California Corporate
& Securities Law

A CSL Riddle – When Does A Corporation With Two Shareholders Have No Outstanding Shares?

By Keith Paul Bishop on October 18, 2011

The Riddle of the Sphinx

Recently, I was fortunate to see an adaption of the play *Trojan Women* by Euripides performed at the amphitheater at the Getty Villa in Malibu. It was wonderfully magical to sit under a bright moon at the edge of the Pacific ocean and watch a play that has been enjoyed by audiences for more than two millenia. Sophocles, a contemporary of Euripides, is famous for his Theban trilogy which tells the story of Oedipus (*Oedipus Rex, Oedipus at Colonus, and Antigone*). Although Oedipus is best known for marrying his mother, Queen Jocasta of Thebes, he only did so after solving the riddle of the Sphinx. The Sphinx in this story is not the well-known Sphinx on the Giza plain in Egypt.

According to Apollodorus, the City of Thebes would be free of the Sphinx only when this riddle was solved: τί ἐστιν ὃ μίαν ἔχον φωνὴν τετράπουν καὶ δίπουν καὶ τρίπουν γίνεται ("what has one voice and is four footed and becomes two footed and then three footed?"). With all this talk of feet, it's interesting to note that Oedipus' name means swollen foot. For a more humorous retelling of the grim story of Oedipus' "odd complex", I encourage you to listen to Tom Lehrer's *Oedipus Rex*.

My Riddle

My Corporate Securities Law riddle is as follows: When does a corporation with two shareholders have no oustanding shares?

Corporations Code § 25103(b) & (c) provide exemptions from the qualification requirements of Corporations Code §§ 25110 & 25120 for any (i) change in rights, preferences, privileges, or restrictions of or on outstanding securities; and (ii) exchange incident to a merger, consolidation, or sale of assets in consideration of the issuance of securities, unless the holders of at least 25% of the outstanding shares are held by persons who have addresses in California. For purposes of applying this jurisdictional test, Corporations Code § 25103(d) provides that any secruities controlled by any one person who controls directly or indirectly 50% or more of the outstanding securities of that class are not considered to be outstanding. The purpose of this exclusion is to direct the statute's application to the "public" security holders.

The Answer

Section 25103(d) is also the answer to my riddle. If a corporation has two shareholders with each shareholder owning 50% of the outstanding shares, then it has no shares outstanding for purposes of Section 25103(d). *See* Commissioner's Opinion 70/125 (Sept. 21, 1970) ("By virtue of this provision [§ 25103(d)], since each of the two shareholders of the disappearing corportion controls 50% of the outstanding shares of that corporation, the shares held by these two shareholders will not be considered outstanding. It follows that the exemption of Section 25103(c) is available for the proposed transaction."). Under the same principle, a corporation with a single shareholder, will have no shares outstanding. *See* Commissioner's Opinion 72/9 (Feb. 2, 1972).

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