



BUSINESS LAW SECTION
INSOLVENCY LAW COMMITTEE
THE STATE BAR OF CALIFORNIA
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***PROVIDING A LEGAL PATH FOR THE WINDUP OF A CALIFORNIA CORPORATION
THAT HAS BEEN LIQUIDATED UNDER A CHAPTER 11 PLAN APPROVED BY A
BANKRUPTCY COURT***

LEGISLATIVE PROPOSAL (BLS-2017-05)

TO: Office of Governmental Affairs
FROM: Corey R. Weber and Leib Lerner, Co-Chairs 2015-16 Business Law Section (the “Section”), Insolvency Law Committee (the “Committee”)
DATE: August 26, 2016
RE: Proposal to Amend Corporations Code Section 1401 and add Section 1905.2

SECTION ACTION AND CONTACTS

Date of Approval by Section Executive Committee (the “Executive Committee”):
Approval Vote:

For: 11 Against: 0

Executive Committee Contact:	Committee Contact:
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HISTORY, DIGEST AND PURPOSE

The Insolvency Law Committee seeks to promote predictability, efficiency and consistency in the administration of federal and California laws governing insolvency and the rights and duties of creditors and debtors. This Legislative Proposal would provide a legal path for the windup of a California corporation that has been liquidated under a Chapter 11 plan approved by a bankruptcy court, thereby eliminating the inefficiencies and waste that result when a corporate shell remains “on the books” of many California state agencies, including the Secretary of State and the Franchise Tax Board.

Relevant Existing Code Sections.

California Corporations Code section 1400, *et seq.*, generally governs the authorizations for the reorganization of corporations under federal bankruptcy statutes. California Corporations Code section 1900, *et seq.*, generally governs the manner in which corporations may elect to wind up a corporation and the manner in which such corporations may dissolve, including who may file certificates of dissolution. Neither of the foregoing sections address how a trustee, master, liquidating agent or other representative appointed by the court for a corporation subject to an order for relief entered in a case under Chapter 11 of Title 11 of the United States Code is authorized to dissolve a corporation in a bankruptcy situation.

Proposal.

This Legislative Proposal would amend Corporations Code § 1401 and add § 1905.2 to specifically authorize a trustee, master, liquidating agent or other representative appointed by the court for a California corporation subject to an order for relief entered in a case under Chapter 11 of Title 11 of the United States Code, under a confirmed Chapter 11 plan that cancels the shares of the corporation and replaces the Board of Directors with a liquidating agent, to file a certificate of dissolution once the affairs of the California corporation are wound up.

Reasons for the Proposal.

Often, a California corporation files a Chapter 11 case which ends up being an orderly liquidation pursuant to a bankruptcy court approved liquidating plan. Typically, the board is replaced by a professional with experience liquidating assets. Further, in a liquidation scenario, the shares are usually canceled because they are “out of the money.” The professional appointed to manage the liquidation is generally called a plan administrator, liquidating agent or liquidating trustee. The exact title depends on the language of the Chapter 11 plan. That professional is also often given by the plan all of the rights and obligations of the board, so the corporation can complete the orderly liquidation. However, once the liquidation and winding up of the Corporation is completed, state law does not authorize the professional to dissolve the corporation under current sections 1400 or 1900. This Legislative Proposal provides that missing authorization so that the corporate records of numerous California state agencies can be cleared of the notion that the corporation is still an existing corporation.

More specifically, current law is ambiguous as to the authority of a trustee, master, liquidating agent or other representative appointed by the court for a corporation subject to an order for relief entered in a case under Chapter 11 of Title 11 of the United States Code to properly wind up and dissolve a California corporation. The problem arises because Corporations Code sections 1400 and 1900 do not address the situation of a liquidating Chapter 11 plan in which the Board of Directors ceases to exist because it is replaced by a liquidating agent. Additionally, in most such plans the shares are cancelled so there is no ability to obtain a shareholder vote to authorize dissolution under Corporations Code sections 1400 and 1900. While Corporations Code section 1400 grants broad authority for a corporation to act under bankruptcy court orders, in many situations an approved plan of liquidation does not contain specific authority for the dissolution of the corporation, and section 1900 does not specifically provide such authorization. In such cases, the general result is that the trustee, master,

liquidating agent or other representative appointed by the court does not file a formal certificate of dissolution, and in effect merely abandons the corporation after all the assets are liquidated and the bankruptcy case is closed. This results in inefficiencies and waste due to the corporate shell remaining “on the books” of many California state agencies, including the Secretary of State and the Franchise Tax Board.

Once a corporation has been wound up in bankruptcy, the trustee (or other official appointed by the court) often abandons the corporation because of a lack of authority to file a certificate of dissolution. The proposed statutory amendments would give such a trustee authorization to file a certificate of dissolution, which would allow the bankrupt corporation to file a final tax return and complete its dissolution.

If the corporation is abandoned without dissolution, the Secretary of State and the Franchise Tax Board keep the corporation on their rolls. When the corporation is abandoned, the corporation does not file annual reports with the Secretary of State and does not file tax returns with the Franchise Tax Board. Those state agencies then mail out notices of non-compliance to the corporation, and the Franchise Tax Board accrues the \$800 minimum annual franchise tax on its books. But as there are no officers, directors, shareholders, or assets in a corporation that qualifies under the proposed amendments, there is no one to respond to the notices and no funds to pay filing fees or taxes. Thus, the state is forced to keep track of and send notices with no purpose to be served.

This Legislative Proposal would also result in an additional public benefit. The Corporations Code prohibits the use of a corporate name that is the same as, or is misleadingly similar to, the name of a domestic corporation. Thus, although a corporation may be suspended, no other corporation is permitted to use that corporate name, or one unduly similar, a prohibition that continues in perpetuity. By allowing a bankrupt corporation that qualifies under the proposed amendments to file a certificate of dissolution, the name is freed up to be used by a new corporation or by existing corporations in good standing. Small businesses wishing to incorporate often incur additional effort (and if they hire an attorney, additional expense) in seeking to reserve or use a corporate name when the name is unavailable because it is the name of, or unduly similar to, the name of a defunct, suspended corporation.

This Legislative Proposal would resolve the problems created under existing law by authorizing the person(s) appointed under a bankruptcy court approved Chapter 11 plan that replaces the board to properly wind up and dissolve a California corporation instead of being left with no apparent statutory option but to abandon it.

APPLICATION

The amendments in this Legislative Proposal should take effect on January 1 of the calendar year immediately following its adoption. It is unnecessary for it to have any retroactive effect.

HISTORY

We are not aware of any similar legislative proposals or bills.

PENDING LITIGATION

We are not aware of any pending litigation that would be affected by this Legislative Proposal.

LIKELY SUPPORT AND OPPOSITION

We are not aware of any opposition to this Legislative Proposal. It should be noted that this Legislative Proposal was reviewed by the Business Law Section Corporations Committee (“Corporations Committee”). The Corporations Committee worked with the Insolvency Law Committee to determine the proper location and wording for this proposal, including discussions with an attorney at the Business Programs Division of the California Secretary of State.

FISCAL IMPACT

Potential positive fiscal impact for the State of California resulting from the elimination of inefficiencies and waste under existing law.

GERMANENESS

This Legislative Proposal is germane to the mission of our Committee because its adoption will promote efficiency, predictability and consistency in the administration of California laws governing insolvency and the rights and duties of corporate debtors and, more generally, clarity and comprehensiveness in the law. This Legislative Proposal also is important to constituents of our Committee, who from time to time represent corporate debtors and plan administrators dealing with liquidating corporate debtors.

DISCLAIMER

This position is only that of the Insolvency Law Committee of the Business Law Section of the State Bar of California. This position has not been adopted by the State Bar’s Board of Trustees or overall membership, and is not to be construed as representing the position of the State Bar of California.

Membership in the Insolvency Law Committee and in the Business Law Section is voluntary and funding for their activities, including all legislative activities, is obtained entirely from voluntary sources

TEXT OF PROPOSAL

SECTION 1. Section 1401 of the Corporations Code is amended to read:

CHAPTER 14 BANKRUPTCY REORGANIZATIONS AND ARRANGEMENTS

* * *

§ 1401. Certificate of amendment, change, alteration, dissolution or agreement of merger; execution and verification; filing.

(a) A certificate of any amendment, change or alteration or of dissolution or any agreement of merger made by such corporation pursuant to Section 1400 and executed as provided in subdivision (b), shall be filed and shall thereupon become effective in accordance with its terms and the provisions of this chapter.

(b) Such certificate, agreement of merger or other instrument shall be signed and verified, as may be directed by such orders of the court or judge, by the trustee or trustees appointed in the reorganization proceeding (or a majority thereof) or, if none is appointed and acting, by officers of the corporation designated or by a master or other representative appointed by the court or judge, and shall state that provision for the making of such certificate, agreement or instrument is contained in an order, identifying the same, of a court or judge having jurisdiction of a proceeding under a statute of the United States for the reorganization of such corporation.

(c) Notwithstanding subdivision (b), a trustee, responsible officer or other agent appointed by the court for a corporation with respect to which a proceeding has been initiated under any applicable statute of the United States as described in subdivision (a) of Section 1905.2 may execute and file a certificate of dissolution as provided in subdivision (b) of Section 1905.2.

SEC. 2. Section 1905.2 is added to the Corporations Code, to read:

Chapter 19. VOLUNTARY DISSOLUTION

* * *

§ 1905.2. Certificate of dissolution; representative under bankruptcy liquidation

(a) A trustee, master, liquidating agent or other representative appointed by the court for a corporation subject to an order for relief entered in a case under Chapter 11 of Title 11 of the United States Code may sign and verify a certificate of dissolution when the corporation has been completely wound up.

(b) The certificate of dissolution shall state the following:

(1) The name of the corporation.

(2) An order for relief was entered in a case under Chapter 11 of Title 11 of the United States Code with respect to the corporation.

(3) The identification of the court in which the order for relief was entered and the court's file number for the matter.

(4) An order confirming a plan has been entered in such case.

(5) The undersigned has been appointed by the court as a trustee, master, liquidating agent or other representative of the corporation.

(6) The shares of the corporation have been canceled pursuant to the terms of such plan.

(7) All the assets of the corporation have been distributed pursuant to the terms of such plan.

(8) The corporation is dissolved.

(c) No certificate evidencing an election to wind up and dissolve pursuant to Section 1901 is required to be filed for a corporation described in subdivision (a).