

TO BE PUBLISHED IN THE OFFICIAL REPORTS

OFFICE OF THE ATTORNEY GENERAL
State of California

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OPINION	:	No. 86-602
	:	
of	:	<u>DECEMBER 31, 1986</u>
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THE HONORABLE M. MARK MICHALKO, DIRECTOR, CALIFORNIA STATE LOTTERY, has requested an opinion on the following question:

When a corporation submits a bid to furnish goods or services to the California State Lottery, must the corporation disclose the names and addresses of the officers, directors and stockholders of a company that owns stock in the corporation?

CONCLUSION

When a corporation submits a bid to furnish goods or services to the California State Lottery, the corporation must disclose the names and addresses of the officers, directors and stockholders of a company that owns stock in the corporation if such company has the power to control the management and policies of the corporation. Shareholder disclosure is limited in the case of publicly traded corporations to those known to the corporation to beneficially own five percent or more of the publicly held securities.

ANALYSIS

Voter approval of Proposition 37 on the California General Election Ballot of November 6, 1984, added by initiative measure the California State Lottery Act ("Act") as Government Code sections 8880 through 8880.71.¹ The Act is administered by a commission and a director (see §§ 8880.24, 8880.35) and has as its purpose the operation of a state lottery so as to provide "additional monies to benefit education without the imposition of additional or increased taxes." (§ 8880.1.)

The question presented for analysis concerns a corporation that submits a bid to obtain a contract for furnishing lottery ticket supplies.² The corporation has a stockholder that is itself a corporation. What information must be disclosed to the commission at the time of the bid concerning this corporate stockholder?

Section 8880.57 is the controlling provision of the Act regarding the disclosures required of lottery contract bidders. It provides in relevant part:

"In order to allow an evaluation of the competence, integrity, and character of potential Lottery Contractors for the California State Lottery, any person, corporation, trust, association, partnership or joint venture which submits a bid, proposal, or offer as part of procurement for a contract for any goods or services for the California State Lottery, other than materials, supplies, services, and equipment which are common to the ordinary operations of state agencies, shall comply with each of the following:

"(a) At the time of the submission of the bid, proposal, or offer to the Lottery, disclose the bidder's name and address and, as applicable, the name and address of the following:

"(1) If the bidder is a corporation, the officers, directors, and each owner, directly or indirectly, of any equity security or other ownership interest in the corporation. However, in the case of owners of publicly held equity securities of a publicly traded corporation, only the names and addresses of those known to the corporation to beneficially own 5 percent or more of the publicly held securities need be disclosed.

¹ All references hereafter to the Government Code are by section number only. Subdivision references hereafter are to section 8880.57.

² Different rules apply concerning contracts for "materials, supplies, services, and equipment which are common to the ordinary operations of state agencies" (§ 8880.57); such latter contracts are outside the scope of this opinion.

".....

"(4) If the bidder is a subsidiary, the officers, directors, and stockholders of the parent company thereof. However, in the case of owners of publicly held equity securities of a publicly traded corporation, only the names and addresses of those known to the corporation to beneficially own 5 percent or more of the publicly held securities need be disclosed.

".....

"(6) If the parent company, general partner, limited partner, or joint venturer of any bidder is itself a corporation, trust, association, subsidiary, partnership, or joint venture, then the disclosure of such information as necessary to determine ultimate ownership. However, in the case of owners of publicly held equity securities of a publicly traded corporation, only the names and addresses of those known to the corporation to beneficially own 5 percent or more of the publicly held securities need be disclosed."

Subdivision (a) of section 8880.57 describes persons and entities who are "bidders" and other persons and entities who have specified relationships with the contract bidders. As for "bidders,"³ subdivision (b) of section 8880.57 gives the commission authority to require the disclosure of such information as (1) the states and jurisdictions where each does business and the nature of such business, (2) the state and jurisdictions where each has contracts to supply gaming goods and services, (3) the states and jurisdictions where each has applied for a gaming license, (4) the details of any conviction for a criminal offense, (5) the details of any bankruptcy litigation, (6) the details of any political contributions made during the past five years, and (7) additional information deemed appropriate for procurement of the particular contract.

With respect to the persons and entities identified as having the particular relationships with the bidders specified in subdivision (a) of section 8880.57, the commission is authorized to "request the disclosure of any information required in subdivision (b), which shall be relevant to the award of any contract." (§ 8880.57, subd. (c).)

The commission is also authorized to contractually require of any successful bidder that the required disclosures be kept current during the term of the contract. A contract may be cancelled by the commission if false statements are discovered in the

³ A subcontractor of "any substantial portion of the work to be performed" is considered to be a bidder for purposes of the disclosure requirements. (§ 8880.57, subd. (a)(7).)

information submitted or if the disclosures are not kept up-to-date as specified in the contract. (§ 8880.57, subd. (d).)

The disclosure provisions of section 8880.57 are to be liberally construed so as to allow for full investigations of potential lottery suppliers:

"This section shall be construed broadly and liberally to achieve the end of full disclosure of all information necessary to allow for a full and complete evaluation of the competence, integrity, and character of potential suppliers of the California State Lottery Commission." (§ 8880.57, subd. (e).)⁴

With this background in mind, we examine the key provisions of subdivision (a) of section 8880.57. Under subsection (1) of subdivision (a), a corporate bidder must disclose the names and addresses of its "officers, directors, and each owner."⁵ Here, one of the bidder's stockholders is another company. The name and address of this stockholder must be disclosed as an "owner" pursuant to subsection (1).

Subdivision (a), subsection (4), requires the disclosure of the names and addresses of the officers, directors and stockholders of any "parent" company of a bidder, where the bidder is a "subsidiary" corporation. No definitions of a "parent" or "subsidiary" corporation are found in the Act.

These terms are, however, defined by the Legislature in the general provisions of the Corporations Code. Except in particularly narrow circumstances, a "parent" corporation is "an affiliate controlling such corporation directly or indirectly through one or more intermediaries." (Corp. Code, § 175.) "Control" is defined for these purposes as "possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a corporation." (Corp. Code, § 160.) Except in one situation a "subsidiary" corporation is "a corporation shares of which possessing more than 50 percent of the voting power are owned directly or indirectly through one or more

⁴ Recently (Stats. 1986, ch. 55, § 19) the Legislature repealed and reenacted section 8880.57, generally making only technical and clarifying changes. It did, however, replace certain of the disclosure requirements mandated by the statute with a grant of discretion to the commission, allowing it to require the information as needed. None of the legislative changes bear upon the issues considered in this opinion.

⁵ Subsections (1), (4) and (6) of subdivision (a) all allow publicly traded corporations to limit the number of their "owner" disclosures to "those known to the corporation to beneficially own 5 percent or more of the publicly held securities." This qualification must be kept in mind throughout the discussion herein.

subsidiaries by the specified corporation." (Corp. Code, § 189.) We believe a California court would apply these definitions to the terms "parent" and "subsidiary" as used in section 8880.57.

Accordingly, when a bidder is a subsidiary corporation (more than 50 percent of the voting power of its shares are owned directly or indirectly by another corporation), the names and addresses of "the officers, directors, and stockholders of the parent company thereof" must be disclosed to the commission at the time of submitting the bid. (§ 8880.57, subd. (a)(4).)

Similarly, we believe that when the parent company (possessing power to direct the management and policies of the bidder either directly or through intermediaries) "is itself a corporation," the names and addresses of its officers, directors, and stockholders must be disclosed since such information is "necessary to determine ultimate ownership." (§ 8880.57, subd. (a)(6).) Such statutory construction provides consistency between subsections (4) and (6) of subdivision (a).

Moreover, if the parent is itself a subsidiary, subsection (6) of subdivision (a) requires the disclosure of the names and addresses of the officers, directors and stockholders of the parent's own parent. Where several intermediary corporations exist between the bidder and an ultimate parent corporation, we believe subsection (6) requires disclosure of the names and addresses of the officers, directors and stockholders of each intermediary and of the ultimate parent corporation. Such construction of subsection (6) is consistent with the definition of a "parent" corporation and in keeping with the statutory purpose of allowing "for a full and complete evaluation of the competence, integrity, and character of potential suppliers." (§ 8880.57, subd. (e).) The commission is entitled to know who has ultimate power of control over its suppliers.

If the corporate stockholder of the bidder does not have sufficient power to be considered a parent corporation, subsections (4) and (6) of subdivision (a) have no applicability. Such stockholder's own officers, directors and stockholders would not have to be disclosed under these subsections.

It may be argued, however, that subsection (1) of subdivision (a) would reach the stockholders of such a corporate stockholder. Subsection (1), it may be recalled, requires the disclosure of the names and addresses of "each owner, directly or indirectly, of any equity security or other ownership interest in the [bidder]." Does a stockholder of a company that owns stock in the bidder have an indirect ownership interest in the bidder for purposes of subsection (1)?

We believe that subdivision (a)(1) must be read in context and harmonized with the remainder of the statute. The provisions of (a)(4) and (a)(6) appear to be carefully worded to cover the situation where one corporation holds stock in another. To read subdivision (a)(1) too broadly would render much of the language of (a)(4) and (a)(6) surplusage and would treat officers and directors unequally with the stockholders of the same corporation. Rather, we believe that the reference in subdivision (a)(1) to an "indirect" ownership interest was meant to cover the normal situations where nominal and beneficial ownership interests are separate—in the case of trustees, executors, administrators, guardians, pledgees, conservators, custodians, receivers, agents and other fiduciaries. (See Corp. Code, § 702; *Most v. First Nat. Bank of San Diego* (1966) 246 Cal.App.2d 425, 431; 6 Witkin, Summary of Cal. Law (8th ed. 1974) Corporations, § 129, p. 4425.) These situations are readily distinguishable from where one owns stock in a corporation that happens to own stock in (but does not have the power of control over) another. (See *Albert v. McGrath* (S.D. Cal.1952) 104 F.Supp. 891, 897, revd. on other grounds sub nom. *Albert v. Brownell* (1954) 219 F.2d 602.)

We believe that the foregoing distinction and analysis fully supports the purposes of the Act as a whole and section 8880.57 in particular. Those persons and entities who are ultimately responsible for furnishing goods and services to the commission must disclose their identities so that "integrity, security, honesty, and fairness in the operation and administration of the Lottery" may be assured. (§ 8880.56.) The officers, directors, and stockholders of corporate stockholders of a supplier are not subject to disclosure unless there exists the power to control the operations through a parent-subsidiary relationship. Minority ownership without such power does not meet the parent or subsidiary reporting requirements of the statute. On the other hand, disclosure is required at each level of a chain of subsidiary-parent relationships until the ultimate parent is ascertained. Such determination harmonizes the reporting requirements for corporate suppliers, subsidiaries, and parent corporations.

In answer to the question presented, therefore, we conclude that when a corporation submits a bid to furnish goods or services to the California State Lottery, the corporation must disclose the names and addresses of the officers, directors and stockholders of a company that owns stock in the corporation if such company has the power to control the management and policies of the corporation.
