



## **BUSINESS LAW SECTION**

NONPROFIT & UNINCORPORATED ORGANIZATIONS COMMITTEE  
THE STATE BAR OF CALIFORNIA  
180 Howard Street  
San Francisco, CA 94105-1639  
<http://www.calbar.org/buslaw/nonprofits/>

### ***INDEMNIFICATION OF EMPLOYEE BENEFIT PLAN FIDUCIARIES***

#### **LEGISLATIVE PROPOSAL (BLS-2012-01)**

**TO:** Office of Governmental Affairs  
**FROM:** Cherie Evans, Chair  
Business Law Section (the "Section") Nonprofit & Unincorporated Organizations Committee (the "Committee")  
**DATE:** April 29, 2011  
**RE:** Proposal to amend Corporations Code Sections 5238(j), 7237(j), 9246(j), and 12377(j)

---

#### **SECTION ACTION AND CONTACTS**

Date of Approval by Section Executive Committee (the "Executive Committee"): June 3, 2011  
Approval Vote: For: 15 Against: 0

<b>Executive Committee Contact:</b>	<b>Committee Contact:</b>
Ellen Friedman Vice Chair for Legislation Friedman Dumas & Springwater LLP 33 New Montgomery Street, Suite 290 San Francisco, CA 94105 Tel: 415-834-3801 <a href="mailto:efriedman@friedumspring.com">efriedman@friedumspring.com</a>	Patrick Sternal Runquist & Associates 17554 Community St Northridge, CA 91325 (818) 609-7761 <a href="mailto:patrick@runquist.com">patrick@runquist.com</a>

#### **HISTORY, DIGEST AND PURPOSE**

This Proposal would eliminate the ambiguity in the Corporations Code regarding the indemnification standards applicable to fiduciaries of an employee benefit plan when acting on behalf of a nonprofit public benefit, mutual benefit, religious or consumer cooperative corporation.

## **History**

The Nonprofit Corporation Law became effective in 1980. The Consumer Cooperative Corporation law became effective in 1984. Some of the code sections affected by this Proposal were amended in 1995, though the specific subdivisions affected have not been amended since enactment.

## **Proposal and Reasons for the Proposal**

The Proposal would amend subdivision (j) of Corporations Code Sections 5238, 7237, 9246, and 12377. Each of these sections makes the indemnification standards provided by Corporations Code section 207(f) applicable to any trustee, investment manager or other fiduciary of an employee benefit plan when acting in that capacity on behalf of a nonprofit public benefit, mutual benefit, religious and consumer cooperative corporation, respectively. Such indemnification is authorized even if the person would also be considered that corporation's agent under Corporations Code sections 5238, 7237, 9246, and 12377, which describes the scope of indemnification generally applicable to a corporation's agents. The Proposal would eliminate ambiguity arising from the internal cross-reference to a section of the General Corporation Law (Corporations Code section 207(f)) where an analogous statute is already contained in the Nonprofit Corporation Law (Corporations Code sections 5140(f), 7140(e), and 9140(f)) and the Consumer Cooperative Corporation Law (Corporations Code section 12320(e)). The Proposal would also eliminate further ambiguity between the different descriptions of employee benefit plan fiduciaries contained in Corporations Code sections 207(f), on the one hand, and sections 5140(f), 7140(e), 9140(f), and subdivision (j) of sections 5238, 7237, 9246, and 12377, on the other hand.

Subdivisions (a) through (i) of Section 5238 of the Corporations Code authorize a nonprofit public benefit corporation to indemnify the corporation's agents (defined to include directors, officers, employees and other agents) against certain liabilities. The statute places certain substantive and procedural limits upon the nature of the indemnification that can be provided. Subdivision (j) of Section 5238 exempts from these limits any trustee, investment manager or other fiduciary of an employee benefit plan in such person's capacity as such, even if the person would also be considered an agent under Section 5238. In place of the limits contained in Section 5238(a) through (i), subdivision (j) authorizes the corporation to provide indemnity to the same extent as permitted by Corporations Code Section 207(f).

Section 207 provides that "a corporation shall have all of the powers of a natural person in carrying out its business activities," including those powers described in subdivision (f):

(f) Pay pensions, and establish and carry out pension, profit-sharing, share bonus, share purchase, share option, savings, thrift and other retirement, incentive and benefit plans, trusts and provisions for any or all of the directors, officers and employees of the corporation or any of its subsidiary

or affiliated corporations, and to indemnify and purchase and maintain insurance on behalf of any fiduciary of such plans, trusts or provisions.

Thus, the effect of Section 5238(j) is to permit a nonprofit public benefit corporation to indemnify and purchase and maintain insurance on behalf of any fiduciary of the type listed in Section 207(f). This would cover a fiduciary of a pension, profit-sharing, share bonus, share purchase, share option, savings, thrift and other retirement, incentive and benefit plans, trusts and other provisions serving the same purpose, benefitting directors, officers and employees of the corporation or any of its subsidiary or affiliated corporations.

An ambiguity arises because the Nonprofit Public Benefit Corporation Law already has a provision in Section 5140(f) that is analogous to Section 207(f). Section 5140 similarly describes the powers of a nonprofit public benefit corporation as those of a natural person, and its subdivision (f) tracks the language of Section 207(f). However, Section 5140(f) differs from Section 207(f) in eliminating reference to certain benefit plans which would be inconsistent with (if not antithetical to) the operation of a nonprofit organization, namely, “profit sharing, share bonus, share purchase, share option” plans. The current cross-reference to Section 207(f) is thus additionally ambiguous in apparently assuming that a nonprofit public benefit corporation may operate a profit sharing plan.

It is worth noting that Section 317 in the General Corporation Law is the indemnification statute analogous to Section 5238. Section 317 also contains a subdivision (j) with the identical cross-reference to Section 207(f) to incorporate the latter statute’s standards for indemnification of employee benefit plan fiduciaries. It appears that the drafters of Section 5238(j) simply copied wholesale Section 317(j) without adjustment for the existence of Section 5140(f), the Nonprofit Public Benefit Corporation Law’s corollary to Section 207(f).

A further ambiguity exists in that Corporations Code sections 5238(j) and 207(f) use different terms to describe the type of plans whose fiduciaries may be indemnified, although it appears the drafters intended the descriptions be treated as equivalents. Section 5238(j) refers simply to “an employee benefit plan” while the cross-referenced Section 207(f) (or Section 5140(f)) contains a more fulsome description of the sort of plans the fiduciaries of which may be indemnified (“pension, profit-sharing, share bonus, share purchase, share option, savings, thrift and other retirement, incentive and benefit plans, trusts and provisions for any or all of the directors, officers and employees of the corporation or any of its subsidiary or affiliated corporations....”) The use of these different descriptions invites an interpretation that the scope of activities that can be indemnified under Section 5238(j) should be narrower than that allowed under Section 207(f) or 5140(f). Although that conclusion may be justified as long as Section 5238(j) cross-references to Section 207(f) and its indemnified profit and stock plans, the conclusion would serve no policy reason if 5238(j) cross-references to Section 5140(f).

It seems the reference to Section 207(f) in Section 5238(j) was a mistake, and ought to be changed to Section 5140(f). In addition, Section 5238(j) should be amended to use the same description of employee benefit plans as found in the cross-referenced Section 5140(f).

The identical language of Section 5238(j), including the mistaken cross-reference to Section 207(f), is found in Sections 7237(j), 9246(j), and 12377(j) which are applicable to mutual benefit, religious and consumer cooperative corporations, respectively. Sections 7237(j), 9246(j), and 12377(j) should be similarly amended for the same reasons, and to achieve the same ends, as the proposed amendment of Section 5238(j).

#### **APPLICATION**

If enacted in 2012, the proposed legislation would become effective on January 1, 2013.

#### **PENDING LITIGATION**

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

#### **LIKELY SUPPORT AND OPPOSITION**

We anticipate support from nonprofit corporations in California. We are unaware of any specific segments that might oppose this Proposal.

#### **FISCAL IMPACT**

None known.

#### **GERMANENESS**

The matters addressed in this Proposal require the special knowledge, training, experience or technical expertise of the Section and of members of the Committee. The position advanced would promote clarity, consistency, and comprehensiveness in the law.

## TEXT OF PROPOSAL

**The following sections of the Corporations Code are amended as follows:**

### **§ 5238. Indemnification of Corporate “Agent.”**

(j) This section does not apply to any proceeding against any trustee, investment manager or other fiduciary of ~~an employee benefit plan~~a pension, deferred compensation, saving, thrift and other retirement, incentive and benefit plan, trust and provision for any or all of the corporation’s directors, officers, employees and persons providing services to the corporation or any of its subsidiary or related or affiliated corporations in such person's capacity as such, even though such person may also be an agent as defined in subdivision (a) of the employer corporation. A corporation shall have power to indemnify such trustee, investment manager or other fiduciary to the extent permitted by subdivision (f) of Section ~~207~~5140.

### **§ 7237. Indemnification of Corporate “Agent.”**

(j) This section does not apply to any proceeding against any trustee, investment manager or other fiduciary of ~~an employee benefit plan~~a pension, deferred compensation, saving, thrift and other retirement, incentive and benefit plan, trust and provision for any or all of the corporation’s directors, officers, employees and persons providing services to the corporation or any of its subsidiary or related or affiliated corporations in such person's capacity as such, even though such person may also be an agent as defined in subdivision (a) of the employer corporation. A corporation shall have power to indemnify such trustee, investment manager or other fiduciary to the extent permitted by subdivision ~~f~~e of Section ~~207~~7140.

### **§ 9246. Indemnification of Corporate Agent.**

(j) This section does not apply to any proceeding against any trustee, investment manager or other fiduciary of ~~an employee benefit plan~~a pension, deferred compensation, saving, thrift and other retirement, incentive and benefit plan, trust and provision for any or all of the corporation’s directors, officers, employees and persons providing services to the corporation or any of its subsidiary or related or affiliated corporations in such person's capacity as such, even though such person may also be an agent as defined in subdivision (a) of the employer corporation. A corporation shall have power to indemnify such trustee, investment manager or other fiduciary to the extent permitted by subdivision (f) of Section ~~207~~9140.

**§ 12377. Indemnification of Corporate Agents and Other Parties.**

(j) This section does not apply to any proceeding against any trustee, investment manager or other fiduciary of ~~an employee benefit plan~~*a pension, deferred compensation, saving, thrift and other retirement, incentive and benefit plan, trust and provision for any or all of the corporation's directors, officers, employees and persons providing services to the corporation or any of its subsidiary or related or affiliated corporations* in such person's capacity as such, even though such person may also be an agent as defined in subdivision (a) of the employer corporation. A corporation shall have power to indemnify such trustee, investment manager or other fiduciary to the extent permitted by subdivision ~~f~~*e* of Section ~~207~~*12320*.