

Date of Hearing: April 29, 2013

ASSEMBLY COMMITTEE ON BANKING AND FINANCE

Roger Dickinson, Chair

AB 434 (Hagman) – As Introduced: February 15, 2013

SUBJECT: Preferred shares: rights and preferences distributions.

SUMMARY: Provides clarity to the California Corporations Code by cleaning up references to old code sections previously repealed and altered in 2011.

EXISTING LAW

- 1) Establishes the Corporations Code to provide the fundamental terms and provisions for the governance of corporations. Corporations Code Sections 400-423 relate to shares and share certificates. Corporations Code Sections 500-511 relate to dividends and requisition of shares.
- 2) Provides the rights, preferences, privileges, and restrictions granted to or imposed upon a class or series of preferred shares the designation of which includes either the word “preferred” or the word “preference” may:
 - a) Provision requiring a vote of a specified percentage or proportion of the outstanding shares of the class or series that is less than a majority of the class or series to approve any corporate action, except where the vote of a majority or greater proportion of the class or series is required by this division, regardless of restrictions or limitations on the voting rights thereof.
 - b) Provide that a corporation may voluntarily wind up and dissolve only upon the vote of a specified percentage (which shall not exceed $66\frac{2}{3}$ percent) of such class or series.
 - c) Provide that Section 502 or 503 not apply in whole or in part with respect to distributions on shares junior to the class or series. (Corporations Code, Section 402.5)
- 3) Provides that neither a corporation nor any of its subsidiaries shall make any distribution to the corporation’s shareholders unless the board of directors has determined in good faith either of the following:
 - a) The amount of retained earnings of the corporation immediately prior to the distribution equals or exceeds the sum of the amount of the proposed distribution plus the preferential dividends arrears amount.
 - b) Immediately after the distribution, the value of the corporation’s assets would equal or exceed the sum of its total liabilities plus the preferential rights amount. (Corporations Code, Section 500)
- 4) Defines "preferential dividends arrears amount" as an amount of cumulative dividends in arrears on all shares having a preference with respect to payment of dividends over the class or series to which the applicable distribution is being made, provided that if the articles of incorporation provide that a distribution can be made without regard to preferential dividends arrears amount, then the preferential dividends arrears amount shall be zero. (Corporations Code, Section 500)

- 5) Defines "preferential rights amount" as the amount that would be needed if the corporation were to be dissolved at the time of the distribution to satisfy the preferential rights, including accrued but unpaid dividends, of other shareholders upon dissolution that are superior to the rights of the shareholders receiving the distribution, provided that if the articles of incorporation provide that a distribution can be made without regard to any preferential rights, then the preferential rights amount shall be zero. (Corporations Code, Section 500)

FISCAL EFFECT: None.

COMMENTS:

AB 434 is a clean-up measure to AB 571 (Hagman) signed into law in 2011. AB 571 updated sections of the Corporations Code governing the issues of dividends and redemption of shares by California Corporations. AB 571 repealed Corporations Code 502 and amended section 503 to address a completely different matter than it did before. However, both section 502 and the pre-revision version of section 503 are referenced in current Corporations Code 402.5. According to the sponsor, the Conference of California Bar Associations, "this creates confusion and, more importantly, could lead to the rejection by the Secretary of State's (SOS) office in regards to corporate documents submitted for filing that include incorrect language in Section 402.5 (c)."

AB 434 corrects this problem by amending Corporations Code, Section 402.5 to remove the incorrect statutory references, to substitute the appropriate reference to Section 500, and to include the terms defined in that section to allow the articles of incorporation to waive the restriction on corporate distribution to junior shares where senior shareholders preferential rights are not met in full.

In addition, according to the author, "documents filed by businesses with the SOS are being rejected because they include language with references to code sections that are now nonexistent or incorrect. AB 434 would correct the improper references in California's Corporation Code to alleviate this additional burden on our state's businesses."

PREVIOUS LEGISLATION:

AB 571 (Hagman, Chapter 203, Statutes of 2011) amended and deleted portions of the General Corporation Law concerning dividends and reacquisitions of shares.

REGISTERED SUPPORT / OPPOSITION:

Support

Conference of California bar Association (Sponsor)

Opposition

None on file.

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