

Date of Hearing: August 29, 2013

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Roger Dickinson, Chair

AB 1255 (Pan) – As Amended: March 18, 2013

SUBJECT: Corporations: consumer cooperatives.

SUMMARY: Expands the Consumer Cooperative Corporation Law to allow consumer cooperatives to include in the articles of incorporations provisions related to preferred, nonvoting shares. Specifically, this bill:

- 1) Provides that if expressed in the articles of incorporation that a consumer cooperative can set forth, the classes of preferred, nonvoting shares, if any, and whether the directors may set the number, the series, and the rights, preferences, privileges, restrictions, and conditions attaching to each class.

EXISTING LAW

- 1) Establishes the California Consumer Cooperative Law under Corporations Code, Section 12200 through 12704.

- 2) Requires consumer cooperative corporations to set forth the following in their articles of incorporation:

- a) The name of the corporation;

- b) The following statement:

“This corporation is a cooperative corporation organized under the Consumer Cooperative Corporation Law. The purpose of this corporation is to engage in any lawful act or activity for which a corporation may be organized under such law.”

- c) The name and street address in this state of the corporation’s initial agent for service of process;

- d) The initial street address of the corporation;

- e) The initial mailing address of the corporation, if different from the initial street address; and,

- f) Whether the voting power or the proprietary interests of the members are equal or unequal. If the voting power or proprietary interests of the members are unequal, the articles shall state either (i) the general rule or rules by which the voting power and proprietary interests of the members shall be determined or (ii) that such rule or rules shall be prescribed in the corporation’s bylaws. Equal voting power means voting power apportioned on the basis of one vote for each member. Equal proprietary rights means property rights apportioned on the basis of one proprietary unit for each member.

[Corporations Code, Section 12310]

- 3) Allows consumer cooperative cooperation's to set forth any or all of the following provisions which become effective when expressly provided in the articles:
- i) A provision limiting the duration of the corporation's existence to a specified date.
 - ii) A provision providing for the distribution of the remaining assets of the corporation, after payment or adequate provision for all of its debts and liabilities, to a charitable trust.
- a) Nothing contained in (3) shall affect the enforceability, as between the parties thereto, of any lawful agreement not otherwise contrary to public policy.
- b) The articles of incorporation may set forth any or all of the following provisions:
- i) The names and addresses of the persons appointed to act as initial directors.
 - ii) Provisions concerning the transfer of memberships.
 - iii) The classes of members, if any, and if there are two or more classes, the rights, privileges, preferences, restrictions and conditions attaching to each class.
 - iv) Any other provision, not in conflict with law, for the management of the activities and for the conduct of the affairs of the corporation, including any provision which is required or permitted by this part to be stated in the bylaws.
 - v) A provision conferring upon members the right to determine the consideration for which memberships shall be issued. (Corporations Code, Section 12313)

FISCAL EFFECT: None.

COMMENTS:

BACKGROUND:

CO-OP:

Simply put, a cooperative is a locally-owned business owned and managed by its members. The structure is to pool resources to satisfy a common need while providing goods and services as economically and efficiently as possible. Owners can have a voice in what is sold to them, as well as in the overall organization of their particular co-op. Owners get the most buying power for their money and the money stays in the community, contributing to its economic strength.

There are roughly 30,000 consumer cooperatives in the United States employing more than two million and bringing in \$654 billion in revenue. There are co-ops that sell bicycles, furniture, camping equipment, appliances, carpeting, clothing, crafts and books. There are cooperative wholesalers, like those in the grocery, natural foods and hardware businesses. There are cooperatives that disseminate news and cooperatives for artists. There are cooperative electric and telephone utilities. There are thousands of farm co-ops, along with co-ops that provide

financing to those farm co-ops. There are subscriber-owned cable TV systems and parent-run day-care centers. There are cooperatively organized employee-owned companies, cooperative purchasing groups for fast food franchises, and various kinds of cooperative housing. There are co-ops that provide health care, such as health maintenance organizations and community health clinics. There are cooperative insurance companies. There are cooperative food stores, food buying clubs and discount warehouses. There are even cooperative funeral societies. The first cooperative was established in 1844.

The Consumer Cooperative Corporation Law also known as the co-op law, became effective as of January 1, 1984, and applies to all co-ops incorporating under it as well as (with certain limited exceptions) to those co-ops incorporated under the repealed pre-1984 law related to co-ops. Generally, the “new” co-op law represents a synthesis of provisions from the former co-op statutes and the current Nonprofit Mutual Benefit Corporation Law, in addition to some completely new provisions.

While co-ops incorporated prior to 1984 are not required to amend their articles of incorporation to take into account current co-op law, those same co-ops may find at least some of their bylaw provisions now in conflict with co-op law. Where there is a conflict, co-op law generally supersedes the contrary bylaw provisions for acts, transactions, etc., occurring after 1984. Also, many co-ops have relatively brief bylaws that do not deal at all with certain corporate “housekeeping” matters (e.g., how to properly “notice” a meeting or retain unclaimed member equity interests). Such gaps in the bylaws may well lead to legally improper actions (or omissions) by a co-op.

Cooperatives incorporating under the California Consumer Cooperative Corporation Law are not formed under the “nonprofit” statutes of the California Corporations Code. Similarly, it is virtually impossible for co-ops incorporated under the co-op law to attain tax-exempt status, mainly due to the fact that coops are established to further the mutual benefit of their members, not the general public.

California statute specifies that co-ops are democratically controlled and are not organized to make a profit for themselves, as such, or for their members, as such, but primarily for their members as patrons. This is important to note because it may be questioned whether what this bill proposes falls in line with the premise of a co-op. Each member of a cooperative, no matter how many shares or memberships she or he has purchased, is generally entitled to only one vote. The primary objective of a cooperative is to provide benefits to its members, rather than a return on members’ capital investment.

Cooperatives are not required to obtain a “permit” from the Department of Corporations for the sale of memberships or shares up to \$300 per member, co-ops may issue unlimited shares of stock (or memberships) to any single member to help generate capital. Under California law, co-ops have to file their articles of incorporation with the Secretary of State (SOS).

A co-op may amend its articles of incorporation in any way so long as the articles, as amended, contain only those provisions that would be lawful as of the time the provisions are filed with the SOS. Although co-op law mandates certain provisions in a co-op's articles, these provisions do not have to be adopted by a co-op that was incorporated before the current co-op law went into effect.

NEED FOR THE BILL:

AB 1255 amends the code section pertaining to what a consumer cooperative may lay out in their articles of corporation. While the changes made in 1984 helped, it caused cooperatives established pre-1984 and post-1984 to be regulated differently.

According to the author, AB 1255 is needed to "eliminate confusion about the law and to enable Consumer Cooperatives to self-finance through the issuance of non-voting, preferred shares to their members." The author goes on to state, "Modern consumer cooperatives need the ability to self-finance through the sale and issuance of preferred non-voting to its member. Modern consumer cooperatives need a uniform statutory scheme, which does not discriminate between cooperatives formed before or after 1984 in its application."

California Consumer Cooperatives would like the ability to issue non-voting, preferred shares to their members for the purpose of self-financing improvements and expansions. These Cooperatives' ability to self-finance has been denied by the SOS based on confusion with how the SOS's Office interprets the Consumer Cooperative Statute. In addition, Consumer Cooperatives incorporated before 1984 and after 1984 are governed by different rules in regards to issuing preferred shares which creates further confusions.

The post 1984 changes to the Consumer Cooperative Law have made it more difficult for cooperatives to self-finance through the sale and issuance of preferred non-voting shares to their members. This is because, while cooperatives routinely separate voting rights from proprietary rights, non-cooperative businesses keep ownership interests and voting rights linked together by a voting structure which votes ownership units. Virtually all consumer cooperatives are governed by a one-member, one-vote structure, regardless of the level of investment, or ownership units a particular member has in a cooperative.

QUESTIONS:

- 1) Currently, are co-ops denied/rejected by the SOS based solely on a CCC trying to amend their articles of incorporation to issue preferred, nonvoting shares?
- 2) Pre-1984, it is implied that CCCs are allowed to issue nonvoting shares, at that time was it implied or expressed in statute? In any case, why when the law became effective in 1984, did the statute not explicitly allow for the ability to issue preferred nonvoting shares?
- 3) Why is the issue being raised now, when the statute has not explicitly allowed for this for almost 30 years?
- 4) Why would a co-op want to issue nonvoting shares which is a bigger risk to the co-op and its members rather than taking out a loan from a bank or credit union?
- 5) How many co-ops have been granted this authority in California and how many have been denied? In addition, do other states allow co-ops to issue nonvoting shares?
- 6) Could a co-op offer these preferred, nonvoting shares to non-members?

- 7) What happens if a member purchases nonvoting shares but then does not renew their membership, making them no longer a member?

REGISTERED SUPPORT / OPPOSITION:

Support

BriarPatch Community Market
Chico Natural Foods Cooperative
Co-opportunity Consumers Cooperative
Davis Food Co-op
National Cooperative Grocers Association
Ocean Beach People's Food Co-op
Quincy Natural Foods Co-op
Sacramento Natural Foods Cooperative, Inc.
Twin Pines Cooperative Foundation
Ukiah Natural Foods Co-op

Opposition

None on file.

Analysis Prepared by: Kathleen O'Malley / B. & F. / (916) 319-3081