

Date of Hearing: June 27, 2016

ASSEMBLY COMMITTEE ON BANKING AND FINANCE
Matthew Dababneh, Chair
SB 726 (Hueso) – As Amended June 8, 2016

AS PROPOSED TO BE AMENDED

SENATE VOTE: 35-0 (vote not relevant)

SUBJECT: Corporate securities: unlawful conduct

SUMMARY: Requires the Commissioner of the Department of Business Oversight (DBO) to adopt regulations that prohibit fraudulent and manipulative practices by persons undertaking short sales in the securities market.

EXISTING LAW:

- 1) Provides that it is unlawful for any person to offer or sell a security in this state, or to buy or offer to buy a security in this state, by means of any written or oral communication that includes an untrue statement of a material fact or omits to state a material fact necessary to make the statements made, in the light of the circumstances under which the statements were made, not misleading. [Corporations Code, Section 25401]
- 2) Provides that it is unlawful for any person to knowingly alter, destroy, mutilate, conceal, cover up, falsify, or make a false entry in any record, document, or tangible object with the intent to impede, obstruct, or influence the administration or enforcement of this division. [Corporations Code, 25404 (a)]
- 3) Provides that it is unlawful for any person to knowingly make an untrue statement to the commissioner during the course of licensing, investigation, or examination, with the intent to impede, obstruct, or influence the administration or enforcement of any provision of this division. [Corporations Code, Section 25404 (b)]
- 4) States that every person who with knowledge directly or indirectly controls and induces any person to violate any provision of this division or any rule or order thereunder shall be deemed to be in violation of that provision, rule, or order to the same extent as the controlled and induced person. [Corporations Code, Section 25403 (a)]
- 5) Any person that knowingly provides substantial assistance to another person in violation of any provision of this division or any rule or order thereunder shall be deemed to be in violation of that provision, rule, or order to the same extent as the person to whom the assistance was provided. [Corporations Code, Section 25403 (b)]
- 6) It shall be unlawful for any person directly or indirectly to do any act or thing which would be unlawful for that person to do under any provision of this division or any rule or order thereunder through or by any other person. [Corporations Code, Section 25403 (c)]

- 7) Provides that nothing in this section shall be construed to limit the power of the state to punish any person for any conduct which constitutes a crime under any other statute.
[Corporations Code, Section 25403 (d)]

FISCAL EFFECT: Unknown.

COMMENTS:

SB 726, as proposed to be amended, will require the Commissioner of DBO to establish regulations to prohibit fraudulent and manipulative practices by persons undertaking short sales in the securities market. While the suggested amendments are an improvement from the previous version of the bill, a number of questions and concerns remain.

Short-Selling

According to the Securities and Exchange Commission (SEC):

"A short sale is generally the sale of a stock you do not own (or that you will borrow for delivery). Short sellers believe the price of the stock will fall, or are seeking to hedge against potential price volatility in securities that they own.

If the price of the stock drops, short sellers buy the stock at the lower price and make a profit. If the price of the stock rises, short sellers will incur a loss. Short selling is used for many purposes, including to profit from an expected downward price movement, to provide liquidity in response to unanticipated buyer demand, or to hedge the risk of a long position in the same security or a related security."

Are short-sales legal? According to the SEC,

"Although the vast majority of short sales are legal, abusive short sale practices are illegal. For example, it is prohibited for any person to engage in a series of transactions in order to create actual or apparent active trading in a security or to depress the price of a security for the purpose of inducing the purchase or sale of the security by others. Thus, short sales effected to manipulate the price of a stock are prohibited."

Herbalife vs. Ackman

This measure is a response to "short-selling" activities that occurred surrounding the company Herbalife and an investor. For more information on this please read this article:
<http://www.wsj.com/articles/probes-of-ackman-and-herbalife-fizzle-1454111460>

Questions & Concerns:

- 1) It is unclear what "short sales" means as it is not defined in the bill or existing law.
- 2) It is unclear what "securities market" means as it is not defined in the bill or existing law.

- 3) It is unclear what problem exists in California that the bill is trying to address. Is this a statewide issue or an issue that should be addressed nationally?

REGISTERED SUPPORT / OPPOSITION:

Support

Bell Gardens Chamber of Commerce
California – Nevada Conference of Operating Engineers
California Legislative Conference of the Plumbing, Heating and Piping Industry
California State Council of Laborers
Herbalife Nutrition
International Brotherhood of Electrical Workers Local Union 569 San Diego
Los Angeles Area Chamber of Commerce
National Electrical Contractors Association
Regional Hispanic Chamber of Commerce
Regional Hispanic Institute
Reinforcing Ironworkers Local #416
San Gabriel Valley Economic Partnership
San Gabriel Valley Regional Chamber of Commerce
South Gate Chamber of Commerce
State Building and Construction Trades Council, AFL-CIO
The Greater Huntington Park Area Chamber of Commerce
The Latino Coalition (TLC)

Opposition

California Teamsters Public Affairs Council
Consumer Watchdog
UNITE-HERE

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