Code provides other methods for giving notice, but the other methods are more readily subject to challenges if a director wishes to claim that notice was not given.

Directors also may sign a "Waiver of Notice," a consent to the holding of the meeting, or an approval of the minutes of the meeting to dispense with notice requirements. Attendance at a meeting is also a waiver of notice for directors.

For directors, a notice of meeting and a waiver of notice do not need to specify the purpose of the meeting.

Action by Written Consent. Under California law directors can take action by written consent, but all members of the board of directors must consent in writing to the action.

Quorum. Under California law a majority of the authorized number of directors constitutes a quorum of the board for the transaction of business. The authorized number of directors is normally set out in the bylaws of the corporation.

Voting. At a meeting of directors, each director has one vote, even if the directors are the same individuals as the shareholders and

their share ownership is not equal. At the director level, percentage ownership is irrelevant. An action approved by a majority of the directors present at a validly held meeting is a valid act of the board.

Number of Directors. Under California law, if a corporation has just one shareholder, it may have just one director and if it has two or more shareholders it must have two or more directors. A corporation with 3 or more shareholders must have 3 or more directors, but beyond 3 shareholders, the board of directors can be comprised of just 3 directors. Plans for transfer of stock that increase the number of shareholders need to anticipate the required increase in the number of directors on the board.

The authorized number of directors is an important issue. Since each director has a vote, increasing the number of directors dilutes the power of each director. For this reason, along with the need for a quorum in order to hold a valid meeting, a corporation owned by few shareholders should prefer a small board of directors.

Since the authorized number of directors is so important, care should be taken to ascertain and maintain the correct number of directors. Bylaws should be amended as necessary to state the correct number of directors. If the bylaws provide that the number of authorized directors is to be set by shareholders or the board of directors, the action to set the number should be properly taken and recorded.

Corporate Challenges

The California Corporations Code requires the keeping of minutes of the meetings of the shareholders and the board of directors. Corporate minutes are not filed with the



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Publisher's Note

I recommend using the most reliable methods for complying with state requirements. For example, although the California Corporations Code authorizes the use of electronic transmission and electronic attendance at meetings, the requirements for a valid meeting using such electronic methods are complex and seem more likely to form the basis to a challenge than to resolve the problems of notice.

A disgruntled shareholder can complain that proper notice of a meeting was not given and that actions taken at the meeting are not valid. A method of notice that requires too many steps and records may just open the door to challenges and objections.

If the validity of a meeting or of an action taken at a meeting is challenged, the records of the notice of meeting and attendance at the meeting, along with any waivers of notice or approval of minutes all become key documents. A corporation should adopt procedures and use documents that will work well for holding meetings and also work well in the event of a challenge to the validity of the meeting.

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Secretary of State or any other agency. They are private records, but may be requested or demanded as part of an audit by state or federal tax authorities or by claimants, creditors, lenders, potential acquirers, and other third parties under a variety of circumstances.

Individuals drafting corporate minutes should keep this potential exposure to third parties in mind when determining the appropriate level of detail in documenting the proceedings. The minutes should be brief, recording only the matters voted on and actions or resolutions approved. In my opinion, notes reflecting the discussion of issues should be kept out of corporate minutes. Any benefit of capturing the discussion is probably outweighed by the risk of exposing internal discussion to unfriendly outside eyes.

In addition to outsiders, disgruntled shareholders and directors are another source of unfriendly scrutiny of corporate minutes. Shareholders and directors of the corporation have broad rights to inspect the minutes of corporate meetings.

A corporation is well-advised to utilize set procedures for every meeting to avoid the need to determine the steps for holding each meeting. A corporation should have procedures that are appropriate for the number of shareholders and directors and also provide a level of certainty that the procedures are adequate for most meetings. For certain corporate actions that require specific levels of approval or specific notice requirements, it can be a simple matter to add the specific requirements to the existing procedures.

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