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November 7, 2017

The Honorable Paul Ryan
Speaker
U.S. House of Representatives
Washington, DC 20515

The Honorable Nancy Pelosi
Democratic Leader
U.S. House of Representatives
Washington, DC 20515

Re: H.R. 2201 – The Micro-Offering Safe Harbor Act

Dear Speaker Ryan and Leader Pelosi:

On behalf of the North American Securities Administrators Association ("NASAA"),[1] I write to express concern and raise specific objections to certain provisions of H.R. 2201, The Micro-Offering Safe Harbor Act, which is scheduled to be considered by the House of Representatives this week. The legislation would amend securities laws in ways that could be profoundly detrimental to investors, and detract from the viability of the marketplace for offerings from new or smaller issuers that are compliant with securities law.

The Micro-Offering Safe Harbor Act amends Section 4 of the Securities Act of 1933 to create a new exemption from registration. To qualify for the exemption, an offering would have to meet certain criteria regarding the number of purchasers, their relationship to the issuer, and the amount of capital raised.[2] However, as more fully discussed below, the legislation fails to include critical investor protection measures and would preempt state regulatory authority.

State securities regulators understand the need of small businesses to efficiently raise capital and the role strong investor protection plays in facilitating this goal. Unfortunately, the changes embodied in H.R. 2201, while well intended, are ill-advised and potentially quite dangerous. For example, unregistered securities purchased under the exemption established by H.R. 2201 would not be "restricted," and could thus be sold immediately, ***exposing investors to classic ''pump and dump'' schemes***. Furthermore, NASAA is aware of no evidence to support the proposition that Congress should create a "safe harbor" to permit ***unregistered*** securities offerings to be offered and sold, including through general solicitation, regardless of investor sophistication or financial wherewithal.[3] Even as the bill stands to introduce new and totally unnecessary risk into securities markets – ***failing***

[1] The oldest international organization devoted to investor protection, the North American Securities Administrators, Inc. was organized in 1919. Its membership consists of the securities administrators in the 50 states, the District of Columbia, Canada, Mexico, Puerto Rico and the U.S. Virgin Islands. NASAA is the voice of securities agencies responsible for grass-roots investor protection and efficient capital formation.

[2] The exemption established by H.R. 2201 would be subject to the following three criteria: (1) each purchaser has a substantive pre-existing relationship with an officer or director of the issuer, or with a shareholder holding 10 percent or more of the issuer's shares; (2) there are no more than 35 purchasers of securities from the issuer in reliance on this exemption during the preceding 12 months; and (3) the aggregate amount raised by the issuer during the 12-month period preceding the transaction, including in reliance on this exemption, does not exceed $500,000.

[3] NASAA questions why an issuer would need to engage in public solicitation if it had a previously existing relationship.

__to even disqualify "bad actors" from these markets__[4] – the goal of the legislation remains unclear and its necessity is, at best, not well-established.[5] It is clear, however, from the terms of the exemption, and its failure to impose even the modicum of regulatory oversight that exists for similar "private" offerings under SEC Regulation D Rule 506, that offerings made under the new exemption are likely to be disproportionately risky and illiquid. This fact alone should be cause for concern by Congress.

Beyond stark new risks to investors, this legislation threatens to jeopardize the continued viability of established markets geared to smaller issuers, many of which operate lawfully within existing federal and state securities laws. Such markets include securities sold pursuant to SEC Rule 506, new federal exemptions established by the JOBS Act, and exemptions adopted in many states to permit intrastate crowdfunding. Without effective investor protection measures a potential effect of H.R. 2201 could be to cause investors to abandon the markets for smaller issues.

In closing, NASAA reiterates strong opposition to the preemption of state registration and notice filing authority in H.R. 2201. There is no valid basis for Congress to prevent states from making decisions about the local or regional issues that H.R. 2201 seeks to encourage. Failure to register or at the very least, to notice file with state regulators results in unknown sales, by unknown actors of unknown enterprises and result in no gatekeeper function to protect retail investors whose only source of recourse for fraudulent sales are the state securities regulators. At a minimum H.R. 2201 should:

1) Include bad actor disqualifications;
2) Establish a holding period to reduce the likelihood of "pump and dump" schemes;
3) Provide at least a notice filing with state regulators so that in the event of a fraudulent offering, state regulators can begin an investigation to try and protect retail investors;
4) Limit the sale amount to retail investors so that investors are not "encouraged" to place all their eggs in one basket; and
5) Prohibit or restrict general solicitation of what are clearly high risk securities.

Thank you for your consideration of NASAA's views. Please do not hesitate to contact me, or Michael Canning, NASAA Director of Policy & Government Affairs, at (202) 737-0900, if we may be of any additional assistance.

Sincerely,

Joseph P. Borg
NASAA President and Alabama Securities Director

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[4] Under the terms of the bill, even persons who have been barred from the securities industry, convicted or otherwise prohibited from selling securities to the general public would technically be able to sell these small unregistered offerings, without any notice to regulators that they are being sold. This creates an impossible situation for regulators attempting to protect investors.

[5] There are already various provisions at the state and federal level that small, microcap issuers can rely upon for limited offerings. For example, an issuer can raise funds under Rule 504, Section 3(a)(11) of the Securities Act of 1933 and its safe harbor Rule 147, and Section 4(a)(2) of the 1933 Act. Further, most states also have de minimus offering exemptions, allowing issuers to raise money with a limited number of purchasers through self-executing exemptions with little or no notice filing requirements. Finally, small issuers can similarly rely on federal crowdfunding rules and Regulation A.