House
Legislative
Analysis
Section

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UNIFORM SECURITIES ACT REVISIONS

House Bill 5763 as enrolled
Public Act 494 of 2000
First Analysis (1-3-01)

Sponsor: Rep. Andrew Richner
House Committee: Family and Civil Law
Senate Committee: Financial Services

THE APPARENT PROBLEM:

On October 11, 1996, President Clinton signed the National Securities Markets Improvement Act of 1996 (NSMIA), which significantly changed the federal securities laws with the intent of eliminating duplicate regulation of securities issuers and transactions by the federal and state governments. The enactment of NSMIA reduced the authority of the states to regulate portions of the securities industry, while leaving the states exclusive authority over other aspects. Under NSMIA, the states are no longer allowed to regulate the registration of "covered securities." NSMIA also changed the registration and regulation requirements for investment advisers. Investment advisers previously were required to register with the Securities and Exchange Commission (SEC) and with each state in which they offered their services. NSMIA created two kinds of advisers: those covered under federal law, who manage assets in excess of $25-30 million and must register with the SEC; and state investment advisers, who manage smaller amounts and must register with the states. States may regulate state investment advisers but are preempted from regulating federally covered advisers. However, NSMIA also allows the states to require registration of the representatives of federally covered advisers, who actually provide the investment advice, if they have a place of business in the state. Although federally covered advisers are exempt from state registration, the states retain regulatory authority over them for fraud and certain other unlawful conduct under state law. Finally, each state may require federally covered advisers to file a notice and pay a fee in order to provide services in the state.

In light of the significant changes to the federal securities laws under NSMIA, legislation has been offered to update the state's securities law to comport with those changes.

THE CONTENT OF THE BILL:

The bill would amend the Uniform Securities Act to make changes that will conform with the National Securities Markets Improvements Act of 1996 (NSMIA), which effectively preempted portions of the state's securities law.

Definitions. "Federally covered securities" would include federally-registered mutual fund shares, national exchange-listed securities, exempt securities based on offers and sales to qualified purchasers, and exempt securities based on certain transactional exemptions under the Securities Act of 1933.

"Federally covered adviser" would mean a person who is registered or required to be registered with the SEC, pursuant to section 203 of the Investment Advisers Act of 1940 or is not excluded from the definition of investment adviser under the same act. Essentially, section 203 requires investment advisers with more than $25 million of assets under management to register with the SEC and investment advisers with less than $25 million of assets under management to register with the states in which they conduct business.

General provisions. The bill would, among other things, allow the administrator to require anyone who applies for registration under the act or sells or offers to sell a security in this state to file an irrevocable consent to service of process, eliminate references to commodities and commodity contracts, and update definitions and clarify existing language. Federally covered advisers would be exempted from restrictions under the act as required by NSMIA. However, federally covered advisers could still be required to make a notice filing, consent to service of process, and pay a filing fee. The fee structures for notice filings would be simplified and all notice filers would pay the same fee. Renewal fees would be based on the issuer's estimate of its sales within the state for the coming year and would be graduated so that smaller funds pay less

than larger ones. The bill would allow the administrator to require a fidelity bond from any broker-dealer, agent, or investment adviser who is required to be registered under the act, but would remove existing provisions regarding the posting of bonds that, among other things, established procedures and specified amounts. The administrator could not require a bond from a broker-dealer who was registered under the Securities Exchange Act or an investment adviser whose principal place of business is in another state.

Securities. Under the bill, securities issued by a unit investment trust could be sold for an indefinite period of time starting on the later of the trust's effectiveness with the SEC or the administrator's receipt of a notice as prescribed by the administrator. Securities issued by an investment company, other than a unit investment trust, could be not be sold in Michigan unless the company was registered or had filed a registration statement and the administrator received a consent to service of process, a fee of $1,000, and a notice as prescribed by the administrator, which could be in the form of a copy of a federal registration statement filed with the SEC.

A notice filing would be effective for a one-year period, beginning on the administrator's receipt of the filing or the effectiveness of the offering with the SEC, whichever was later. Notice filings made after the enactment of NSMIA, but prior to the enactment of the bill's provisions, would not be made ineffective by the bill's enactment. A notice filing could be renewed for an additional year by re-filing the required documents and fee before the first year expired. A notice filing could also be terminated by filing a notice of termination, which would be effective upon receipt by the administrator.

An issuer of federally covered securities would be required to file a notice on the SEC's form "D" or another form approved by the administrator no later than 15 days after the first sale of a covered security in this state. The issuer would also be required to provide a consent to service of process and a $100 filing fee.

The administrator could also require the filing of any documents filed with the SEC regarding a federally covered security. These documents would also have to be accompanied by a $100 filing fee. The administrator could stop the offer and sale of a federally covered security (except for those under sections 18(b)(1) of the Securities Act of 1933 -- a security issued by an investment company that is registered, or that has filed a registration statement, under the Investment Company Act of 1940), if it found that it was in the public interest to do so and that the issuer had failed to comply with the filing provisions. Further, the administrator would also have the authority to waive any or all of the filing provisions.

Small company offerings. The rules regarding securities offerings by small business issuers would be extended to Canadian companies and limited liability corporations. The minimum offering price for such stock or securities would be $1 per share and the issuer could not split the security or declare a dividend for two years after the effective date of the registration if the effect would be to lower the price below $1 per share.

Financial statements in these cases would be made in accordance with generally accepted accounting principles or the Canadian equivalent. Where appropriate, statements of receipts and disbursements could be accepted instead of statements of income. Annual financial statements would have to be audited by independent certified public accountants or chartered accountants as appropriate, but interim financial statements would not have to be audited. Annual financial statements could be reviewed instead of audited in accordance with the American Institute of Certified Public Accountants or the Canadian equivalent, if all of the following were true: neither the amount of the small company offering nor the aggregate amount of all previous sales of securities by that issuer over the preceding 24 months exceeded $1 million; the issuer had not previously sold securities through an offering involving general advertising or the solicitation of prospective investors; and the issuer had not previously been required to provide audited financial statements in connection with the sale of its securities.

Investment advisers. Those investment advisers who continue to be regulated by the state would, unless the administrator decided to waive the requirement, be required to furnish their clients and prospective clients with a written disclosure statement in a form set by the administrator. The statement would have to be provided to each client or prospective client no less than 48 hours before contract is entered or at the time the contract is entered provided that the client is able to rescind the contract without penalty within five business days after he or she enters the contract. An adviser would also have to re-offer the disclosure statement to each client on an annual basis. If the client accepted the offer, the statement would have to be mailed or delivered to the client within five business days.

Registration as an investment adviser would take effect upon the order of the administrator and would expire on December 31 of that year. If the adviser failed to file an annual report before December 31, the adviser could not continue to transact business in this state as an investment adviser, broker-dealer, or agent. On the other hand, the administrator would not be able to place any record keeping or financial reporting requirements on an investment adviser that maintains its principal place of business in another state and had met the record keeping or financial reporting requirements of that state, beyond those required by the adviser's home state.

The bill would specify that federally covered advisors could act as investment advisers in this state. In addition, investment advisers who are not required to be registered under the Investment Advisers Act of 1940 would be allowed to act as an investment adviser within this state if any of the following applied: 1) The adviser's only clients in this state are other investment advisers, federally covered advisers, broker-dealers, or institutional investors. 2) The adviser has no place of business within this state and directs business communications to an existing customer whose principal residence is not within this state. 3) The adviser has no place of business in the state and during the preceding 12 months has not had more than five clients who are residents of the state, not counting those clients who are investment advisers, federally covered advisers, broker-dealers, or institutional investors.

Federally covered advisers. A federally covered adviser would not have to make a notice filing if: a) he or she is a registered broker-dealer who is not subject to conditions ordered by the administrator that prevent him or her from transacting business as an investment adviser; b) he or she is not an investment adviser; c) he or she does not have a place of business in the state and during any period of 12 consecutive months had no more than five clients in this state who are not investment companies; or d) he or she does not have a place of business in the state and his or her only clients in the state are individuals who access service through a toll-free telephone number and those services are generic in nature and are not specific to the individual.

In all other cases, before conducting business in the state, a federally covered adviser would be required to file some or all of the documents, including amendments (at the discretion of the administrator), that the federally covered adviser had to file with the SEC. The administrator could also require a consent to service of process and a fee in conjunction with the filing. Furthermore, a federally covered adviser who acquired the business of an investment adviser or another federally covered adviser, or an investment adviser who acquired the business of a federally covered adviser, would be required to make a notice filing. However, a broker-dealer who was registered under the Securities Exchange Act of 1934 could not be required to make, maintain or preserve any records or file a financial report that were not required under the Securities Exchange Act.

A notice filing would take effect upon its receipt by the administrator and would expire on December 31 of that year. A new notice filing would have to be made in subsequent years in order for the adviser to continue doing business within the state. A notice filing could be withdrawn or terminated by notifying the administrator in writing. The termination or withdrawal would be effective upon receipt.

MCL 451.501 et al.

FISCAL IMPLICATIONS:

According to the House Fiscal Agency, the bill is expected to have no fiscal impact on the state or local units of government.

ARGUMENTS:

For:

The changes made by the bill are necessary in light of the 1996 changes to federal law. The state no longer has the authority to enforce many of the current law's provisions. Almost every other state in the union has already made these changes; it is time for Michigan to catch up. The bill would create a fee structure that would not violate federal law and would still provide significant income for the state. The fees charged are intended to make the impact of the bill revenue neutral.

Analyst: W. Flory

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