

RESIDENCY REQUIREMENT FOR REGISTRATION EXEMPTIONS WHEN ISSUING SECURITIES

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House Bill 4305 as enrolled
Public Act 141 of 2017
Sponsor: Rep. Bronna Kahle
Committee: Commerce and Trade
Complete to 5-10-17

Analysis available at
<http://www.legislature.mi.gov>

SUMMARY:

Public Act 264 of 2013 and Public Act 355 of 2014¹ amended the Uniform Securities Act to allow for specific exemptions from regulation for securities when certain criteria are met, and to create the Michigan Investment Market. Collectively, these bills addressed and provided for what is known as *investment crowdfunding*. (See [Background](#) for a description of crowdfunding.)

House Bill 4305 would amend the Uniform Securities Act (MCL 451.2202a and 541.2451) to provide a technical update to that legislation by referencing new federal securities rules for use in determining whether a Michigan company is exempt from certain state filing and registration requirements when issuing securities. (See [Background](#) for a description of those rules.)

(The Uniform Securities Act (2002) is based on a model act from the Uniform Law Commission of the National Conference of Commissioners on Uniform State Laws (NCCUSL) and is designed to coordinate federal and state securities legislation. The purpose of such regulation is to prevent fraudulent sales of securities to investors.)

Specifically, the bill would do the following (**bold** added to show changes described in the bill):

- Add that the issuer must be "**a resident of this state under SEC rule 147, 17 CFR 230.147, or SEC Rule 147A, 17CFR 230.147a**" in order to be exempt from state-level filing and registration requirements for a sale of security.
- Add that the transaction must meet "**the federal exemption for intrastate offerings under 15 USC 77 and SEC Rule 147A, 17 CFR 230.147A**", or an existing standard.
- Add that the provisions of SEC rule 147, 17 CFR 230.147, "**or SEC rule 147A, 17 CFR 230.147A, as applicable,**" apply in determining the residence of an offeree or purchaser that is a corporation, partnership, trust, or other form of business organization.
- Reduce from 9 months to **6 months** the time period in which an investment agreement is void if the purchaser sells the security to a person that is not a resident of this state.
- Add a reference to "**Subsection (E) of SEC rule 147A, 17 CFR 230.147A(E)**" in a disclosure statement that must be provided to prospective purchasers.

¹ See summaries <http://www.legislature.mi.gov/documents/2013-2014/billanalysis/House/pdf/2013-HLA-4996-B589A29C.pdf> and <http://www.legislature.mi.gov/documents/2013-2014/billanalysis/House/pdf/2013-HLA-5273-E6A2B0E8.pdf>

- Redefine "Intrastate offering exemption" to specify that the exemption is from section 202a or any other exemption from federal securities regulation under 15 USC 77c(a)(11) and SEC rule 147, 17 CFR 230.147, "**15 USC 77E and SEC rule 147A, 17 CFR 230.147A.**"

BACKGROUND:

As noted earlier, PA 264 of 2013 and PA 355 of 2014 amended Michigan's Uniform Securities Act to address what is known as *investment crowdfunding*.

According to the U.S. Securities and Exchange Commission (SEC):²

Crowdfunding is a term used to describe an evolving method of raising money through the Internet. For several years, this funding method has been used to generate financial support for such things as artistic endeavors like films and music recordings, typically through small individual contributions from a large number of people.

While crowdfunding can be used to raise funds for many things, it generally has not been used as a means to offer and sell securities. That is because offering a share of the financial returns or profits from business activities could trigger the application of the federal securities laws, and an offer or sale of securities must be registered with the SEC unless an exemption is available.

Congress created an exemption to permit securities-based crowdfunding when it passed the JOBS Act [. . .]. Among other things, the JOBS Act was intended to help alleviate the funding gap and accompanying regulatory concerns faced by startups and small businesses in connection with raising capital in relatively low dollar amounts.

*Title III of the JOBS Act established the foundation for a regulatory structure that would permit these entities to use crowdfunding, and **directed the SEC to write rules implementing the exemption.** It also created a new entity – a funding portal – to allow Internet-based platforms or intermediaries to facilitate the offer and sale of securities without having to register with the SEC as brokers. Together these measures were intended to facilitate capital raising by small businesses while providing significant investor protections. **(Emphasis added)***

HB 4305 updates the Uniform Securities Act to reference these rules (see below).

The U.S. Securities and Exchange Commission (SEC) adopted amendments to Rule 147 and adopted the new Rule 147A at its October 26, 2016 meeting. The changes would take effect 150 days after publication in the Federal Register.

According to the SEC's website, Rule 147, 147A, and the amendments serve the following purpose:

The adoption of new Rule 147A and the amendments to Securities Act Rule 147 would update and modernize the existing intrastate offering framework that permits companies to raise money from investors within their state without concurrently registering the offers and sales at the federal level.

² <https://www.sec.gov/news/press-release/2013-227> "SEC Issues Proposal on Crowdfunding"

Amended Rule 147 would remain a safe harbor under Section 3(a)(11) of the Securities Act, so that issuers may continue to use the rule for securities offerings relying on current state law exemptions. New Rule 147A would be substantially identical to Rule 147 except that it would allow offers to be accessible to out-of-state residents and for companies to be incorporated or organized out-of-state.

Both new Rule 147A and amended Rule 147 would include the following provisions:

- A requirement that the issuer has its "principal place of business" in-state and satisfies at least one "doing business" requirement that would demonstrate the in-state nature of the issuer's business*
- A new "reasonable belief" standard for issuers to rely on in determining the residence of the purchaser at the time of the sale of securities*
- A requirement that issuers obtain a written representation from each purchaser as to residency*
- A limit on resales to persons residing within the state or territory of the offering for a period of six months from the date of the sale by the issuer to the purchaser*
- An integration safe harbor that would include any prior offers or sales of securities by the issuer made under another provision, as well as certain subsequent offers or sales of securities by the issuer occurring after the completion of the offering*
- Legend requirements to offerees and purchasers about the limits on resales³*

FISCAL IMPACT:

House Bill 4305 would not have a significant impact on the Department of Licensing and Regulatory Affairs or on other units of state and local government.

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■ This analysis was prepared by nonpartisan House Fiscal Agency staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.

³ <https://www.sec.gov/news/pressrelease/2016-226.html> "SEC Adopts Final Rules to Facilitate Intrastate and Regional Securities Offerings"