Assessment of Public Comment on Proposed Changes to 13 NYCRR 10

The below represents the substance of comments sent to the Department of Law (The "Department") in response to its proposal to amend 13 NYCRR 10 as summarized in the April 15, 2020 edition of the New York State Register (the "Part 10 Proposal"). Below each comment the Department has responded. The final rule adopting the Part 10 Proposal is referred to herein as the "Adopted Rule."

1. Comment: One commenter urged the Department to accept the proposition that an issuer that chooses to take advantage of federal exemptions from registration and files Form D, represents a claim that the issuer of the offering is not offering or selling "to the public" under the Martin Act. The commenter referenced a 2002 paper by the Business Law Section of the New York State Bar Association (the "NYSBA Paper") that concluded that private placements and other unregistered securities offerings pursuant to section 4(a)(2) of the Securities Act of 1933 and Rule 506 were not offered "to the public" under the Martin Act and that no fees or filings are required The commenter noted that many practitioners have followed the NYSBA Paper's opinion.

   Response: The Department hereby expresses its interpretation of GBL § 359-e(1)(a) with respect to offers "to the public" and rejects the NYSBA Paper's conclusions and the notion that filings pursuant to the Part 10 Proposal are not required. Under the Martin Act, private placements and other offerings to limited amounts of offerees may qualify as offerings "to the public." The Department's interpretation of New York law is supported by GBL § 359-e, GBL § 359-f, and the Court of Appeals' decision in *People v. Landes*, 84 N.Y.2d 655 (1994). [1]First, GBL § 359-e explicitly identifies and excludes the offers or sales of only certain types of "private placement(s)" (e.g. offers of sale made solely to a bank) from its definition of dealer. *See* GBL § 359-e(1)(a). It naturally follows that other, unidentified private placements are captured under the definition of dealer. The Department views offering or selling these private placements (including, but not limited to, those offered to natural persons) as constituting dealer activity. Second, GBL § 359-f buttresses this conclusion. It explicitly provides for discretionary exemptions for dealers who are engaged in the business of offering to limited offerees, exemptions that would only be necessary if these offerings constituted dealer activity under GBL § 359-e. *See* GBL § 359-f(2)(d). Finally, the Court of Appeals in *Landes* described the factors to be used to determine whether a dealer is offering securities privately or to the public. These factors are: "the number of offerees and their relationship to each other and to the issuer, the number of units offered, the size of the offering, and the manner of the offering." *Landes* at 661. These factors do not rely on the

[1] The NYSBA Paper also argues that the legislative history behind certain amendments to GBL § 359-e suggest that private placements and limited offerings must be interpreted in line with SEC determinations regarding the thresholds for exemption from securities registration. The NYSBA Paper suggests that Governor Rockefeller intended to subordinate the Department's interpretation of its laws to determinations made by a federal agency. The Department disagrees because the NYSBA Paper misinterprets and misconstrues concerns by the securities industry and statements made by Governor Rockefeller at the time of implementation of amendments to GBL § 359-e, circa 1959.

dealer's own determination of which securities exemption to claim. Notably, in *Landes* the Court of Appeals held that an offering sold to just twelve people was made to the public. See *Landes* at 663.

While New York understands that the SEC has deemed that certain transactions do "not involv[e] a public offering within the meaning of section 4(a)(2) of the [33] Act"[2] for the purpose of federal registration requirements, that determination does not define the phrase "to the public" as used in GBL § 359-e(1)(a).

Moreover, the SEC itself has acknowledged that, as a factual matter, offerings it considers not "a public offering" are routinely offered to the public at large and may pose a danger to investors:

> As an individual investor, you may be offered an opportunity to invest in an unregistered offering. You may be told that you are being given an exclusive opportunity. The opportunity may come from a broker, acquaintance, friend or relative. You may have seen an advertisement regarding the opportunity. The securities involved may be, among other things, common or preferred stock, limited partnerships interests, a membership interest in a limited liability company, or an investment product such as a note or bond. Keep in mind that private placements can be very risky and any investment may be difficult, if not virtually impossible to sell…Issuers relying on the Rule 506(c) exemption can generally advertise their offerings. As a result, **you may see an investment opportunity advertised through the Internet, social media, seminars, print, or radio or television broadcast… Private placements may be pitched as a unique opportunity being offered to only a handful of investors, including you….** Generally, most securities that you acquire in a private placement will be *restricted securities*…. This issue primarily affects the sale of restricted securities in private companies**. Information about a private company is not typically available to the public, and a private company may not provide information to you…**[3]

The NYSBA Paper acknowledges that New York State could "impose notice filing requirements substantially similar to those required by Rule 503 and Form D." This is exactly what is being done for Federal Covered Regulation D Securities Dealers in the Part 10 Proposal. Practitioners should take note. [4]

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[2] 17 CFR 230.506

[3] https://www.sec.gov/oiea/investor-alerts-bulletins/ib_privateplacements.html last visited November 17, 2020. (Emphasis added.)

[4] The NYSBA Paper further posits that certain dealers selling securities through a broker need not file with the Department. The NYSBA Paper again misconstrues legislative history and builds on prior insubstantial arguments to conclude that dealers of all kinds of securities who sell some shares through a broker, are excluded from the filing requirements of GBL § 359-e. While not raised by the commenter, the Department takes this opportunity to specifically reject these assertions and to reaffirm its longstanding position that only persons solely selling the entirety of a security issuance on a "firm commitment" basis are covered by the following exclusionary language in GBL § 359-e (1)(a)(i): "selling, offering for sale, purchasing or offering to purchase any security or securities to, from or through any bank, dealer or broker, or to or from any syndicate, corporation, or group formed for the specific purpose of acquiring such securities for resale to the public directly or through other syndicates or

Under the Department's interpretation of GBL 359-e(1)(a), compliance with New York's filing requirements for Federally Covered Regulation D Securities Dealers is mandatory, not voluntary. Failure to make required filings under GBL § 359-e and 13 NYCRR 10 will subject the delinquent filer to liability prescribed under the law.

2. Comment: One commenter requested that the Attorney General state that Form 99 is superseded. Another commenter's submission suggested that it understood that instead of the currently required Form 99 eligible issuers would file the Form D through the North American Association of Securities Administrators' ("NASAA") electronic filing depository system ("EFD").

   Response: The Adopted Rule effectively supersedes any requirement that Form 99 be filed by the classes of dealers defined in 10.11 (a) (3), (5) and (7). However, the Form 99 will remain available for other dealers not classified in the Proposal, wishing to notice file in New York. In particular, certain dealers filing with the Real Estate Finance Bureau will still be required to file Form 99 pursuant to the Real Estate Finance Bureau's instructions. In addition, issuers of theatrical securities may continue to file the Form 99.

3. Comment: One commenter asked the Department to clarify that the Part 10 Proposal does not apply to Real Estate Finance Bureau filings.

   Response: The Adopted Rule is only applicable to filings related to general securities offerings which shall be filed with the Investor Protection Bureau. The Adopted Rule is <u>not</u> applicable to filings with the Real Estate Finance Bureau, such as filings of securities constituted of participation interests or investments in real estate, mortgages or leases, including stocks, bonds, debentures, evidences of interest or indebtedness, limited partnership interests or other security or securities as defined in General Business Law § 352-e, when such securities consist primarily of participation interests or investments in one or more real estate ventures, including cooperative interests in realty. The Real Estate Finance Bureau may accept filings through EFD at a later date and will provide notice of any such change.

4. Comment: One commenter notes that 13 NYCRR 10.3 (d) requires the filing of an amended Form D with the Department whenever such amendment is filed with the SEC but notes that such filings are annual as opposed to the Department's quadrennial schedule. The commenter requests that the Department clarify that such annual amendments do not require payment of a fee.

   Response: The Department agrees that while such annual renewal filings must be filed with OAG through EFD, that such filings will not require any annual fee. However, any dealer continuing to offer or sell in New York after the initial four-year filing period must again pay the statutory fee for dealer registration. Additionally, any amendments to the information in

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groups..." Thus, persons offering or selling securities on a "best efforts" basis are *not* excluded from the definition of dealer under GBL § 359-e(1)(a).

the Form D, even if appearing on the annual amended filing, will constitute a supplemental filing under 10.3 or 10.4 and require payment of the $30 fee.

5. Comment: One Commenter noted that while they applauded a move to electronic payments, they urged that the Department allow for payment by physical checks in cases of hardship, as opposed to restricting all paper payments.

   Response: The Department agrees and has modified the language in 13 NYCRR 10.5 and 10.8 accordingly.

6. Comment: One commenter urged that the Department set a flat fee for filings, which the commenter believed would encourage "voluntary" filing.

   Response: The Department may ultimately propose a flat fee for such filings. However, the Department rejects the notion that filings under the Adopted Rule are submitted on a voluntary basis. Failure to timely submit a filing under 13 NYCRR 10 as amended, will constitute a violation of law. The Attorney General is authorized to seek relief under GBL § 352 *et seq* for violations of GBL § 359-e or the rules thereunder. Such remedies include, *inter alia* suspending the offer or sale of securities within New York as a result of the failure to submit any filing or fee required under law.

7. Comment: One commenter noted that EFD should be explicitly authorized as an e-payment system.

   Response: Use of EFD is clearly authorized by rules adopted under the Adopted Rule. However, the Department anticipates implementing additional e-payment systems for filings not eligible for EFD.

8. Comment: One commenter questioned whether the inclusion of Section 18(b)(4)(G) in the definition of Federal Regulation D Covered Securities in the Part 10 Proposal is necessary. The commenter highlighted that a person selling securities under 18(b)(4)(G) cannot file a Form D with the SEC, as any such sale would be a non-issuer resale transaction.

   Response: The Department has adopted this comment. As Section 18(b)(4)(G) does not apply to issuers, it has been removed from the definition of Federal Covered Regulation D Securities in the Adopted Rule.

9. Comment: One commenter expressed concern over the classification of "finder" as a type of Broker requiring an examination and registration. The commenter suggests the definition of Broker under "GBL § 359-e(1)(b) provides enough of a means of regulating the type of activity that would warrant registration and examination." The commenter expressed concern that "licensing requirements for this class of person could dampen legitimate activity." Another commenter recommended against defining "finder" as the SEC is reviewing the status of finders.

Response: Finder conduct is a subset of conduct defined under GBL § 359-e(1)(b), and thus already requires registration. Based on the comments, and in light of recent proposals by the SEC, the reference to finder has been removed from the Adopted Rule. Instead, OAG intends to issue guidance on the types of finder activity that constitute broker activity under GBL 359-e(1)(b) and any registration requirement for such finders.

10. Comment: One Commenter suggested that the Department include time for a transition period to the EFD system once EFD accepts Form NF.

    Response: The Adopted Rule been modified slightly to allow for a transition period.

11. Comment: One Commenter suggests changing 13 NYCRR 10.11(b) to clarify that the Form D filing deadline is triggered by sales within New York State.

    Response: The Department has added clarifying language in the Adopted Rule.

12. Comment: One commenter urged the Department to consider accepting a consent to service for Form D filings in the form provided on the Form D in lieu of the separate Form U-2 consent to service filed with the Department of State.

    Response: All Form D issuers using the EFD system must agree to consent to service language substantially similar to the Form U-2, which is currently accepted by the state. Thus, the Department will accept the EFD filing including the issuer's agreement to the system's consent to service language as sufficient consent to service. The Department has removed from the adopted rules the additional U-2 filing, for EFD filings only. The Department notes that nothing in this assessment of comment or the filing of a Form D, Form U-2 or other consent to service in New York, limits the operation of GBL 352-a or GBL 352-b, or any other state law.