

HOUSE BILL 1365

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By: **Delegates Schuh, Barve, and Costa**

Introduced and read first time: February 10, 2014

Assigned to: Rules and Executive Nominations

A BILL ENTITLED

AN ACT concerning

Corporations and Associations – Securities – Maryland Small Business Funding Act

FOR the purpose of exempting a certain security issued to a resident of the State by a certain business entity from certain registration and filing requirements under certain circumstances; exempting a certain Web site that is used to facilitate the sale of a certain security from certain registration and filing requirements under certain circumstances; requiring the Division of Securities within the Office of the Attorney General to inspect and review certain Web sites under certain circumstances; requiring a certain issuer, before using a Web site to offer to sell a security, to provide to the Division and the operator of the Web site certain documentation; requiring a certain issuer to obtain certain documentation from certain purchasers of securities; requiring the operator of a certain Web site to provide to the Division certain documentation and information under certain circumstances; requiring a certain issuer and the operator of a certain Web site to maintain certain records and provide access to certain records under certain circumstances; requiring a financial institution to hold a certain payment for the purchase of a security under certain circumstances; requiring the financial institution to notify the Division of the receipt of certain payments and provide certain information to the Division; providing that certain information is confidential and is deemed to be a trade secret; authorizing a certain notice to be submitted to the Division in writing or in electronic form; requiring the notice to contain certain information and include copies of certain documents; requiring an issuer of certain securities to provide a quarterly report to certain purchasers; requiring the report to be sent in a certain manner within a certain time period; requiring the report to include certain information; prohibiting the issuer from charging a fee for the production or provision of the report; providing for the application of certain provisions of this Act; defining certain terms; making certain conforming changes; and generally relating to securities and registration and filing exemptions.

EXPLANATION: CAPITALS INDICATE MATTER ADDED TO EXISTING LAW.

[Brackets] indicate matter deleted from existing law.



BY repealing and reenacting, without amendments,
 Article – Corporations and Associations
 Section 11–101(a), (d), (k), (m), (p), and (r)
 Annotated Code of Maryland
 (2007 Replacement Volume and 2013 Supplement)

BY repealing and reenacting, with amendments,
 Article – Corporations and Associations
 Section 11–205, 11–401(a), and 11–501
 Annotated Code of Maryland
 (2007 Replacement Volume and 2013 Supplement)

BY adding to
 Article – Corporations and Associations
 Section 11–901 through 11–907 to be under the new subtitle “Subtitle 9. Filing
 and Registration Exemptions for Small Business Funding”
 Annotated Code of Maryland
 (2007 Replacement Volume and 2013 Supplement)

SECTION 1. BE IT ENACTED BY THE GENERAL ASSEMBLY OF MARYLAND, That the Laws of Maryland read as follows:

Article – Corporations and Associations

11–101.

(a) In this title, unless the context requires otherwise, the following words have the meanings indicated.

(d) “Commissioner” means the Securities Commissioner of the Division of Securities.

(k) “Issuer” means any person who issues or proposes to issue a security, except that:

(1) With respect to certificates of deposit, voting–trust certificates, or collateral–trust certificates or with respect to certificates of interest or shares in an unincorporated investment trust not having a board of directors or persons performing similar functions or of the fixed, restricted management, or unit type, the term “issuer” means the person performing the acts and assuming the duties of depositor or manager under the provisions of the trust or other agreement or instrument under which the security is issued; and

(2) With respect to certificates of interest or participation in oil, gas, or mining titles or leases or in payments out of production under the titles or leases, there is not considered to be any “issuer”.

(m) “Offer” or “offer to sell”, except as provided in § 11–102(a) of this subtitle, includes every attempt or offer to dispose of or solicitation of an offer to buy, a security or interest in a security for value.

(p) “Sale” or “sell”, except as provided in § 11–102(a) of this subtitle, includes every contract of sale of, contract to sell, or disposition of a security or interest in a security for value.

- (r) (1) “Security” means any:
- (i) Note;
 - (ii) Stock;
 - (iii) Treasury stock;
 - (iv) Bond;
 - (v) Debenture;
 - (vi) Evidence of indebtedness;
 - (vii) Certificate of interest or participation in any profit–sharing agreement;
 - (viii) Collateral–trust certificate;
 - (ix) Preorganization certificate or subscription;
 - (x) Transferable share;
 - (xi) Investment contract;
 - (xii) Voting–trust certificate;
 - (xiii) Certificate of deposit for a security;
 - (xiv) Certificate of interest or participation in an oil, gas, or mining title or lease or in payments out of production under the title or lease;
 - (xv) In general, any interest or instrument commonly known as a “security”; or
 - (xvi) Certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase any of the preceding.

(2) “Security” does not include any insurance or endowment policy or annuity contract under which an insurance company promises to pay money either in a lump sum, periodically for life, or some other specified period.

11-205.

The Commissioner by rule or order may require the filing of any prospectus, pamphlet, circular, form letter, advertisement, or other sales literature or advertising communication, whether communicated in hard copy, electronic means, or otherwise, addressed or intended for distribution to prospective investors, including clients or prospective clients of an investment adviser, unless the security or transaction is exempted by Subtitle 6 **OR SUBTITLE 9** of this title or the security is a federal covered security or the transaction is with respect to a federal covered security.

11-401.

(a) A person may not transact business in this State as a broker-dealer or agent unless the person is registered under this subtitle **OR EXEMPTED UNDER SUBTITLE 9 OF THIS TITLE**.

11-501.

A person may not offer or sell any security in this State unless:

- (1) The security is registered under this title;
- (2) The security or transaction is exempted under Subtitle 6 **OR SUBTITLE 9** of this title; or
- (3) The security is a federal covered security.

SUBTITLE 9. FILING AND REGISTRATION EXEMPTIONS FOR SMALL BUSINESS FUNDING.

11-901.

(A) IN THIS SUBTITLE THE FOLLOWING WORDS HAVE THE MEANINGS INDICATED.

(B) “BUSINESS ENTITY” MEANS A CORPORATION, PROFESSIONAL CORPORATION, PARTNERSHIP, LIMITED LIABILITY COMPANY, LIMITED LIABILITY PARTNERSHIP, OR ANY OTHER LEGAL ENTITY FORMED UNDER THE LAWS OF THE STATE.

(C) "FINANCIAL INSTITUTION" HAS THE MEANING STATED IN § 1-101 OF THE FINANCIAL INSTITUTIONS ARTICLE.

11-902.

THIS SUBTITLE APPLIES TO ANY SECURITY ISSUED TO A RESIDENT OF THE STATE BY A BUSINESS ENTITY.

11-903.

SUBJECT TO § 11-905 OF THIS SUBTITLE, A SECURITY IS EXEMPTED FROM §§ 11-205 AND 11-501 OF THIS TITLE IF:

(1) THE ISSUER, EITHER BEFORE OR AS A RESULT OF THE OFFERING, IS NOT:

(I) AN INVESTMENT COMPANY AS DEFINED IN § 3 OF THE INVESTMENT COMPANY ACT OF 1940; OR

(II) SUBJECT TO THE REPORTING REQUIREMENTS OF § 13 OR § 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934;

(2) THE ISSUER ENTERS INTO AN ESCROW AGREEMENT WITH A FINANCIAL INSTITUTION LOCATED IN THE STATE THAT SPECIFIES THAT:

(I) THE FINANCIAL INSTITUTION WILL RELEASE ALL OFFERING PROCEEDS TO THE ISSUER ONLY WHEN THE AGGREGATE CAPITAL RAISED IS AT LEAST THE MINIMUM TARGET OFFERING AMOUNT SPECIFIED IN THE ISSUER'S BUSINESS PLAN; AND

(II) A PURCHASER MAY CANCEL THE PURCHASER'S COMMITMENT TO PURCHASE A SECURITY IF THE TARGET OFFERING AMOUNT IS NOT RAISED BEFORE THE DATE SPECIFIED IN THE DISCLOSURE STATEMENT;

(3) THE TOTAL OF ALL CASH AND CONSIDERATION PAID FOR THE SECURITY DOES NOT EXCEED:

(I) IF THE ISSUER HAS NOT UNDERGONE OR PROVIDED DOCUMENTATION OF A FINANCIAL AUDIT THAT APPLIED GENERALLY ACCEPTED ACCOUNTING PRINCIPLES WITHIN THE 12-MONTH PERIOD IMMEDIATELY PRECEDING THE FIRST OFFER OR SALE OF A SECURITY UNDER THIS SUBTITLE, \$1,000,000, INCLUDING THE AGGREGATE AMOUNT THE ISSUER RECEIVED FOR ALL SALES OF SECURITIES WITHIN THE 12-MONTH PERIOD IMMEDIATELY

PRECEDING THE FIRST OFFER OR SALE OF A SECURITY UNDER THIS SUBTITLE;
OR

(II) IF THE ISSUER HAS UNDERGONE AND PROVIDED DOCUMENTATION OF A FINANCIAL AUDIT THAT APPLIED GENERALLY ACCEPTED ACCOUNTING PRINCIPLES WITHIN THE 12-MONTH PERIOD IMMEDIATELY PRECEDING THE FIRST OFFER OR SALE OF A SECURITY UNDER THIS SUBTITLE, \$2,000,000, INCLUDING THE AGGREGATE AMOUNT THE ISSUER RECEIVED FOR ALL SALES OF SECURITIES WITHIN THE 12-MONTH PERIOD IMMEDIATELY PRECEDING THE FIRST OFFER OR SALE OF A SECURITY UNDER THIS SUBTITLE;

(4) THE ISSUER HAS NOT ACCEPTED MORE THAN \$2,000 FROM ANY SINGLE PURCHASER WHO IS NOT AN ACCREDITED INVESTOR AS DEFINED IN 17 C.F.R. § 230.501;

(5) NOT MORE THAN 15 DAYS AFTER THE SALE OF A SECURITY UNDER THIS SUBTITLE, THE ISSUER SUBMITS TO THE DIVISION THE NOTICE REQUIRED UNDER § 11-906 OF THIS SUBTITLE; AND

(6) THE ISSUER:

(I) INFORMS EACH PURCHASER THAT THE SECURITIES BEING OFFERED:

1. HAVE NOT BEEN REGISTERED UNDER FEDERAL OR STATE SECURITIES LAWS; AND

2. ARE SUBJECT TO LIMITATIONS ON RESALE; AND

(II) DISPLAYS A NOTICE CONSPICUOUSLY ON THE COVER PAGE OF THE DISCLOSURE DOCUMENT FOR THE SALE OF A SECURITY THAT INCLUDES THE FOLLOWING STATEMENT:

“IN MAKING INVESTMENT DECISIONS, INVESTORS MUST RELY ON THEIR OWN EXAMINATION OF THE ISSUER AND THE TERMS OF THE OFFERING, INCLUDING THE MERITS AND RISKS INVOLVED. THESE SECURITIES HAVE NOT BEEN RECOMMENDED BY ANY FEDERAL OR STATE SECURITIES COMMISSION OR REGULATORY AUTHORITY. FURTHERMORE, THE FOREGOING AUTHORITIES HAVE NOT CONFIRMED THE ACCURACY OR DETERMINED THE ADEQUACY OF THIS DOCUMENT. MAKING ANY REPRESENTATION TO THE CONTRARY IS A CRIMINAL OFFENSE.

THESE SECURITIES ARE SUBJECT TO RESTRICTIONS ON TRANSFERABILITY AND RESALE AND MAY NOT BE TRANSFERRED OR RESOLD EXCEPT AS PERMITTED UNDER SEC RULE 147, 17 C.F.R. § 230.147(E) AND APPLICABLE STATE SECURITIES LAWS. INVESTORS SHOULD BE AWARE THAT THEY WILL BE REQUIRED TO BEAR THE FINANCIAL RISKS OF THIS INVESTMENT FOR AN INDEFINITE PERIOD OF TIME.”.

11-904.

SUBJECT TO § 11-905 OF THIS SUBTITLE, A WEB SITE THAT IS USED TO FACILITATE THE SALE OF A SECURITY UNDER THIS SUBTITLE IS EXEMPTED FROM § 11-401 OF THIS TITLE IF THE WEB SITE AND THE OPERATOR OF THE WEB SITE DO NOT:

- (1) OFFER INVESTMENT ADVICE OR RECOMMENDATIONS;
- (2) SOLICIT PURCHASES, SALES, OR OFFERS TO BUY THE SECURITIES OFFERED OR DISPLAYED ON THE WEB SITE;
- (3) COMPENSATE EMPLOYEES, AGENTS, OR OTHER PERSONS:
 - (I) FOR THE SOLICITATION OF THE SALE OF SECURITIES DISPLAYED OR REFERENCED ON THE WEB SITE; OR
 - (II) BASED ON THE SALE OF SECURITIES DISPLAYED OR REFERENCED ON THE WEB SITE;
- (4) HOLD, MANAGE, POSSESS, OR OTHERWISE HANDLE PURCHASER FUNDS OR SECURITIES; AND
- (5) ENGAGE IN OTHER ACTIVITIES THAT THE COMMISSIONER FINDS INAPPROPRIATE.

11-905.

- (A) THIS SECTION APPLIES A TRANSACTION IN WHICH A WEB SITE IS USED TO FACILITATE THE SALE OF A SECURITY UNDER THIS SUBTITLE.
- (B) THE DIVISION SHALL INSPECT AND REVIEW EACH WEB SITE BEING USED TO FACILITATE THE SALE OF A SECURITY UNDER THIS SUBTITLE.
- (C) AN ISSUER:

(1) BEFORE USING A WEB SITE TO OFFER TO SELL A SECURITY, SHALL PROVIDE TO THE DIVISION AND THE OPERATOR OF THE WEB SITE USED TO FACILITATE THE SALE DOCUMENTATION THAT THE ISSUER IS A BUSINESS ENTITY AUTHORIZED TO DO BUSINESS UNDER THE LAWS OF THE STATE; AND

(2) SHALL OBTAIN FROM EACH PURCHASER OF A SECURITY DOCUMENTATION THAT THE PURCHASER IS A RESIDENT OF MARYLAND AND, IF APPLICABLE, AN ACCREDITED INVESTOR.

(D) THE OPERATOR OF A WEB SITE USED TO FACILITATE THE SALE OF SECURITIES UNDER THIS SUBTITLE SHALL PROVIDE TO THE DIVISION:

(1) DOCUMENTATION THAT:

(I) THE OPERATOR IS A BUSINESS ENTITY;

(II) THE OPERATOR IS AUTHORIZED TO DO BUSINESS IN THE STATE; AND

(III) THE WEB SITE IS BEING USED TO OFFER AND SELL SECURITIES IN ACCORDANCE WITH THIS SUBTITLE;

(2) THE NAME, ADDRESS, AND TELEPHONE NUMBER OF THE OPERATOR; AND

(3) THE NAME, ADDRESS, AND TELEPHONE NUMBER OF THE ISSUER OF THE SECURITIES.

(E) THE ISSUER AND THE OPERATOR OF THE WEB SITE SHALL:

(1) MAINTAIN RECORDS OF THE OFFERS AND SALES OF SECURITIES FACILITATED THROUGH THE WEB SITE; AND

(2) ON REQUEST BY THE DIVISION, PROVIDE ACCESS TO THE RECORDS RELATING TO THE OFFERS AND SALES OF SECURITIES FACILITATED THROUGH THE WEB SITE.

(F) (1) A FINANCIAL INSTITUTION SHALL HOLD EACH PAYMENT FOR THE PURCHASE OF A SECURITY FACILITATED THROUGH A WEB SITE.

(2) ON RECEIPT OF A PAYMENT FOR A SECURITY, THE FINANCIAL INSTITUTION SHALL:

(I) NOTIFY THE DIVISION OF THE RECEIPT OF THE PAYMENT; AND

(II) PROVIDE TO THE DIVISION THE NAME AND ADDRESS OF THE PURCHASER OF THE SECURITY.

(3) ANY INFORMATION RETAINED BY A FINANCIAL INSTITUTION OR THE DIVISION UNDER THIS SUBSECTION IS CONFIDENTIAL AND IS DEEMED TO BE A TRADE SECRET.

11-906.

(A) A NOTICE TO THE DIVISION UNDER § 11-903(5) OF THIS SUBTITLE MAY BE SUBMITTED IN WRITING OR ELECTRONIC FORM.

(B) THE NOTICE SHALL CONTAIN:

(1) A STATEMENT THAT THE ISSUER WILL BE CONDUCTING AN OFFERING UNDER THIS SUBTITLE;

(2) A DESCRIPTION OF THE BUSINESS ENTITY ISSUING THE SECURITY, INCLUDING THE STRUCTURE, HISTORY, AND BUSINESS PLAN OF THE BUSINESS ENTITY;

(3) THE INTENDED USE OF THE OFFERING PROCEEDS;

(4) THE NAMES AND TITLES OF THE OFFICERS OF THE BUSINESS ENTITY;

(5) THE TERMS AND CONDITIONS OF THE SECURITIES BEING OFFERED;

(6) THE TERMS AND CONDITIONS OF EACH OUTSTANDING SECURITY OF THE BUSINESS ENTITY;

(7) THE NAME OF EACH PERSON WHO WILL BE OFFERING AND SELLING THE SECURITIES, INCLUDING THE NAME OF EACH OPERATOR OF A WEB SITE THAT WILL BE USED TO FACILITATE THE SALE OF THE SECURITIES;

(8) A DESCRIPTION OF ANY LEGAL PROCEEDINGS INVOLVING THE BUSINESS ENTITY; AND

(9) ANY OTHER MATERIAL INFORMATION THAT MAY MAKE ANY REPRESENTATIONS ABOUT THE BUSINESS ENTITY OR SALE MISLEADING OR INCOMPLETE.

(C) THE NOTICE SHALL INCLUDE A COPY OF:

(1) THE DISCLOSURE STATEMENT THAT THE ISSUER WILL PROVIDE TO INVESTORS IN CONNECTION WITH THE OFFERING; AND

(2) THE ESCROW AGREEMENT BETWEEN THE ISSUER AND A FINANCIAL INSTITUTION LOCATED IN THE STATE IN WHICH PAYMENTS FOR THE SECURITIES SOLD IN THE OFFERING WILL BE DEPOSITED.

11-907.

(A) AN ISSUER OF A SECURITY UNDER THIS SUBTITLE SHALL PROVIDE A QUARTERLY REPORT TO THE PURCHASER OF THE SECURITY.

(B) A REPORT UNDER THIS SECTION SHALL BE SENT BY ELECTRONIC MAIL OR FIRST-CLASS MAIL TO THE PURCHASER NO MORE THAN 45 DAYS AFTER THE END OF A REPORTING QUARTER.

(C) THE REPORT SHALL INCLUDE:

(1) THE COMPENSATION OF EACH DIRECTOR AND EXECUTIVE OFFICER OF THE ISSUER FOR THE LAST YEAR, INCLUDING CASH COMPENSATION EARNED SINCE THE PREVIOUS QUARTERLY REPORT; AND

(2) AN ANALYSIS OF THE BUSINESS OPERATION AND FINANCIAL CONDITION OF THE ISSUER THAT IS WRITTEN BY MANAGEMENT.

(D) THE ISSUER MAY NOT CHARGE A FEE TO THE PURCHASER FOR THE PRODUCTION OR PROVISION OF THE REPORT.

SECTION 2. AND BE IT FURTHER ENACTED, That this Act shall take effect October 1, 2014.