

# STATEMENT OF POLICY REGARDING PREFERRED STOCK

*Adopted April 27, 1997; Amended March 31, 2008*

## I. INTRODUCTION

This statement of policy applies to all applications to register by coordination or by qualification.

## II. DEFINITIONS

This statement of policy uses the following terms defined in the North American Administrators Association, Inc., *Statement of Policy Regarding Corporate Securities Definitions*:

- Adjusted Net Earnings
- Administrator
- Cash Analysis
- Disclosure Document
- Equity Securities
- Independent Director
- Promoter

## III. GROUNDS FOR DENIAL OF SECURITIES REGISTRATION RELATING TO PAYMENT ABILITY

The Administrator may deny the offer or sale of preferred stock based on the issuer's Adjusted Net Earnings or a Cash Analysis. In either case, the issuer must have enough cash to pay the dividend, if any, on the preferred stock being offered whether or not declared.

- A. The Administrator may deny the offer and sale of preferred stock if either the issuer's Adjusted Net Earnings for its last fiscal year or the issuer's Adjusted Net Earnings for its last three fiscal years were insufficient to pay the issuer's:
  - 1. Fixed charges;
  - 2. Preferred stock dividends, whether or not accrued; and
  - 3. The redemption requirements, if any, of the preferred stock being offered to investors.
  
- B. The Administrator may deny the offer or sale of preferred stock unless the issuer's Statement of Cash Flows shows that "Net Cash Provided by Operating Activities" was positive for the issuer's last fiscal year. The Administrator may require the issuer to submit a financial statement that is presented in conformity with generally accepted accounting principles and demonstrates that the issuer had an average positive "Net Cash Provided by Operating Activities" for the last three fiscal years. [*See editor's Note at end regarding the Administrator's use of sections III.A or III.B.*]

#### **IV. EXEMPTION FROM DENIAL OF SECURITIES REGISTRATION RELATING TO PAYMENT ABILITY**

Section III does not apply to public offerings of:

- A. Convertible preferred stock that ranks ahead of any convertible debt relating to payment of dividends, interest, and liquidation proceeds; or
- B. Preferred stock that is or may be legally or beneficially, directly or indirectly, owned by Promoters.

#### **V. GROUNDS FOR DENIAL OF SECURITIES REGISTRATION RELATING TO SHAREHOLDER APPROVAL**

The Administrator may deny the offer or sale of Equity Securities if the issuer's articles of incorporation authorize the board of directors to issue preferred stock without a vote by the common shareholders.

#### **VI. EXEMPTION FROM DENIAL OF SECURITIES REGISTRATION RELATING TO SHAREHOLDER APPROVAL**

Section V does not apply if:

- A. The Disclosure Document states that the issuer will not offer preferred stock to Promoters except on the same terms as it is offered to all other existing or new shareholders; or
- B. A majority of the issuer's Independent Directors that do not have an interest in the transaction:
  - 1. Approve any offering of preferred stock; and
  - 2. Have access, at the issuer's expense, to issuer's counsel or independent counsel.

#### **VII. DISCLOSURE REQUIREMENTS**

The issuer's Disclosure Document relating to an offering of preferred stock must disclose:

- A. Whether dividends on the preferred stock are cumulative;
- B. The risks of failure to declare or pay dividends on the preferred stock; and
- C. The equity characteristics of any convertible preferred stock being offered to investors.

*Note: The Administrator may adopt section III in its entirety. Alternatively, the Administrator may adopt either section III.A or section III.B.*