California Corporate & Securities Law

Choice Of Law And Derivative Suits

By Keith Paul Bishop on January 23, 2012

The California Corporations Code carefully defines the terms “corporation” (Section 162), “domestic corporation” (Section 167), “foreign corporation” (Section 171); and “foreign association” (Section 170). For example, when the legislature provided in Section 1500 that “[e]ach corporation shall keep adequate and correct books and records . . . “, the legislature imposed a mandatory obligation (See Section 15 as to the meaning of “shall”) only on corporations organized under the General Corporation Law or subject to it pursuant to Section 102(a). Thus, Section 1500 is not applicable to, among other business entities, domestic corporations, foreign corporations or foreign associations.

Section 800 of the Corporations Code governs derivative suits. Unlike Section 1500, the legislature has not limited its application to just corporations. Rather, the statute applies to domestic corporations and foreign corporations. The legislature didn’t stop there, it went on to provide that in Section 800, the term “corporation” includes an unincorporated association. Thus, the legislature has chosen to override the general principle that derivative suits are governed by the law of the state of incorporation.

This may come as a surprise to devotees of the internal affairs doctrine. However, ample precedent exists demonstrating that Section 800 isn’t applied only to corporations organized under the General Corporation Law.

- In *Shields v. Singleton,* 15 Cal. App. 4th 1611, 1621 (1993), the Court of Appeal applied Section 800 to a Delaware corporation.
- In J*ohnson v. Myers*, 2011 U.S. Dist. LEXIS 112897 (N.D. Cal. Sept. 30, 2011), the District Court applied Section 800 to derivative claims involving a company organized under the law of Scotland.
- In *Oakland Raiders v. Nat’l Football League,* 93 Cal. App. 572 (2001), the Court of Appeal applied Section 800 to an unincorporated (presumably foreign) association.

The California courts, moreover, have applied several other provisions of the Corporations Code to foreign corporations as directed by the legislature: Section 1600 (shareholder inspection rights), *Valtz v. Penta Corp. et al.*, 139 Cal. App. 3d 803 (1983); Section 1602 (inspection rights of directors),

Havlicek v. Coast-to-Coast Analytical Services, *Inc.,* 39 Cal. App. 4th 1844 (1995); and Section 25502.5 (liability for insider trading), *Friese v. Superior Court*, 134 Cal. App. 4th 693 (2005).

Finally, U.S. Supreme Court precedent supports the application of Section 800. *Cohen v. Beneficial Indus. Loan Corp.*, 337 U.S. 541 (1949) involved a derivative claim brought in the United States District Court for New Jersey against Beneficial Industrial Loan Corporation, a Delaware corporation doing business in New Jersey. The U.S. Supreme Court framed the question on appeal as "whether a federal court, having jurisdiction of a stockholder's derivative action only because the parties are of diverse citizenship, must apply a statute of the forum state which makes the plaintiff, if unsuccessful, liable for the reasonable expenses, including attorney's fees, of the defense and entitles the corporation to require security for their payment." Citing the Federal Rules of Decision Act, 28 U. S. C. § 1652, the Supreme Court held that the District Court had erred in declining to apply the New Jersey statute.

In a future post, I explain why matters.

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