STATE OF CALIFORNIA
BUSINESS, TRANSPORTATION AND HOUSING AGENCY
DEPARTMENT OF CORPORATIONS

Pete Wilson
Governor

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Commissioner of Corporations

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TRANSACTIONS INVOLVING THE OFFER OR SALE OF SECURITIES PURSUANT TO THE NEW EXEMPTION FOR COMPENSATORY STOCK OPTION AND PURCHASE PLANS; REVISION OF THE SMALL CORPORATE OFFERING EXEMPTION; OTHER CHANGES TO THE CORPORATE SECURITIES LAW OF 1968

In General.

Under existing provisions of the Corporate Securities Law of 1968 ("CSL"), the offer and sale of a security in this state must be first reviewed and approved by the Commissioner of Corporations, unless an exemption from the review and approval process is available under the CSL or the rules adopted by the Commissioner. Both the CSL and the Commissioner's rules contain many exemptions from this review and approval process for securities, issuers, and transactions meeting specified conditions.

Senate Bill 261 (Chapter 41, Statutes 1996) establishes a new exemption from the Commissioner's review and approval process and, among other things, amends other provisions of the CSL to make it easier for small companies to raise capital in this state. This bill passed the Legislature as an urgency measure and became law on May 6, 1996, shortly after it was signed by the Governor.

Specifically, SB 261: (1) adds subdivision (o) to Corporations Code Section 25102 to establish a new exemption for the offer or sale of securities pursuant to a stock option plan or agreement or a stock purchase plan or agreement provided the security is exempt from registration under the Securities Act of 1933 pursuant to Rule 701 (17 C.F.R. 230.701) of the Securities and Exchange Commission ("SEC"), the terms of the stock purchase or option plan agreement comply with specified rules of the Commissioner, and a notice of transaction is filed with the Commissioner; (2) amends Corporations Code Section 25111 to provide that Regulation A offerings are to be processed by the Commissioner on a basis similar to SEC offerings that will be fully-registered under the Securities Act of 1933 and filed by "coordination" with the

Commissioner for review and approval; (3) amends Corporations Code Section 25113(b)(2), the Small Corporate Offering Registration ("SCOR") provisions of the CSL, to authorize the issuance of preferred stock, reduce the initial minimum offering price to $2 per share from $5 per share, and allow for the majority (instead of all) of the board of directors to review and sign the SCOR application and disclosure document; (4) amends Corporations Code Section 25103(h) to establish a new exemption for exchanges incident to merger, consolidation, and sale of asset transactions if the transaction would have been exempt pursuant to Corporations Code Section 25102(f) had the exchange involved the issuance of a security subject to qualification pursuant to Corporations Code Section 25110 and where the transaction meets specified requirements; (5) amends Corporations Code Section 25102(h) to repeal the requirement of the restriction on transfer legend, requires that a purchaser of stock must represent that he or she is purchasing the securities for his or her own account and not to immediately resell to other investors, and provides that the restriction on transfer legend imposed on all outstanding stock previously issued under the small offering exemption is removed by operation of law.

Corporations Code Section 25102(o).

Several questions have arisen with respect to the interpretation and application of the new exemption under Corporations Code Section 25102(o). As a result of reviewing the questions posed by some of the language in Corporations Code Section 25102(o), the following reflects the Department of Corporations' interpretations.

1. An issuer that has already obtained a qualification for the issuance of securities under its stock option plan or stock purchase plan, or both a stock option and stock purchase plan under a "flexible" plan, may use the exemption from qualification afforded by Corporations Code Section 25102(o) for a prospective amendment to the already existing plan; provided, all of the requirements of the new exemption are met, including the payment of the required fee under the new exemption as calculated as provided for in Corporations Code Section 25608(y).

2. The payment of the fee required by the exemption afforded by Corporations Code Section 25102(o) is based upon the transaction for which the exemption is claimed. That is, the new exemption is a "transaction" exemption, not a "securities" exemption. Thus, amendments to a stock option or stock purchase plan that would require qualification, including an amendment to increase the number of options or shares that may be issued under the plan, requires the filing of a new notice and payment of an additional fee based on the value of the underlying securities which are the subject of the claim of exemption.

3. The exemption under Corporations Code Section 25102(o) requires, among other things, that the transaction meet the requirements of specified rules adopted by the Commissioner. While the Commissioner has proposed amendments to these rules, and the Commissioner will, upon request waive the requirements of existing rules when the issuer demonstrates that the issuance will meet the requirements of the rules as proposed to be amended, the Commissioner cannot accord the same treatment in the case of the exemption from qualification afforded by Corporations Code Section 25102(o). The new exemption is a statutory exemption; the Commissioner has no authority to waive provisions of the statute other than through rulemaking. As a consequence, an issuer seeking to rely on the exemption afforded by Corporations Code Section 25102(o) must meet the requirements of the rules as adopted and in effect, and not as proposed to be amended.

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