

Senate Bill No. 1155

CHAPTER 516

An act to amend Sections 25102, 28047, 28100, 28152, 28154, 28400, and 28404 of, to add Sections 28047.1 and 28111 to, to repeal Sections 28401, 28402, and 28403 of, and to repeal and add Article 2 (commencing with Section 28820) of Chapter 12 of Division 3 of Title 4 of, the Corporations Code, relating to capital access companies.

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LEGISLATIVE COUNSEL'S DIGEST

SB 1155, Dutton. Capital access companies.

Existing law, the Capital Access Company Law, provides for the licensure and regulation by the Commissioner of Corporations of capital access companies to enable those entities to provide risk capital and management assistance to small businesses in the state, exempt from the requirements of the federal Investment Company Act of 1940.

Under existing law, a capital access company is only authorized to engage in the business of providing financing assistance through the purchase of securities of small business firms doing business or proposing to do business wholly or substantially in this state, and providing managerial and technical assistance to these firms, subject to certain exceptions. Existing law defines a "small business firm" as a person meeting specified criteria, including, without limitation, having fewer than 500 employees.

This bill would redefine a small business firm as a person that, together with its affiliates, has a net worth of not more than \$18,000,000 and average net income after federal income taxes, as specified, no greater than \$6,000,000. The bill would also define a "smaller business firm" as a person that, together with its affiliates, has a net worth of not more than \$6,000,000 and average net income after federal income taxes, as specified, no greater than \$2,000,000, and would require that at least 20% of all financing assistance provided by a licensee shall be through the purchase of securities of smaller business firms proposing to do business wholly or substantially in this state.

Existing federal law provides for licensure and regulation of small business investment companies by the Small Business Administration.

This bill would provide that, if a capital access company becomes a small business investment company, specified federal regulations shall supersede regulatory requirements under the Corporations Code, except as specified, and that a violation of those federal regulations would constitute a violation of this act.

Existing law requires, as a condition of licensure of a capital access company, that a person who makes recommendations with respect to the investment of funds of the company be an investment adviser, as specified, and not be subject to specified acts and omissions, convictions, and other legal actions.

This bill would instead require that no person with a specified relationship or connection with the applicant be subject to those acts, omissions, convictions, or other legal actions.

This bill would also revise and recast provisions of the Capital Access Company Law relating to conflicts of interest.

Existing state law requires a capital access company to use its best efforts to provide financing assistance to small business firms doing business or proposing to do business wholly or substantially in this state, and makes related prohibitions and exceptions to providing services to persons out of state. Existing state law also prohibits a capital access company from providing financing assistance to a small business firm whose primary business is providing financing assistance. Existing federal law requires a California capital access company to state in its organizational documents that its activities are limited to providing financial or managerial services to enterprises doing business, or proposing to do business, in this state.

This bill would eliminate those state law prohibitions.

Existing law makes it unlawful for any person to offer or sell in this state any security in an issuer transaction unless the sale has been qualified or unless the security or transaction is exempt or not subject to qualification, as specified. Under existing law, an offer or sale of nonredeemable securities to accredited investors by a person licensed pursuant to the Capital Access Company Law is exempt from these qualification requirements.

This bill would maintain that exemption provided that all purchasers either have a preexisting personal or business relationship with the offeror, as specified, or by reason of their business or financial experience or the business or financial experience of their specified professional advisers could be reasonably assumed to have the capacity to protect their own interests in connection with the transaction. The bill would specify that this exemption is not available under certain circumstances.

The people of the State of California do enact as follows:

SECTION 1. Section 25102 of the Corporations Code is amended to read:

25102. The following transactions are exempted from the provisions of Section 25110:

(a) Any offer (but not a sale) not involving any public offering and the execution and delivery of any agreement for the sale of securities pursuant to the offer if (1) the agreement contains substantially the following provision: “The sale of the securities that are the subject of this agreement has not been qualified with the Commissioner of Corporations of the State

of California and the issuance of the securities or the payment or receipt of any part of the consideration therefor prior to the qualification is unlawful, unless the sale of securities is exempt from the qualification by Section 25100, 25102, or 25105 of the California Corporations Code. The rights of all parties to this agreement are expressly conditioned upon the qualification being obtained, unless the sale is so exempt"; and (2) no part of the purchase price is paid or received and none of the securities are issued until the sale of the securities is qualified under this law unless the sale of securities is exempt from the qualification by this section, Section 25100, or 25105.

(b) Any offer (but not a sale) of a security for which a registration statement has been filed under the Securities Act of 1933 but has not yet become effective, or for which an offering statement under Regulation A has been filed but has not yet been qualified, if no stop order or refusal order is in effect and no public proceeding or examination looking towards an order is pending under Section 8 of the act and no order under Section 25140 or subdivision (a) of Section 25143 is in effect under this law.

(c) Any offer (but not a sale) and the execution and delivery of any agreement for the sale of securities pursuant to the offer as may be permitted by the commissioner upon application. Any negotiating permit under this subdivision shall be conditioned to the effect that none of the securities may be issued and none of the consideration therefor may be received or accepted until the sale of the securities is qualified under this law.

(d) Any transaction or agreement between the issuer and an underwriter or among underwriters if the sale of the securities is qualified, or exempt from qualification, at the time of distribution thereof in this state, if any.

(e) Any offer or sale of any evidence of indebtedness, whether secured or unsecured, and any guarantee thereof, in a transaction not involving any public offering.

(f) Any offer or sale of any security in a transaction (other than an offer or sale to a pension or profit-sharing trust of the issuer) that meets each of the following criteria:

(1) Sales of the security are not made to more than 35 persons, including persons not in this state.

(2) All purchasers either have a preexisting personal or business relationship with the offeror or any of its partners, officers, directors or controlling persons, or managers (as appointed or elected by the members) if the offeror is a limited liability company, or by reason of their business or financial experience or the business or financial experience of their professional advisers who are unaffiliated with and who are not compensated by the issuer or any affiliate or selling agent of the issuer, directly or indirectly, could be reasonably assumed to have the capacity to protect their own interests in connection with the transaction.

(3) Each purchaser represents that the purchaser is purchasing for the purchaser's own account (or a trust account if the purchaser is a trustee) and not with a view to or for sale in connection with any distribution of the security.

(4) The offer and sale of the security is not accomplished by the publication of any advertisement. The number of purchasers referred to above is exclusive of any described in subdivision (i), any officer, director, or affiliate of the issuer, or manager (as appointed or elected by the members) if the issuer is a limited liability company, and any other purchaser who the commissioner designates by rule. For purposes of this section, a husband and wife (together with any custodian or trustee acting for the account of their minor children) are counted as one person and a partnership, corporation, or other organization that was not specifically formed for the purpose of purchasing the security offered in reliance upon this exemption, is counted as one person. The commissioner may by rule require the issuer to file a notice of transactions under this subdivision.

The failure to file the notice or the failure to file the notice within the time specified by the rule of the commissioner shall not affect the availability of this exemption. An issuer who fails to file the notice as provided by rule of the commissioner shall, within 15 business days after discovery of the failure to file the notice or after demand by the commissioner, whichever occurs first, file the notice and pay to the commissioner a fee equal to the fee payable had the transaction been qualified under Section 25110.

(g) Any offer or sale of conditional sale agreements, equipment trust certificates, or certificates of interest or participation therein or partial assignments thereof, covering the purchase of railroad rolling stock or equipment or the purchase of motor vehicles, aircraft, or parts thereof, in a transaction not involving any public offering.

(h) Any offer or sale of voting common stock by a corporation incorporated in any state if, immediately after the proposed sale and issuance, there will be only one class of stock of the corporation outstanding that is owned beneficially by no more than 35 persons, provided all of the following requirements have been met:

(1) The offer and sale of the stock is not accompanied by the publication of any advertisement, and no selling expenses have been given, paid, or incurred in connection therewith.

(2) The consideration to be received by the issuer for the stock to be issued consists of any of the following:

(A) Only assets (which may include cash) of an existing business enterprise transferred to the issuer upon its initial organization, of which all of the persons who are to receive the stock to be issued pursuant to this exemption were owners during, and the enterprise was operated for, a period of not less than one year immediately preceding the proposed issuance, and the ownership of the enterprise immediately prior to the proposed issuance was in the same proportions as the shares of stock are to be issued.

(B) Only cash or cancellation of indebtedness for money borrowed, or both, upon the initial organization of the issuer, provided all of the stock is issued for the same price per share.

(C) Only cash, provided the sale is approved in writing by each of the existing shareholders and the purchaser or purchasers are existing shareholders.

(D) In a case where after the proposed issuance there will be only one owner of the stock of the issuer, only any legal consideration.

(3) No promotional consideration has been given, paid, or incurred in connection with the issuance. Promotional consideration means any consideration paid directly or indirectly to a person who, acting alone or in conjunction with one or more other persons, takes the initiative in founding and organizing the business or enterprise of an issuer for services rendered in connection with the founding or organizing.

(4) A notice in a form prescribed by rule of the commissioner, signed by an active member of the State Bar of California, is filed with or mailed for filing to the commissioner not later than 10 business days after receipt of consideration for the securities by the issuer. That notice shall contain an opinion of the member of the State Bar of California that the exemption provided by this subdivision is available for the offer and sale of the securities. The failure to file the notice as required by this subdivision and the rules of the commissioner shall not affect the availability of this exemption. An issuer who fails to file the notice within the time specified by this subdivision shall, within 15 business days after discovery of the failure to file the notice or after demand by the commissioner, whichever occurs first, file the notice and pay to the commissioner a fee equal to the fee payable had the transaction been qualified under Section 25110. The notice, except when filed on behalf of a California corporation, shall be accompanied by an irrevocable consent, in the form that the commissioner by rule prescribes, appointing the commissioner or his or her successor in office to be the issuer's attorney to receive service of any lawful process in any noncriminal suit, action, or proceeding against it or its successor that arises under this law or any rule or order hereunder after the consent has been filed, with the same force and validity as if served personally on the issuer. An issuer on whose behalf a consent has been filed in connection with a previous qualification or exemption from qualification under this law (or application for a permit under any prior law if the application or notice under this law states that the consent is still effective) need not file another. Service may be made by leaving a copy of the process in the office of the commissioner, but it is not effective unless (A) the plaintiff, who may be the commissioner in a suit, action, or proceeding instituted by him or her, forthwith sends notice of the service and a copy of the process by registered or certified mail to the defendant or respondent at its last address on file with the commissioner, and (B) the plaintiff's affidavit of compliance with this section is filed in the case on or before the return day of the process, if any, or within the further time as the court allows.

(5) Each purchaser represents that the purchaser is purchasing for the purchaser's own account, or a trust account if the purchaser is a trustee, and not with a view to or for sale in connection with any distribution of the stock.

For the purposes of this subdivision, all securities held by a husband and wife, whether or not jointly, shall be considered to be owned by one person, and all securities held by a corporation that has issued stock pursuant to this

exemption shall be considered to be held by the shareholders to whom it has issued the stock.

All stock issued by a corporation pursuant to this subdivision as it existed prior to the effective date of the amendments to this section made during the 1996 portion of the 1995–96 Regular Session that required the issuer to have stamped or printed prominently on the face of the stock certificate a legend in a form prescribed by rule of the commissioner restricting transfer of the stock in a manner provided for by that rule shall not be subject to the transfer restriction legend requirement and, by operation of law, the corporation is authorized to remove that transfer restriction legend from the certificates of those shares of stock issued by the corporation pursuant to this subdivision as it existed prior to the effective date of the amendments to this section made during the 1996 portion of the 1995–96 Regular Session.

(i) Any offer or sale (1) to a bank, savings and loan association, trust company, insurance company, investment company registered under the Investment Company Act of 1940, pension or profit-sharing trust (other than a pension or profit-sharing trust of the issuer, a self-employed individual retirement plan, or individual retirement account), or other institutional investor or governmental agency or instrumentality that the commissioner may designate by rule, whether the purchaser is acting for itself or as trustee, or (2) to any corporation with outstanding securities registered under Section 12 of the Securities Exchange Act of 1934 or any wholly owned subsidiary of the corporation that after the offer and sale will own directly or indirectly 100 percent of the outstanding capital stock of the issuer, provided the purchaser represents that it is purchasing for its own account (or for the trust account) for investment and not with a view to or for sale in connection with any distribution of the security.

(j) Any offer or sale of any certificate of interest or participation in an oil or gas title or lease (including subsurface gas storage and payments out of production) if either of the following apply:

(1) All of the purchasers meet one of the following requirements:

(A) Are and have been during the preceding two years engaged primarily in the business of drilling for, producing, or refining oil or gas (or whose corporate predecessor, in the case of a corporation, has been so engaged).

(B) Are persons described in paragraph (1) of subdivision (i).

(C) Have been found by the commissioner upon written application to be substantially engaged in the business of drilling for, producing, or refining oil or gas so as not to require the protection provided by this law (which finding shall be effective until rescinded).

(2) The security is concurrently hypothecated to a bank in the ordinary course of business to secure a loan made by the bank, provided that each purchaser represents that it is purchasing for its own account for investment and not with a view to or for sale in connection with any distribution of the security.

(k) Any offer or sale of any security under, or pursuant to, a plan of reorganization under Chapter 11 of the federal bankruptcy law that has been

confirmed or is subject to confirmation by the decree or order of a court of competent jurisdiction.

(l) Any offer or sale of an option, warrant, put, call, or straddle, and any guarantee of any of these securities, by a person who is not the issuer of the security subject to the right, if the transaction, had it involved an offer or sale of the security subject to the right by the person, would not have violated Section 25110 or 25130.

(m) Any offer or sale of a stock to a pension, profit-sharing, stock bonus, or employee stock ownership plan, provided that (1) the plan meets the requirements for qualification under Section 401 of the Internal Revenue Code, and (2) the employees are not required or permitted individually to make any contributions to the plan. The exemption provided by this subdivision shall not be affected by whether the stock is contributed to the plan, purchased from the issuer with contributions by the issuer or an affiliate of the issuer, or purchased from the issuer with funds borrowed from the issuer, an affiliate of the issuer, or any other lender.

(n) Any offer or sale of any security in a transaction, other than an offer or sale of a security in a rollup transaction, that meets all of the following criteria:

(1) The issuer is (A) a California corporation or foreign corporation that, at the time of the filing of the notice required under this subdivision, is subject to Section 2115, or (B) any other form of business entity, including without limitation a partnership or trust organized under the laws of this state. The exemption provided by this subdivision is not available to a “blind pool” issuer, as that term is defined by the commissioner, or to an investment company subject to the Investment Company Act of 1940.

(2) Sales of securities are made only to qualified purchasers or other persons the issuer reasonably believes, after reasonable inquiry, to be qualified purchasers. A corporation, partnership, or other organization specifically formed for the purpose of acquiring the securities offered by the issuer in reliance upon this exemption may be a qualified purchaser if each of the equity owners of the corporation, partnership, or other organization is a qualified purchaser. Qualified purchasers include the following:

(A) A person designated in Section 260.102.13 of Title 10 of the California Code of Regulations.

(B) A person designated in subdivision (i) or any rule of the commissioner adopted thereunder.

(C) A pension or profit-sharing trust of the issuer, a self-employed individual retirement plan, or an individual retirement account, if the investment decisions made on behalf of the trust, plan, or account are made solely by persons who are qualified purchasers.

(D) An organization described in Section 501(c)(3) of the Internal Revenue Code, corporation, Massachusetts or similar business trust, or partnership, each with total assets in excess of five million dollars (\$5,000,000) according to its most recent audited financial statements.

(E) With respect to the offer and sale of one class of voting common stock of an issuer or of preferred stock of an issuer entitling the holder thereof to at least the same voting rights as the issuer's one class of voting common stock, provided that the issuer has only one-class voting common stock outstanding upon consummation of the offer and sale, a natural person who, either individually or jointly with the person's spouse, (i) has a minimum net worth of two hundred fifty thousand dollars (\$250,000) and had, during the immediately preceding tax year, gross income in excess of one hundred thousand dollars (\$100,000) and reasonably expects gross income in excess of one hundred thousand dollars (\$100,000) during the current tax year or (ii) has a minimum net worth of five hundred thousand dollars (\$500,000). "Net worth" shall be determined exclusive of home, home furnishings, and automobiles. Other assets included in the computation of net worth may be valued at fair market value.

Each natural person specified above, by reason of his or her business or financial experience, or the business or financial experience of his or her professional adviser, who is unaffiliated with and who is not compensated, directly or indirectly, by the issuer or any affiliate or selling agent of the issuer, can be reasonably assumed to have the capacity to protect his or her interests in connection with the transaction. The amount of the investment of each natural person shall not exceed 10 percent of the net worth, as determined by this subparagraph, of that natural person.

(F) Any other purchaser designated as qualified by rule of the commissioner.

(3) Each purchaser represents that the purchaser is purchasing for the purchaser's own account (or trust account, if the purchaser is a trustee) and not with a view to or for sale in connection with a distribution of the security.

(4) Each natural person purchaser, including a corporation, partnership, or other organization specifically formed by natural persons for the purpose of acquiring the securities offered by the issuer, receives, at least five business days before securities are sold to, or a commitment to purchase is accepted from, the purchaser, a written offering disclosure statement that shall meet the disclosure requirements of Regulation D (17 C.F.R. 230.501 et seq.), and any other information as may be prescribed by rule of the commissioner, provided that the issuer shall not be obligated pursuant to this paragraph to provide this disclosure statement to a natural person qualified under Section 260.102.13 of Title 10 of the California Code of Regulations. The offer or sale of securities pursuant to a disclosure statement required by this paragraph that is in violation of Section 25401, or that fails to meet the disclosure requirements of Regulation D (17 C.F.R. 230.501 et seq.), shall not render unavailable to the issuer the claim of an exemption from Section 25110 afforded by this subdivision. This paragraph does not impose, directly or indirectly, any additional disclosure obligation with respect to any other exemption from qualification available under any other provision of this section.

(5) (A) A general announcement of proposed offering may be published by written document only, provided that the general announcement of proposed offering sets forth the following required information:

- (i) The name of the issuer of the securities.
- (ii) The full title of the security to be issued.
- (iii) The anticipated suitability standards for prospective purchasers.
- (iv) A statement that (I) no money or other consideration is being solicited or will be accepted, (II) an indication of interest made by a prospective purchaser involves no obligation or commitment of any kind, and, if the issuer is required by paragraph (4) to deliver a disclosure statement to prospective purchasers, (III) no sales will be made or commitment to purchase accepted until five business days after delivery of a disclosure statement and subscription information to the prospective purchaser in accordance with the requirements of this subdivision.

(v) Any other information required by rule of the commissioner.

(vi) The following legend: "For more complete information about (Name of Issuer) and (Full Title of Security), send for additional information from (Name and Address) by sending this coupon or calling (Telephone Number)."

(B) The general announcement of proposed offering referred to in subparagraph (A) may also set forth the following information:

- (i) A brief description of the business of the issuer.
- (ii) The geographic location of the issuer and its business.
- (iii) The price of the security to be issued, or, if the price is not known, the method of its determination or the probable price range as specified by the issuer, and the aggregate offering price.

(C) The general announcement of proposed offering shall contain only the information that is set forth in this paragraph.

(D) Dissemination of the general announcement of proposed offering to persons who are not qualified purchasers, without more, shall not disqualify the issuer from claiming the exemption under this subdivision.

(6) No telephone solicitation shall be permitted until the issuer has determined that the prospective purchaser to be solicited is a qualified purchaser.

(7) The issuer files a notice of transaction under this subdivision both (A) concurrent with the publication of a general announcement of proposed offering or at the time of the initial offer of the securities, whichever occurs first, accompanied by a filing fee, and (B) within 10 business days following the close or abandonment of the offering, but in no case more than 210 days from the date of filing the first notice. The first notice of transaction under subparagraph (A) shall contain an undertaking, in a form acceptable to the commissioner, to deliver any disclosure statement required by paragraph (4) to be delivered to prospective purchasers, and any supplement thereto, to the commissioner within 10 days of the commissioner's request for the information. The exemption from qualification afforded by this subdivision is unavailable if an issuer fails to file the first notice required under subparagraph (A) or to pay the filing fee. The commissioner has the authority to assess an administrative penalty of up to one thousand dollars (\$1,000)

against an issuer that fails to deliver the disclosure statement required to be delivered to the commissioner upon the commissioner's request within the time period set forth above. Neither the filing of the disclosure statement nor the failure by the commissioner to comment thereon precludes the commissioner from taking any action deemed necessary or appropriate under this division with respect to the offer and sale of the securities.

(o) An offer or sale of any security issued by a corporation or limited liability company pursuant to a purchase plan or agreement, or issued pursuant to an option plan or agreement, where the security at the time of issuance or grant is exempt from registration under the Securities Act of 1933, as amended, pursuant to Rule 701 adopted pursuant to that act (17 C.F.R. 230.701), the provisions of which are hereby incorporated by reference into this section, provided that (1) the terms of any purchase plan or agreement shall comply with Sections 260.140.42, 260.140.45, and 260.140.46 of Title 10 of the California Code of Regulations, (2) the terms of any option plan or agreement shall comply with Sections 260.140.41, 260.140.45, and 260.140.46 of Title 10 of the California Code of Regulations, and (3) the issuer files a notice of transaction in accordance with rules adopted by the commissioner no later than 30 days after the initial issuance of any security under that plan, accompanied by a filing fee as prescribed by subdivision (y) of Section 25608. The failure to file the notice of transaction within the time specified in this subdivision shall not affect the availability of this exemption. An issuer that fails to file the notice shall, within 15 business days after discovery of the failure to file the notice or after demand by the commissioner, whichever occurs first, file the notice and pay the commissioner a fee equal to the maximum aggregate fee payable had the transaction been qualified under Section 25110.

Offers and sales exempt pursuant to this subdivision shall be deemed to be part of a single, discrete offering and are not subject to integration with any other offering or sale, whether qualified under Chapter 2 (commencing with Section 25110), or otherwise exempt, or not subject to qualification.

(p) An offer or sale of nonredeemable securities to accredited investors (Section 28031) by a person licensed under the Capital Access Company Law (Division 3 (commencing with Section 28000) of Title 4), provided that all purchasers either (1) have a preexisting personal or business relationship with the offeror or any of its partners, officers, directors, controlling persons, or managers (as appointed or elected by the members), or (2) by reason of their business or financial experience or the business or financial experience of their professional advisers who are unaffiliated with and who are not compensated by the issuer or any affiliate or selling agent of the issuer, directly or indirectly, could be reasonably assumed to have the capacity to protect their own interests in connection with the transaction. All nonredeemable securities shall be evidenced by certificates that shall have stamped or printed prominently on their face a legend in a form to be prescribed by rule or order of the commissioner restricting transfer of the securities in the manner as the rule or order provides. The exemption under this subdivision shall not be available for any offering that is exempt or

asserted to be exempt pursuant to Section 3(a)(11) of the Securities Act of 1933 (15 U.S.C. Sec. 77c(a)(11)) or Rule 147 (17 C.F.R. Sec. 230.147) thereunder or otherwise is conducted by means of any form of general solicitation or general advertising.

(q) Any offer or sale of any viatical or life settlement contract or fractionalized or pooled interest therein in a transaction that meets all of the following criteria:

(1) Sales of securities described in this subdivision are made only to qualified purchasers or other persons the issuer reasonably believes, after reasonable inquiry, to be qualified purchasers. A corporation, partnership, or other organization specifically formed for the purpose of acquiring the securities offered by the issuer in reliance upon this exemption may be a qualified purchaser only if each of the equity owners of the corporation, partnership, or other organization is a qualified purchaser. Qualified purchasers include the following:

(A) A person designated in Section 260.102.13 of Title 10 of the California Code of Regulations.

(B) A person designated in subdivision (i) or any rule of the commissioner adopted thereunder.

(C) A pension or profit-sharing trust of the issuer, a self-employed individual retirement plan, or an individual retirement account, if the investment decisions made on behalf of the trust, plan, or account are made solely by persons who are qualified purchasers.

(D) An organization described in Section 501(c)(3) of the Internal Revenue Code, corporation, Massachusetts or similar business trust, or partnership, each with total assets in excess of five million dollars (\$5,000,000) according to its most recent audited financial statements.

(E) A natural person who, either individually or jointly with the person's spouse, (i) has a minimum net worth of one hundred fifty thousand dollars (\$150,000) and had, during the immediately preceding tax year, gross income in excess of one hundred thousand dollars (\$100,000) and reasonably expects gross income in excess of one hundred thousand dollars (\$100,000) during the current tax year or (ii) has a minimum net worth of two hundred fifty thousand dollars (\$250,000). "Net worth" shall be determined exclusive of home, home furnishings, and automobiles. Other assets included in the computation of net worth may be valued at fair market value.

Each natural person specified above, by reason of his or her business or financial experience, or the business or financial experience of his or her professional adviser, who is unaffiliated with and who is not compensated, directly or indirectly, by the issuer or any affiliate or selling agent of the issuer, can be reasonably assumed to have the capacity to protect his or her interests in connection with the transaction.

The amount of the investment of each natural person shall not exceed 10 percent of the net worth, as determined by this subdivision, of that natural person.

(F) Any other purchaser designated as qualified by rule of the commissioner.

(2) Each purchaser represents that the purchaser is purchasing for the purchaser's own account (or trust account, if the purchaser is a trustee) and not with a view to or for sale in connection with a distribution of the security.

(3) Each natural person purchaser, including a corporation, partnership, or other organization specifically formed by natural persons for the purpose of acquiring the securities offered by the issuer, receives, at least five business days before securities described in this subdivision are sold to, or a commitment to purchase is accepted from, the purchaser, the following information in writing:

(A) The name, principal business and mailing address, and telephone number of the issuer.

(B) The suitability standards for prospective purchasers as set forth in paragraph (1) of this subdivision.

(C) A description of the issuer's type of business organization and the state in which the issuer is organized or incorporated.

(D) A brief description of the business of the issuer.

(E) If the issuer retains ownership or becomes the beneficiary of the insurance policy, an audit report of an independent certified public accountant together with a balance sheet and related statements of income, retained earnings, and cashflows that reflect the issuer's financial position, the results of the issuer's operations, and the issuer's cashflows as of a date within 15 months before the date of the initial issuance of the securities described in this subdivision. The financial statements listed in this subparagraph shall be prepared in conformity with generally accepted accounting principles. If the date of the audit report is more than 120 days before the date of the initial issuance of the securities described in this subdivision, the issuer shall provide unaudited interim financial statements.

(F) The names of all directors, officers, partners, members, or trustees of the issuer.

(G) A description of any order, judgment, or decree that is final as to the issuing entity of any state, federal, or foreign country governmental agency or administrator, or of any state, federal or foreign country court of competent jurisdiction (i) revoking, suspending, denying, or censuring for cause any license, permit, or other authority of the issuer or of any director, officer, partner, member, trustee, or person owning or controlling, directly or indirectly, 10 percent or more of the outstanding interest or equity securities of the issuer, to engage in the securities, commodities, franchise, insurance, real estate, or lending business or in the offer or sale of securities, commodities, franchises, insurance, real estate, or loans, (ii) permanently restraining, enjoining, barring, suspending, or censuring any such person from engaging in or continuing any conduct, practice, or employment in connection with the offer or sale of securities, commodities, franchises, insurance, real estate, or loans, (iii) convicting any such person of, or pleading nolo contendere by any such person to, any felony or misdemeanor involving a security, commodity, franchise, insurance, real estate, or loan, or any aspect of the securities, commodities, franchise, insurance, real estate, or lending business, or involving dishonesty, fraud, deceit, embezzlement,

fraudulent conversion, or misappropriation of property, or (iv) holding any such person liable in a civil action involving breach of a fiduciary duty, fraud, deceit, embezzlement, fraudulent conversion, or misappropriation of property. This subparagraph does not apply to any order, judgment, or decree that has been vacated, overturned, or is more than 10 years old.

(H) Notice of the purchaser's right to rescind or cancel the investment and receive a refund pursuant to Section 25508.5.

(I) The name, address, and telephone number of the issuing insurance company, and the name, address, and telephone number of the state or foreign country regulator of the insurance company.

(J) The total face value of the insurance policy and the percentage of the insurance policy the purchaser will own.

(K) The insurance policy number, issue date, and type.

(L) If a group insurance policy, the name, address, and telephone number of the group, and, if applicable, the material terms and conditions of converting the policy to an individual policy, including the amount of increased premiums.

(M) If a term insurance policy, the term and the name, address, and telephone number of the person who will be responsible for renewing the policy if necessary.

(N) That the insurance policy is beyond the state statute for contestability and the reason therefor.

(O) The insurance policy premiums and terms of premium payments.

(P) The amount of the purchaser's moneys that will be set aside to pay premiums.

(Q) The name, address, and telephone number of the person who will be the insurance policy owner and the person who will be responsible for paying premiums.

(R) The date on which the purchaser will be required to pay premiums and the amount of the premium, if known.

(S) A statement to the effect that any projected rate of return to the purchaser from the purchase of a viatical or life settlement contract or a fractionalized or pooled interest therein is based on an estimated life expectancy for the person insured under the life insurance policy; that the return on the purchase may vary substantially from the expected rate of return based upon the actual life expectancy of the insured that may be less than, equal to, or may greatly exceed the estimated life expectancy; and that the rate of return would be higher if the actual life expectancy were less than, and lower if the actual life expectancy were greater than the estimated life expectancy of the insured at the time the viatical or life settlement contract was closed.

(T) A statement that the purchaser should consult with his or her tax adviser regarding the tax consequences of the purchase of the viatical or life settlement contract or fractionalized or pooled interest therein and, if the purchaser is using retirement funds or accounts for that purchase, whether or not any adverse tax consequences might result from the use of those funds for the purchase of that investment.

(U) Any other information as may be prescribed by rule of the commissioner.

SEC. 2. Section 28047 of the Corporations Code is amended to read:

28047. “Small business firm” means a person that proposes to transact, or transacts, business on a regular and continuous basis in California and, together with its affiliates, has a net worth of not more than eighteen million dollars (\$18,000,000) and average net income after federal income taxes, excluding any carryover losses, for the preceding two years no greater than six million dollars (\$6,000,000).

SEC. 3. Section 28047.1 is added to the Corporations Code, to read:

28047.1. “Smaller business firm” means a person that proposes to transact, or transacts, business on a regular and continuous basis in California and, together with its affiliates, has a net worth of not more than six million dollars (\$6,000,000), and average net income after federal income taxes, excluding any carryover losses, for the preceding two years no greater than two million dollars (\$2,000,000).

SEC. 4. Section 28100 of the Corporations Code is amended to read:

28100. The commissioner shall administer and enforce the provisions of this division in a manner that facilitates the legislative purposes set forth in Section 28004, consistent with protection of investors.

SEC. 5. Section 28111 is added to the Corporations Code, to read:

28111. (a) If a licensee becomes licensed as a small business investment company and is subject to regulation by the Small Business Administration under the federal Small Business Investment Act of 1958, the commissioner may by rule or order provide that a licensee in compliance with those federal regulations shall be deemed to be in compliance with the regulatory requirements under this division except those provisions required to exempt licensees from regulation under the federal Investment Company Act of 1940, and the provisions of Chapter 8 (commencing with Section 28550), Chapter 9 (commencing with Section 28600), Chapter 10 (commencing with Section 28650), Chapter 11 (commencing with Section 28700), Chapter 12 (commencing with Section 28800), Chapter 13 (commencing with Section 28900), and Chapter 14 (commencing with Section 28950).

(b) A violation by a licensee of any regulation promulgated by the Small Business Administration that the commissioner has by rule or order deemed to be consistent with the regulatory requirements under this division shall constitute a violation of this division. The commissioner shall have all of the powers granted in this division to enforce those federal regulations against a licensee.

SEC. 6. Section 28152 of the Corporations Code is amended to read:

28152. If the commissioner finds all of the following with respect to an application for a license, the commissioner shall approve the application:

(a) That the applicant has a tangible net worth, exclusive of the funds to invest under subdivision (b), in an amount that is not less than two hundred fifty thousand dollars (\$250,000) and that the tangible net worth is adequate for the applicant to transact business as a capital access company.

(b) That the applicant has funds to invest in an amount that is not less than five million dollars (\$5,000,000).

(c) That the applicant has, in addition to the requirements of subdivisions (a) and (b), financial resources in an amount that is adequate for the applicant to pay its expenses in transacting business as a capital access company for a period of not less than three years from the date of licensure.

(d) That the directors, officers, and controlling persons of the applicant are each of good character and sound financial standing, that the directors and officers of the applicant are each competent to perform their functions with respect to the applicant, and that the directors and officers of the applicant are collectively adequate to manage the business of the applicant as a capital access company. For purposes of this subdivision, the commissioner shall accord weight to the prior or current successful operation of a commercial or investment enterprise.

(e) That none of the following persons are subject to any act or omission enumerated in subdivision (a), (e), (f), or (g) of Section 25212, or has been convicted of, or pled nolo contendere to, any offense or been held liable in any civil action specified in subdivision (b) of Section 25212, or is enjoined from any act, conduct, or practice specified in subdivision (c) of Section 25212, or is subject to any order specified in subdivision (d) of Section 25212:

(1) A person who is or will be a controlling person of the applicant.

(2) A person who makes or will make recommendations with respect to the investment of funds of the applicant.

(3) A person who is or will be a partner, principal executive officer, manager, or director of the applicant.

(4) A person who occupies or will occupy a similar status or who performs or will perform similar functions to those listed above in paragraphs (1) to (3), inclusive.

(5) An employee who materially aids or assists or will materially aid or assist in the applicant's investment-related functions.

(6) A broker-dealer or agent who materially aids or assists or will materially aid or assist in the sale or distribution of any securities of the applicant.

(f) That it is reasonable to believe that the applicant, if licensed, will comply with the provisions of Section 6(a)(5) of the Investment Company Act of 1940, the applicable provisions of the Corporate Securities Law of 1968, this division, and of any regulation adopted or order issued under this division.

If, after notice and a hearing, the commissioner finds otherwise, the commissioner shall deny the application.

SEC. 7. Section 28154 of the Corporations Code is amended to read:

28154. Except pursuant to Section 28551, no license shall be transferable or assignable.

SEC. 8. Section 28400 of the Corporations Code is amended to read:

28400. No licensee shall engage in any business other than the following:

(a) The business of providing financing assistance through the purchase of securities of small business firms or smaller business firms doing business or proposing to do business wholly or substantially in this state.

(b) The business of providing managerial assistance (including managerial and technical assistance) to small business firms or smaller business firms doing business or proposing to do business wholly or substantially in this state.

(c) At least 20 percent of all financing assistance provided by the licensee shall be through purchase of securities of smaller business firms doing business or proposing to do business wholly or substantially in this state.

SEC. 9. Section 28401 of the Corporations Code is repealed.

SEC. 10. Section 28402 of the Corporations Code is repealed.

SEC. 11. Section 28403 of the Corporations Code is repealed.

SEC. 12. Section 28404 of the Corporations Code is amended to read: 28404. No licensee shall provide financing assistance to any small business firm for the purpose of evading the requirements of this division.

SEC. 13. Article 2 (commencing with Section 28820) of Chapter 12 of Division 3 of Title 4 of the Corporations Code is repealed.

SEC. 14. Article 2 (commencing with Section 28820) is added to Chapter 12 of Division 3 of Title 4 of the Corporations Code, to read:

Article 2. Conflicts of Interest

28820. In this article, unless the context otherwise requires:

(a) (1) "Associate," when used with respect to a licensee, means all of the following:

(A) Any principal shareholder, director, officer, manager, agent, or adviser of the licensee.

(B) Any director, officer, partner, general manager, agent, employer, or employee of any person referred to in subparagraph (A).

(C) Any person who controls, is controlled by, or is under common control with, any person referred to in subparagraph (A), directly or indirectly, through one or more intermediaries.

(D) Any close relative of any person referred to in subparagraph (A).

(E) Any person of whom any person referred to in subparagraphs (A) to (D), inclusive, is a director or officer.

(F) Any person in whom any person referred to in subparagraphs (A) to (D), inclusive, or any combination of persons acting in concert owns or controls, directly or indirectly, a 10-percent or greater equity interest.

(2) For purposes of this subdivision, any person who is in any of the relationships referred to in subparagraphs (A) to (F), inclusive, of paragraph (1) within six months before or after a licensee provides financing assistance shall be deemed to be in the relationship as of the date when the licensee provides the financing assistance.

(3) For purposes of this subdivision, if a licensee, in order to protect its interests, designates any person to serve as a director of, officer of, or in

any capacity in the management of, a small business firm to which the licensee provides financing assistance, the person shall not, on that account, be deemed to have any relationship with the small business firm. However, this paragraph shall not apply in any case where the person has, directly or indirectly, any other financial interest in the small business firm or where the person, at any time before the licensee provides the financing assistance, served as a director of, officer of, or in any other capacity in the management of, the small business firm for a period of 30 days or more.

(b) “Close relative” means ancestor, lineal descendant, brother or sister and lineal descendants of either, spouse, father-in-law, mother-in-law, son-in-law, brother-in-law, daughter-in-law, or sister-in-law.

28821. (a) A licensee shall not provide financial or managerial assistance to, or for the benefit of, any person to the detriment of a small business firm or smaller business firm, the licensee, its shareholders, or partners. Unless a licensee obtains a prior written exemption from the commissioner for special instances in which providing financial assistance may further the purposes of this division despite presenting a conflict of interest, a licensee shall not directly or indirectly do any of the following:

(1) Provide financial assistance to any of the licensee’s associates.

(2) Provide financial assistance to an associate of another licensee, if one of the licensee’s associates has received or will receive any direct or indirect financial assistance or a commitment from that licensee or a third licensee, including financial assistance or commitments received under any understanding, agreement, or cross dealing, reciprocal or circular arrangement.

(3) Borrow money from any of the following:

(A) A small business firm or smaller business firm to which the licensee has provided financial assistance.

(B) An officer, director, or owner of at least a 10-percent equity interest in the business.

(C) A close relative of a person described in subparagraph (B).

(4) Provide financial assistance to a small business firm or smaller business firm to discharge an obligation to a licensee’s associate or to make other funds available to pay the obligation, except if the obligation is to an associate lending institution and is a line of credit or other obligation incurred in the normal course of business.

(5) Provide financial assistance to a small business firm or smaller business firm for the purpose of purchasing property from a licensee’s associate.

(b) Without the commissioner’s prior written approval, a licensee’s associates shall not, directly or indirectly, do either of the following:

(1) Borrow money from any person described in paragraph (3) of subdivision (a).

(2) Receive from a small business firm or smaller business firm any compensation in connection with any financial assistance a licensee provides or anything of value for procuring, attempting to procure, or influencing a licensee’s action with respect to that financial assistance.

(c) (1) Without the commissioner's prior written approval, a licensee shall not provide financial assistance to any business in which the licensee's associate has either a voting equity interest, or total equity interests, including potential interests, of at least 5 percent.

(2) If a licensee and its associate provide financial assistance to the same small business firm or smaller business firm, whether at the same time or different times, a licensee shall demonstrate to the commissioner's satisfaction that the terms and conditions are, or were, fair and equitable to the licensee, taking into account any differences in the timing of each party's financial transactions.

(3) Financial assistance that meets either of the following criteria is exempt from the prior approval requirement in paragraph (1) and shall be presumed to be fair and equitable to the licensee for the purposes of paragraph (2):

(A) The licensee's associate is a lending institution that is providing financing under a credit facility in order to meet the operational needs of a small business firm or smaller business firm, and the terms of that financing are usual and customary.

(B) The licensee's associate invests in the small business firm or smaller business firm on the same terms and conditions and at the same time as the licensee.

(d) To protect a licensee's investment, a licensee may designate an associate to serve as an officer, director, or other participant in the management of a small business firm or smaller business firm. The licensee shall identify this associate in the licensee's records maintained and made available for the commissioner's review. Without the commissioner's prior written approval, the associate shall not do any of the following:

(1) Have any other direct or indirect financial interest in the small business firm or smaller business firm that exceeds, or has the potential to exceed, 5 percent of the firm's equity.

(2) Have served for more than 30 days as an officer, director, or other participant in the management of the small business firm or smaller business firm before the licensee provided the financial assistance.

(3) Receive any income or anything of value from the small business firm or smaller business firm unless it is for the licensee's benefit, with the exception of director's fees, expenses, and distributions based upon the associate's ownership interest in the small business firm or smaller business firm.