

AMENDED IN ASSEMBLY MAY 8, 1996

CALIFORNIA LEGISLATURE—1995–96 REGULAR SESSION

**ASSEMBLY BILL**

**No. 3061**

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**Introduced by Assembly Member Weggeland**

February 23, 1996

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An act to amend Sections 403, 25116, 25117, and 31125 of, and to add Sections 31105, 31106, and 31107 to, the Corporations Code, relating to corporations.

LEGISLATIVE COUNSEL'S DIGEST

AB 3061, as amended, Weggeland. Corporations: securities.

Existing law, the General Corporation Law, provides that when provided in the articles of incorporation, a corporation may issue shares convertible into any class or series under certain conditions.

This bill would provide that, in addition, the articles may provide for the issuance of shares which are convertible if the corporation is a "listed corporation," as defined, both at the time of the original issuance of the convertible shares and at the time of the conversion, as specified.

Existing law, the Corporate Securities Act of 1968, provides that it is unlawful for any person to offer or sell in this state any security in an issuer transaction, as specified, unless the sale is qualified or exempted. Existing law provides that certain evidences of indebtedness and its purchasers are exempt from state usury laws if the evidence of indebtedness is issued in compliance with specific provisions.

This bill would make ~~this provision~~ *the usury exemption* applicable to an evidence of indebtedness, ~~whether or not it constitutes a “security” under applicable federal or state securities laws issued in accordance with those provisions regardless of whether a court determines that it is a security.~~

Existing law, the Franchise Investment Law, provides that it is unlawful for any person to offer or sell in this state any franchise unless the offer has been registered or exempted. Existing law exempts from certain provisions of the act, the offer and sale of a franchise if the franchisor meets specified requirements.

This bill would also exempt, subject to specified conditions, any offer, sale, or other transfer of a franchise to a nonresident under specified conditions, or to certain experienced franchisees, any offer, but not the sale, by a franchisor of a franchise, while an application for renewal or amendment is pending, as specified, and any modification of a franchise agreement with an existing franchisee of a franchisor, as specified.

Vote: majority. Appropriation: no. Fiscal committee: no. State-mandated local program: no.

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

1 SECTION 1. Section 403 of the Corporations Code is  
2 amended to read:

3 403. (a) When so provided in the articles, a  
4 corporation may issue shares convertible within the time  
5 or upon the happening of one or more specified events  
6 and upon the terms and conditions that are stated in the  
7 articles if any of the following conditions apply:

8 (1) At the option of the holder or automatically upon  
9 either the vote of at least a majority of the outstanding  
10 shares of the class or series to be converted or upon the  
11 happening of one or more specified events, into shares of  
12 any class or series.

13 (2) If it is a corporation which has a license or franchise  
14 from a governmental agency to conduct its business or a  
15 member corporation of a national securities exchange  
16 registered under the United States Securities Exchange



1 Act of 1934, the license, franchise or membership of which  
2 is conditioned upon some or all of the holders of its stock  
3 possessing prescribed qualifications, to the extent  
4 necessary to prevent the loss of such license, franchise or  
5 membership or to reinstate it, at the option of the  
6 corporation, into shares of any class or series or into any  
7 other security of the corporation.

8 (3) If the corporation is a “listed corporation” as  
9 defined in subdivision (d) of Section 301.5, both at the  
10 time of the original issuance of the convertible shares and  
11 at the time of the conversion, at the option of the  
12 corporation into shares of any class or series or into any  
13 other security of the corporation, provided that any such  
14 securities received upon conversion are traded on a stock  
15 exchange or market system referred to in subdivision (d)  
16 of Section 301.5.

17 (b) Unless otherwise provided in the articles, a  
18 corporation may issue its debt securities convertible into  
19 other debt securities or into shares of the corporation  
20 within such time or upon the happening of one or more  
21 specified events and upon such terms and conditions as  
22 are fixed by the board.

23 ~~SEC. 2. Section 25116 of the Corporations Code is~~  
24 ~~amended to read:~~

25 ~~25116. An evidence of indebtedness, whether or not~~  
26 ~~constituting a “security” under applicable federal or state~~  
27 ~~securities laws, issued pursuant to a qualification under~~  
28 ~~this chapter or Chapter 3 (commencing with Section~~  
29 ~~25120), and its purchaser, shall be exempt from the usury~~  
30 ~~provisions of the Constitution, subject to compliance by~~  
31 ~~the issuer and purchaser with the terms and~~  
32 ~~requirements that may be imposed by the commissioner~~  
33 ~~as a condition of the qualification. This section creates and~~  
34 ~~authorizes a class of persons pursuant to Section 1 of~~  
35 ~~Article XV of the Constitution.~~

36 ~~SEC. 3. Section 25117 of the Corporations Code is~~  
37 ~~amended to read:~~

38 ~~25117. (a) An evidence of indebtedness, whether or~~  
39 ~~not constituting a “security” under applicable federal or~~  
40 ~~state securities laws, and the purchasers thereof, shall be~~



1 exempt from the usury provisions of Section 1 of Article  
2 XV of the California Constitution if (1) the evidence of  
3 indebtedness is rated or provisionally rated by Standard  
4 & Poor's Corporation as AAA, AA, A, BBB, or investment  
5 grade commercial paper, or by Moody's Investors  
6 Service, Inc. as Aaa, Aa, A, Baa, or investment grade  
7 commercial paper, including any such ratings with "+"  
8 or "-" designation or other variations that occur within  
9 these ratings, or has a rating or a provisional rating by  
10 another nationally recognized rating agency or system,  
11 which rating and agency or system have been certified by  
12 rule or order of the commissioner, or (2) the issuer  
13 thereof either (A) has any security listed or approved for  
14 listing upon notice of issuance on a national securities  
15 exchange or designated or approved for designation upon  
16 notice of issuance as a national market system security on  
17 an interdealer quotation system by the National  
18 Association of Securities Dealers, if the exchange or  
19 interdealer quotation system has been certified by the  
20 commissioner, pursuant to subdivision (e) of Section  
21 25100, or (B) meets each of the following requirements:

22 (i) The issuer is a corporation which is subject to  
23 Section 13 of the Securities Exchange Act of 1934.

24 (ii) The issuer had total shareholders' equity of at least  
25 one million dollars (\$1,000,000) at the end of its most  
26 recent fiscal year, and had consolidated net income, after  
27 all charges, including taxes and extraordinary losses, and  
28 excluding extraordinary gains, of at least five hundred  
29 thousand dollars (\$500,000) for three of its last four fiscal  
30 years, including its most recent fiscal year. The  
31 determination of total shareholders' equity and net  
32 income shall be determined in conformity with generally  
33 accepted accounting principles applicable to that fiscal  
34 year or years, on a consolidated basis, or (3) the evidence  
35 of indebtedness is issued by any corporation all of the  
36 outstanding shares of which are owned by an issuer which  
37 meets the requirements of subparagraph (A) or (B) of  
38 paragraph (2).



1 ~~(b) This section creates and authorizes a class of~~  
2 ~~persons pursuant to Section 1 of Article XV of the~~  
3 ~~California Constitution.~~

4 *SEC. 2. Section 25116 of the Corporations Code is*  
5 *amended to read:*

6 25116. An evidence of indebtedness issued pursuant  
7 to a qualification under this chapter or Chapter 3  
8 (commencing with Section 25120), and its purchaser,  
9 shall be exempt from the usury provisions of the  
10 Constitution, subject to compliance by the issuer and  
11 purchaser with the terms and requirements that may be  
12 imposed by the commissioner as a condition of the  
13 qualification. This section creates and authorizes a class of  
14 persons pursuant to Section 1 of Article XV of the  
15 Constitution.

16 *Any evidence of indebtedness issued in compliance*  
17 *with this section shall be entitled to the benefits of the*  
18 *usury exemption contained in this section regardless of*  
19 *whether the evidence of indebtedness is determined by*  
20 *a court to be a security.*

21 *SEC. 3. Section 25117 of the Corporations Code is*  
22 *amended to read:*

23 25117. (a) An evidence of indebtedness, and the  
24 purchasers thereof, shall be exempt from the usury  
25 provisions of Section 1 of Article XV of the California  
26 Constitution if (1) the evidence of indebtedness is rated  
27 or provisionally rated by Standard & Poor's Corporation  
28 as AAA, AA, A, BBB, or investment grade commercial  
29 paper, or by Moody's Investors Service, Inc. as Aaa, Aa, A,  
30 Baa, or investment grade commercial paper, including  
31 any such ratings with "+" or "-" designation or other  
32 variations that occur within these ratings, or has a rating  
33 or a provisional rating by another nationally recognized  
34 rating agency or system, which rating and agency or  
35 system have been certified by rule or order of the  
36 commissioner, or (2) the issuer thereof either (A) has any  
37 security listed or approved for listing upon notice of  
38 issuance on a national securities exchange or designated  
39 or approved for designation upon notice of issuance as a  
40 national market system security on an interdealer



1 quotation system by the National Association of Securities  
 2 Dealers, if the exchange or interdealer quotation system  
 3 has been certified by the commissioner, pursuant to  
 4 subdivision (o) of Section 25100, or (B) meets each of the  
 5 following requirements:

6 (i) The issuer is a corporation which is subject to  
 7 Section 13 of the Securities Exchange Act of 1934.

8 (ii) The issuer had total shareholders' equity of at least  
 9 one million dollars (\$1,000,000) at the end of its most  
 10 recent fiscal year, and had consolidated net income, after  
 11 all charges, including taxes and extraordinary losses, and  
 12 excluding extraordinary gains, of at least five hundred  
 13 thousand dollars (\$500,000) for three of its last four fiscal  
 14 years, including its most recent fiscal year. The  
 15 determination of total shareholders' equity and net  
 16 income shall be determined in conformity with generally  
 17 accepted accounting principles applicable to that fiscal  
 18 year or years, on a consolidated basis, or (3) the evidence  
 19 of indebtedness is issued by any corporation all of the  
 20 outstanding shares of which are owned by an issuer which  
 21 meets the requirements of subparagraph (A) or (B) of  
 22 paragraph (2).

23 (b) This section creates and authorizes a class of  
 24 persons pursuant to Section 1 of Article XV of the  
 25 California Constitution.

26 (c) *Any evidence of indebtedness issued in*  
 27 *compliance with this section shall be entitled to the*  
 28 *benefits of the usury exemption contained in this section*  
 29 *regardless of whether the evidence of indebtedness is*  
 30 *determined by a court to be a security.*

31 SEC. 4. Section 31105 is added to the Corporations  
 32 Code, to read:

33 31105. Any offer, sale, or other transfer of a franchise,  
 34 or any interest in a franchise, to a resident of another state  
 35 or any territory or foreign country, shall be exempted  
 36 from the provisions of Chapter 2 (commencing with  
 37 Section 31110) of this part, if all locations from which  
 38 sales, leases or other transactions between the franchised  
 39 business and its customers are made, or goods or services  
 40 are distributed, are physically located outside this state.



1 SEC. 5. Section 31106 is added to the Corporations  
2 Code, to read:

3 31106. There shall be exempted from the provisions of  
4 Chapter 2 (commencing with Section 31110) of this part,  
5 any offer, sale, or other transfer of a franchise or any  
6 interest therein if any of the following conditions apply:

7 (a) The prospective franchisee, or one or more of the  
8 prospective franchisee's shareholders who has owned at  
9 least a 50 percent interest in the prospective franchisee's  
10 business for at least 24 months, or an officer, director,  
11 partner, member, or managing agent of the franchisee,  
12 has at least 24 months' experience operating a business  
13 offering products or services substantially similar to those  
14 offered by the franchise business.

15 (b) The prospective franchisee, or one or more of the  
16 prospective franchisee's shareholders who has owned at  
17 least a 50 percent interest in the prospective franchisee's  
18 business for at least 24 months, or an officer, director,  
19 partner, member, or managing agent of the franchisee, is  
20 or has been within 60 days prior to the sale or other  
21 transfer an officer, director, partner, member, managing  
22 agent, or shareholder of the franchisor for at least 12  
23 months.

24 (c) The offer, sale, or other transfer is of an additional  
25 franchise to a present franchisee of the franchisor, or to  
26 an entity, one or more of the officers, directors, partners,  
27 members, managing agents or shareholders of which is an  
28 existing franchisee of the franchisor; provided that, in  
29 either case, for 24 months or more the franchisee, or the  
30 qualifying person, has been engaged in a business offering  
31 products or services substantially similar to those to be  
32 offered by the franchise being sold.

33 SEC. 6. Section 31107 is added to the Corporations  
34 Code, to read:

35 31107. There shall be exempted from the provisions of  
36 Chapter 2 (commencing with Section 31110) of this part,  
37 any offer (but not the sale) by a franchisor of a franchise  
38 while an application for renewal or amendment is  
39 pending if the prospective franchisee receives all of the  
40 following:

1 (a) The offering circular and its exhibits as filed with  
2 the commissioner with the application for renewal or  
3 amendment.

4 (b) A written statement from the franchisor that (1)  
5 the filing has been made but is not effective, (2) the  
6 information in the offering circular and exhibits has not  
7 been reviewed by the commissioner, and (3) the  
8 franchisor will deliver to the prospective franchisee an  
9 effective offering circular and exhibits at least 10 business  
10 days prior to execution by the prospective franchisee of  
11 a binding agreement or payment of any consideration to  
12 the franchisor, or any person affiliated with the  
13 franchisor, whichever occurs first, showing all material  
14 changes from the offering circular and exhibits received  
15 by the prospective franchisee.

16 (c) The offering circular and exhibits in accordance  
17 with paragraph (3) of subdivision (b) of this section.

18 SEC. 7. Section 31125 of the Corporations Code is  
19 amended to read:

20 31125. (a) An application for registration of a  
21 material modification of an existing franchise or of  
22 existing franchises shall be in such form and contain such  
23 information as the commissioner may by rule prescribe,  
24 and shall be accompanied by a proposed disclosure form  
25 as specified in subdivision (b). Such an application may  
26 be included with an application pursuant to Section 31111  
27 or 31121.

28 (b) Except as provided in subdivision (c), it is  
29 unlawful to solicit the agreement of a franchisee to a  
30 proposed material modification of an existing franchise  
31 without first delivering to the franchisee a written  
32 disclosure, in a form and containing such information as  
33 the commissioner may by rule or order require,  
34 identifying the proposed modification, either five  
35 business days prior to the execution of any binding  
36 agreement by the franchisee to such modification or  
37 containing a statement that the franchisee may, by  
38 written notice mailed or delivered to the franchisor or a  
39 specified agent of the franchisor within not less than five



1 business days following the execution of such agreement,  
2 rescind such agreement to the material modification.

3 (c) Any modification of a franchise agreement with an  
4 existing franchisee of a franchisor shall be exempted from  
5 the provisions of Chapter 2 (commencing with Section  
6 31110) of this part, if all of the following occur:

7 (1) The modification is in connection with the  
8 resolution of a bona fide dispute between the franchisor  
9 and the franchisee or the resolution of a franchisee  
10 default.

11 (2) The franchisee receives the complete written  
12 modification at least five business days prior to the  
13 execution of a binding agreement; provided (A) the  
14 agreement is not executed within 12 months after the  
15 date of the franchise agreement, and (B) the  
16 modification does not waive any right of the franchisee  
17 under the California Franchise Relations Act (Chapter  
18 5.5 (commencing with Section 20000) of Division 8 of the  
19 Business and Professions Code), but the modification may  
20 include a general release of all known and unknown  
21 claims by a party to the modification.

22 (3) The modification is not applied on a franchise  
23 systemwide basis at or about the time the modification  
24 becomes a binding agreement.

