

# Why A Delaware Corporation Can Not Be A Subsidiary Of A California Corporation

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The California General Corporation Law defines a "subsidiary" of a specified corporation to be a "corporation shares of which possessing more than 50% of the voting power are owned directly or indirectly through one or more subsidiaries by the specified corporation." Cal. Corp. Code § 189(a). This may seem simple enough, but a careful reading of the definition yields many unexpected, and perhaps unintended, consequences.

As an initial matter, it is important to recognize that the definition employs several terms that are also defined by the GCL (*i.e.*, "corporation" (Section 162), "shares" (Section 184) and "voting power" (Section 194.5)). Applying these definitions, several significant, but likely unintended, conclusions can be reached. First, the statute does not define what constitutes a subsidiary of a foreign corporation because a foreign corporation is not a "corporation." Second, the statute does not define what constitutes a subsidiary of a limited liability company or other form of entity (domestic or foreign). Third, a foreign corporation or other form of entity cannot be a subsidiary.

The statute lays down a special rule in the case of Section 703(b) which provides that "Shares of a corporation owned by its subsidiary shall not be entitled to vote on any matter." In this case, a corporation will be a subsidiary if more than 25% of the

voting power (rather than 50%) is possessed by another corporation. Interestingly, this means that the same corporation could be a subsidiary of multiple corporations.

Putting the foregoing together, can yield some surprising results. For example, a California corporation may possess 100% of the voting power of a Delaware corporation and 30% of the voting power of a California corporation. If both of these corporations own shares in the California corporation, Section 703(b) would prevent the voting of those shares by the California corporation but not the Delaware corporation.

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