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OPINION	:	No. 86-108
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of	:	<u>SEPTEMBER 4, 1986</u>
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THE HONORABLE NORMAN S. WATERS, MEMBER, CALIFORNIA ASSEMBLY, has requested an opinion on the following questions:

1. May the resource conservation districts of California organize their statewide association formed pursuant to Public Resources Code section 9417 as a non-profit corporation composed of and controlled by the districts?
2. What is the liability of districts as members and district directors as elected officials if the unincorporated association of districts were sued and judgment rendered against it and would this exposure to liability change if the association were incorporated?

CONCLUSIONS

1. The resource conservation districts of California may organize their statewide association formed pursuant to Public Resources Code section 9417 as a non-profit corporation composed of and controlled by the districts.

2. A judgment rendered against the unincorporated association of districts would generally bind the member districts but not the district directors. A judgment rendered against the corporation formed to replace the un-incorporated association would generally not bind the member districts or district directors. Incorporation of the association, however, would not assure member districts or district directors that they would not be liable for corporate obligations or joined in the litigation against the corporation.

ANALYSIS

The California Association of Resource Conservation Districts ("Association") is currently an unincorporated organization formed under the statutory provisions of Public Resources Code section 9417:

"The directors of any district may cooperate with the directors of any other district in respect to matters of common interest or benefit to the districts. An association of resource conservation districts may be organized to facilitate such cooperation, to provide for the loan of equipment and tools by one district to another, and for the making of investigations and studies and the carrying out of projects of joint interest to the districts participating therein."

The two questions presented for analysis concern whether the Association may incorporate and, if so, whether such incorporation would affect the exposure to liability of the member districts and district directors if the Association were sued and judgment rendered against it.

We have previously examined the purposes of the Association and concluded that it is a nonprofit instrumentality of the member districts which in turn are governmental agencies carrying out the soil and water conservation policies of the state. (32 Ops.Cal.Atty.Gen. 97, 99 (1958).)¹ The districts construct and manage public works to control soil erosion and distribute water resources primarily in agricultural areas. (Pub. Resources Code, §§ 9001, 9151, 9152, 9415.)

As indicated in Public Resources Code section 9417, the Association has three interrelated functions: (1) to facilitate cooperation among the districts in matters of

¹ In our prior opinion we concluded that the Association was entitled to elective coverage of its employees for purposes of social security and unemployment insurance, since it was an instrumentality of the member districts. We found it unnecessary to decide whether the Association was a "local agency" for purposes of employee health benefits coverage.

common interest or benefit, (2) to provide for the loan of equipment and tools by one district to another, and (3) to investigate, study and carry out projects of interest to the districts.

We are informed that in performing these duties, the Association initiates and takes positions on pending legislation, publishes a newsletter, annually holds a state conference for the districts and forms various committees comprised of directors of the member districts to study issues of mutual concern. Occasionally the Association enters into contracts with state and federal agencies to perform specified services in such areas as mapping surveys of agricultural lands and the planning and construction of irrigation systems.

The Association has divided the state into nine regional areas, with each area electing a member of the board of directors of the Association. Officers and directors of the Association meet regularly to conduct Association business. The Association has one employee, its executive director. It leases office space and owns several pieces of office equipment and furniture. The Association is funded primarily by the approximately 120 districts that have chosen to participate in its programs.

1. Incorporation of the Association

The first question presented for analysis is whether the Association may incorporate as a nonprofit corporation composed of and controlled by its member districts. We conclude that it may.

Corporations Code section 5111² authorizes the formation of a corporation for any public purpose "[s]ubject to any other provisions of law of this state applying to the particular class of corporation or line of activity." Section 5121 specifically authorizes existing unincorporated associations to incorporate:

"(a) In the case of an existing unincorporated association, the association may change its status to that of a corporation upon a proper authorization for such by the association in accordance with its rules and procedures.

"(b) In addition to the matters required to be set forth in the articles pursuant to Section 5130, the articles in the case of an incorporation authorized by subdivision (a) shall set forth that an existing unincorporated association, stating its name, is being incorporated by the filing of the

² All references hereafter to the Corporations Code are by section number only.

articles.

"(c) The articles filed pursuant to this section shall be accompanied by an affidavit of any two officers or governing board members of the association stating that the incorporation of the association by means of the articles to which the affidavit is attached has been approved by the association in accordance with its rules and procedures.

"(d) Upon the change of status of an unincorporated association to a corporation pursuant to subdivision (a), the property of the association becomes the property of the corporation and the members of the association who had any voting rights of the type referred to in Section 5056 become members of the corporation.

"(e) The filing for record in the office of the county recorder of any county in this state in which any of the real property of the association is located of a copy of the articles of incorporation filed pursuant to this section, certified by the Secretary of State shall evidence record ownership in the corporation of all interests of the association in and to the real property located in that county.

"(f) All rights of creditors and all liens upon the property of the association shall be preserved unimpaired. Any action or proceeding pending by or against the unincorporated association may be prosecuted to judgment, which shall bind the corporation, or the corporation may be proceeded against or substituted in its place.

""³

Sections 5111 and 5121 are part of the Nonprofit Public Benefit Corporation Law (§§ 5110-6910). This statutory scheme allows a corporation formed thereunder to "admit persons to membership, as provided in its articles or bylaws." (§ 5310, subd. (a).) "Persons" for this purpose includes a "government or political subdivision, agency or instrumentality of a government." (§ 5065.) Subdivision (c) of section 5056 states: "Where a member of a corporation is not a natural person, such member may authorize in writing one or more natural persons to vote on its behalf on any or all matters which may

³ Section 5130 requires that the articles of incorporation set forth the name of the corporation, a statement of purpose, and the name and address of the corporation's agent for service of process. Section 5056 refers to voting rights for the election of a director or directors, the disposition of assets, a merger, a dissolution, or a change to the articles or bylaws.

require a vote of the members."

Are there "any other provisions of law of this state applying to the . . . line of activity" (§ 5111) that would prevent the Association from incorporating? Does Public Resources Code section 9417 limit the application of section 5111?

Public Resources Code section 9417 is silent, other than use of the word "association," in describing the type of organizational structure which it authorizes. "The word 'association' has no definite significance in the legal terminology of this state." (7 Cal.Jur.3d, Associations and Clubs, § 1, p. 115.) It is used to describe both unincorporated bodies (see Estate of Irwin (1915) 196 Cal. 366, 372) and corporations (see, e.g., Food & Agr. Code, § 54002).

We find nothing in Public Resources Code section 9417 that may be said to prohibit the possibility of incorporation. The language of the statute is broad and in general terms, with the specified duties and functions being capable of performance by the Association whether unincorporated or incorporated. We know of no other law that would prohibit the Association from incorporating under the terms of section 5111.

We thus conclude in answer to the first question that the resource conservation districts of California may organize their statewide association formed under Public Resources Code section 9417 as a nonprofit corporation composed of and controlled by the districts.

2. Liability of Members and Directors

The second question presented concerns the liability of districts as members and district directors as elected officials if the Association were sued and judgment rendered against it and whether this exposure to liability would change if the Association were incorporated.

Preliminarily, we note that no set of circumstances has been presented upon which to give a specific response. Our analysis must accordingly be stated in general terms. Also, this area of law has been an evolving one over a lengthy period of time and may continue to evolve.

The members of unincorporated associations were once treated as partners for purposes of liability. "'Where a business is conducted in the name of an unincorporated association all of the parties thereto are regarded as partners.'" (*Leake v. City of Venice* (1920) 50 Cal.App. 462, 465.) As stated by the Supreme Court in *Fazzi v. Peters* (1968) 68 Cal.2d 590, 595:

"At common law neither a partnership nor any other unincorporated association could be sued by its firm name. 'The basic reason was that the association was not, in the eyes of the law, a legal unit or entity, and it had no legal capacity to become a party to an action.' (*Jardine v. Superior Court* (1931) 213 Cal. 301, 307; see also 40 Am.Jur. Partnership, § 434, pp. 432-433.) An action brought upon a partnership obligation was considered like any other action upon a joint obligation, and all individual partners were necessary parties. (40 Am.Jur. Partnership, § 434, pp. 432-433.) Thus, as a general rule, failure to join, or dismissal of, a partner resulted in abatement of the action, at least insofar as it sought to bind the partnership estate rather than the individual estates of the partners joined. (See generally Annot. 44 A.L.R.2d 580; 40 Am.Jur. Partnership, § 434, pp. 432-433.)"

The Legislature has changed certain of the common law rules, allowing unincorporated associations to be sued (see *Barr v. United Methodist Church* (1979) 90 Cal.App.3d 259, 264-267) and limiting the scope of liability of unincorporated association members. (§§ 21100-21102; 24000- 24002). None of the latter liability statutes, however, appear to be applicable to the Association and its members, since the statutory language concerns associations "of natural persons" (§ 21000) and excludes a "governmental subdivision or agency" (§ 24000). The Association, in contrast, is a creature of statute and a governmental agency that is itself comprised of statutory, governmental bodies.

Case law in the area of nonprofit unincorporated associations has provided little interpretation of these legislative enactments. (See Comment, *Liability of Members and Officers of Nonprofit Unincorporated Associations for Contracts and Torts* (1954) 42 Cal.L.Rev. 812, 823 (hereafter "*Liability of Members*").) Instead, the courts have focused on the liability of members for the obligations of the organization where the members give actual or constructive assent, express or implied authorization, or the obligation arose in attempting to accomplish an objective of the organization in an appropriate manner. (*Barr v. United Methodist Church, supra*, 90 Cal.App.3d 259, 267; *Steuer v. Phelps* (1974) 41 Cal.App.3d 468, 472; *Security-First Nat. Bk. v. Cooper* (1944) 62 Cal.App.2d 653, 667; 59 Ops.Cal.Atty.Gen. 162, 164 (1976); Advising California Nonprofit Corporations (Cont. Ed. Bar 1984) § 1.4, pp. 8-9 (hereafter CEB); *Liability of Members, supra*, pp. 821-822, 825-826.)

This finding of member liability distinguishes nonprofit unincorporated associations from associations that are incorporated. The general rule for corporations is that its stockholders, directors, and officers are not liable for corporate debts, obligations, or liabilities. (*Wyatt v. Union Mortgage Co.* (1979) 24 Cal.3d 773, 785; *Alexander v. Abbey of the Chimes* (1980) 104 Cal.App.3d 39, 46; CEB, *supra*, §§ 5.63, 6.21, pp. 326, 342; Fessler, *The Fate of Closely Held Business Associations: The Debatable Wisdom of*

"Incorporation" (1980) 13 U.C. Davis L.Rev. 473, 487-488 (hereafter "*Business Associations*").) For nonprofit public benefit corporations the Legislature has codified this rule in subdivision (a) of section 5350: "A member of a corporation is not, as such, personally liable for the debts, liabilities, or obligations of the corporation." ⁴

In exceptional circumstances, however, a court may "pierce the corporate veil" and find a stockholder, director, or officer liable for corporate obligations if it finds that the person is an "alter ego" of the corporation. (See *Wyatt v. Union Mortgage Co.*, *supra*, 24 Cal.3d 773, 785; *Alexander v. Abbey of the Chimes*, *supra*, 104 Cal.App.3d 39, 46-47; CEB, *supra*, §§ 5.63, 6.21, pp. 326, 342; *Business Association*, pp. 487-488.) This theory of liability is equitable in nature and is applied where the corporation has come under the control of the person to further his or her own interests.

Finally, we note that the situation presented concerns the possibility of the Association being sued and judgment rendered against it. A judgment against the Association, whether incorporated or not, would not in itself bind the members. (*Fazzi v. Peters*, *supra*, 68 Cal.2d 590, 594-597; *Alexander v. Abbey of the Chimes*, *supra*, 104 Cal.App.3d 39, 46-47; *Barr v. United Methodist Church*, *supra*, 90 Cal.App.3d 259, 272-273; *Ross v. Campbell Union School Dist.* (1977) 70 Cal.App.3d 113, 120; *Promoters Enterprises, Inc. v. Jiminez* (1971) 21 Cal.App.3d 560, 564-566.)

On the other hand, the facts that give rise to a judgment rendered against the Association, whether incorporated or not, might also give rise to liability for particular member districts as well as district directors who may be sued thereon and judgment obtained against them individually. We know of no theory upon which liability may be imposed upon a district director except where based upon his or her own individual conduct.

In answer to the second question, therefore, we generally conclude that a judgment rendered against the Association would bind the member districts but not the district directors, while a judgment rendered against the Association, if it incorporates, would bind neither the districts nor directors. Incorporation of the Association, however, would not assure member districts or district directors that they would not be liable for corporate obligations or joined in the litigation against the corporation.

⁴ As previously mentioned, the articles or bylaws of a nonprofit public benefit corporation may provide that the corporation have members. (§ 5310, subd. (a).)