ORAL ARGUMENT NOT YET SCHEDULED
Nos. 15-1149/1150 (Consolidated)

UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

MONICA J. LINDEEN, MONTANA STATE AUDITOR, *EX OFFICIO* MONTANA COMMISSIONER OF SECURITIES AND INSURANCE and WILLIAM F. GALVIN, SECRETARY OF THE COMMONWEALTH OF MASSACHUSETTS,
***Petitioners*,**

v.

SECURITIES AND EXCHANGE COMMISSION,
***Respondent*.**

On petitions for review of a final rule of the Securities and Exchange Commission

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AMICUS CURIAE BRIEF SUBMITTED BY THE NATIONAL SMALL BUSINESS ASSOCIATION

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CERTIFICATE AS TO PARTIES, RULINGS, AND RELATED CASES

Pursuant to D.C. Circuit Rules 28(a)(1) and 29(d), the undersigned counsel certifies as follows:

A. Parties and Amici

All parties, intervenors, and *amici* appearing in this Court are listed in the Brief for Petitioners and Brief for Respondent.

Amici are the National Small Business United, d/b/a National Small Business Association, North American Securities Administrators Association, Inc., current and former members of the U.S. Congress: Representative Maxine Waters, Representative Stephen Lynch, Representative Keith Ellison, Representative Michael Capuano, Representative Carolyn Maloney, Representative Niki Tsongas, Senator Ed Markey and former Representative Barney Frank, and Michael Cunningham.

B. Rulings Under Review

References to the rule at issue appear in the Brief for Petitioners.

C. Related Cases

Counsel is aware of no related cases currently pending in any other court.

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CORPORATE DISCLOSURE STATEMENT

Pursuant to Rule 26.1 of the Federal Rules of Appellate Procedure and D.C. Circuit Rule 26.1, the National Small Business United, d/b/a National Small Business Association, certifies that it is a trade association, qualified under 501(c)(6) of the Internal Revenue Code, that it does not have outstanding shares or debt securities in the hands of the public, and that it does not have a parent company. No publicly held company has a 10% or greater ownership interest in the National Small Business United, d/b/a the National Small Business Association.

/S/ Ford C. Ladd
Ford C. Ladd

GLOSSARY

Commission	U.S. Securities and Exchange Commission
GAO	U.S. Government Accountability Office
GAO Report	Factors that May Affect Trends in Regulation A Offerings, GAO-12-839 (July 2012)
JOBS Act	Jumpstart Our Business Startups Act, Pub. L. No. 112-106, 126 Stat. 306 (2012)
NASAA	North American Securities Administrators Association, Inc.
NASAA Program	NASAA's Coordinated Review Program for Regulation A Offerings
NSMIA	National Securities Markets Improvement Act, 15 U.S.C. § 77r
Regulation A	17 C.F.R. §§ 230.251-230.263
Regulation A Amendment	Amendments for Small and Additional Issues Exemptions Under the Securities Act (Regulation A), Final Rule, 80 Fed. Reg. 21,806 (Apr. 20, 2015)
1933 Act	Securities Act of 1933

STATUTES AND REGULATIONS

All applicable statutes and regulations are contained in the Brief for the Petitioners.

STATEMENT OF IDENTITY, INTEREST IN CASE, SOURCE OF AUTHORITY TO FILE, AND STATEMENT OF SEPARATE BRIEFING

The National Small Business Association and its members ("NSBA") best represent the interests of the small businesses Congress intended to benefit when passing Title IV of the JOBS Act. Our members, the NSBA, and its counsel participated in the legislative and rulemaking process that resulted in the final rule provisions now at issue. Most important, our members and other similar small businesses have a material interest in the outcome of this action because they will bear the adverse consequences of striking the preemption provisions now at issue.

The NSBA represents the national interests of over 65,000 small business members across the country, in all sectors and industries of our economy. Our average member has 17 employees, with 28% employing more than 20 workers. Most members have annual revenues that exceed $1 million, with a quarter exceeding $5 million.

Jeff Van Winkle, our Immediate Past Chair, a partner with Clark Hill, BLC, has seen the benefits and burdens imposed by our securities laws on businesses, and has testified before Congress on the JOBS Act Implementation. Ford C. Ladd represents businesses and investors, and has submitted comment to the Commission on the Regulation A Amendment, and the impact of our securities laws on businesses and investors. Mr. Ladd has led D.C. Bar seminars with Commission Staff on Regulations A and D, and the provisions now at issue.

STATEMENT OF AUTHORSHIP AND FINANCIAL CONTRIBUTIONS

Pursuant to Rule 29(c)(5) of the Federal Rules of Appellate Procedure, the National Small Business United, d/b/a National Small Business Association, certifies that: neither party's counsel authored this brief, in whole or in part; neither party, nor their counsel, contributed money that was intended to fund preparing or submitting this brief; and no person, other than the National Small Business United, d/b/a National Small Business Association, its members, and its undersigned counsel in this matter contributed money that was intended to fund this brief.

ARGUMENT

I. Section 401(b) unambiguously authorizes the Commission to preempt all Tier 2 Offerings, as demonstrated by its Legislative History

The express language in Section 401(b) of the Jumpstart Our Business Startups ("JOBS") Act is not ambiguous, and clearly authorized the Securities and Exchange Commission ("Commission") to adopt rules or regulations that could preempt State registration laws on sales to all qualified purchasers, "as defined by the Commission pursuant to paragraph (3) with respect to that purchase or sale;" JOBS Act at Sec. 401(b), where paragraph (3) [15 U.S.C. 77r(b)(3)] states:

> A security is a covered security with respect to the offer or sale of the security to qualified purchasers, as defined by the Commission by rule. In prescribing such rule, the Commission may define the term ''qualified

> purchaser'' differently with respect to different categories of securities, consistent with the public interest and the protection of investors.

Further, Congress knew that one of our nation's leading securities law experts, Professor John C. Coffee, Jr., Columbia Law School, had testified before the Senate Committee on Banking, Housing and Urban Affairs that this language gave the Commission authority to define "qualified purchaser," and that it "was unclear how the Commission will use this authority (and the Commission could preclude offerings to unsophisticated investors as the price of escaping Blue Sky regulation). S. Comm. on Banking, Housing and Urban Affairs, Examining Job Growth through Capital Formation, S. Hrg. 112-444 at 63 (12/1/2011).

Title IV of the JOBS Act was taken from H.R. 1070 that was introduced with bi-partisan support to address burdens imposed on smaller businesses in capital formation that had resulted in a declining number of public companies. Initially, H.R. 1070 was limited to creating a new class of unrestricted securities, exempt from full federal registration under Section 3(b) of the Securities Act, for offerings up to $50 million, but with enhanced disclosure requirements. *See* H.R. 1070 IH. During a hearing held by the House Financial Services sub-Committee on Capital Markets and Government Sponsored Enterprises on March 16, 2011, Dave Weld testified that the United States is losing more public companies from our listed exchanges than we are replacing with IPOs, that H.R. 1070 could help

the economy by driving "down costs for issuers by permitting the use of a simpler offering circular for the SEC's review," … "allow[ing] companies to list on the New York Stock Exchange and NASDAQ and to **avail themselves of the so-called "blue sky" exemption, thus avoiding extremely costly State-by-State filings**" … [and allowing] "testing the waters …." (Emphasis added) H.Ser. No. 112-19 (Mar. 16, 2011). This testimony alerted Members to the burdens imposed by meeting State registration requirements, after which Mr. Schweikert introduced an amendment during a Sub-Committee Markup on May 3, 2011, that added new paragraph (6) to preempt securities offered through brokers and dealers from State registration.

When H.R. 1070 was called for Markup before the full Committee on June 22, 2011, an *Amendment in the Nature of a Substitute to H.R. 1070 Offered by Mr. Schweikert* was marked as Amendment No. 1, which restated most of sub-sections (a) and (b), but removed the broker-dealer exemption from State registration in former sub-paragraph (b)(6), and, in lieu thereof, added new sub-section:

> (b) TREATMENT AS COVERED SECURITIES FOR PURPOSES OF NSMIA.-- Section 18(b)(4) of the Securities Act of 1933 (15 U.S.C. 77r(b)(4)) is amended-
>
> (1) in subparagraph (C), by striking "; or" at the end and inserting a semicolon; and
>
> (2) by redesignating subparagraph (D) as sub-paragraph (E), and inserting after subparagraph (C) the following:
>
> "(D) a rule or regulation adopted pursuant to section 3(b)(2) and such security is-
>
> "(i) offered or sold through a broker or dealer;

> "(ii) offered or sold on a national securities exchange; or
> "(iii) sold to a qualified purchaser as defined by the Commission pursuant to paragraph (3)."[1]

Congressman Frank opposed the broker-dealer exemption, and introduced Amendment 1c, later denied, to remove the broker-dealer exemption, but retaining the same exemption for sales to qualified purchasers as defined by the Commission pursuant to paragraph (3). *See, House Financial Services Committee Webcast* (6/22/2011) at video time 2:56 to 3:14; and H. Rep. 112-206 at 13 (9/14/2011).

On September 12, 2011, Senator Tester introduced S.1544, which mirrored H.R. 1070 as amended on June 22, 2011, but with two important changes (later incorporated into H.R. 1070). First, S.1544 removed the controversial broker-dealer exemption, and, second, it added a new Section 3, which directed the Comptroller General to complete a report within 3 months on the impact of State laws regulating securities offerings under Regulation A.

On November 2, 2011, the full House suspended rules to consider a further amended H.R. 1070 that conformed to Senator Tester's Bill by removing the broker-dealer exemption, and adding new Section 3 to direct the Comptroller General to complete a study and report within 3 months on the impact of State

[1] Mr. Schweikert proffered that this "Amendment is actually one that we've reached out to a wide variety of people. It helps us cover a handful of concerns and actually serves to clean up one or two things - **we got much of it from the SEC**. *See*, House Financial Services Committee Webcast (6/22/11) (emphasis added), at video time 02:03:17.

"Blue Sky" securities laws on Regulation A offerings. 157 Cong. Rec. H72229 - H7230 (daily ed. 11/2/2011). H.R. 1070 then passed the full House by an overwhelming vote of 421 to 1, *see, id*. at H7236, and was placed on the Senate Legislative Calendar under General Orders.

On March 7, 2012, the House renamed H.R. 3606 as the "Jumpstart Our Business Startups [JOBS] Act," and added the text from pending bills under separate Titles, with the text of H.R. 1070 placed under Title IV, *see* 158 Cong. Rec. H1234 - H1262 (daily ed. 2/7/2012). This Bill passed the full House by a vote of 390-23, *see id*. at. H1288, and then faced strong opposition in the Senate to Title III of H.R. 3606 (Crowdfunding). After considerable debate, the Senate substituted Title III with Senator Merkley's amendment, and then passed the bill by a vote of 73-26, after which the House agreed by a vote of 380 – 41. *See*, 158 Cong. Rec. H1586-1588 (daily ed. 3/27/2012).

Throughout this process, Congress knew Sec. 401(b) of the JOBS Act gave the Commission unrestricted authority to define "qualified purchaser" in a manner that could preempt securities sold to all Tier 2 purchasers because Professor John C. Coffee, Jr., testified on December 1, 2011, that Sec. 3(b) of S.1544 (which mirrored Sec. 3(b) of H.R. 1070 and Sec. 401(b) of the JOBS Act), gave the Commission authority to define "qualified purchaser," and cautioned that:

> It is unclear how the Commission will use this authority (and the Commission could preclude offerings to unsophisticated investors as the price of escaping Blue Sky regulation.)

S. Hrg. 112-444 at 63 (12/1/2011) (*Prepared Statement of Professor John C. Coffee, Jr., Hearings Before the Senate Committee on Banking, Housing and Urban Affairs, "Spurring Job Growth Through Capital Formation While Protecting Investors*" (12/1/2011)).

Congressional intent to give the Commission even broader discretion in defining "qualified purchaser," so that it could preempt all of Tier 2 offerings from State registration, is demonstrated further by adding Sec. 402 which directed the Comptroller General to complete a study and report on the impact of State "Blue Sky" registration laws within 3 months, well before the Commission would issue its Regulation A Amendments.

II. Deference should be given to the Commission's definition for "qualified purchaser" because additional burdens imposed by State registration on Tier 2 Offerings will lead to "absurd" results not intended by Congress

We agree with the Commission's Brief in support of deference to the Commission's position on what Congress intended under Sections 401 and 401 of the JOBS Act, with the additional caveat that:

> with respect to the propriety of addressing policy arguments in the context of a step-one *Chevron* analysis, this Court acknowledges that such arguments may be relevant to the first *Chevron* inquiry based on "the longstanding rule that a statute should not be construed to produce an absurd result." *Mova Pharm. Corp. v. Shalala*, 140 F.3d 1060, 1068 (D.C.Cir.1998). It is clear beyond cavil that in any exercise of statutory interpretation, whether under *Chevron* or otherwise, "[t]he plain meaning of legislation should be conclusive, *except* in the rare cases [in which] the literal application of a

> statute will produce a result demonstrably at odds with the intentions of its drafters." *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 242, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989) (emphasis added) (internal quotation marks and citation omitted). Thus, in the *Chevron* step-one context, "the rule that statutes are to be read to avoid absurd results allows an agency to establish that seemingly clear statutory language does not reflect the unambiguously expressed intent of Congress." *Mova*, 140 F.3d at 1068 (internal quotation marks and citations omitted).

Depomed, Inc. v. United States Dep't of Health & Human Servs., 66 F. Supp. 3d 217, 234 (D.D.C. 2014) *appeal dismissed sub nom. Depomed Inc. v. U.S. Dep't of Health & Human Servs.*, No. 14-5271, 2014 WL 5838247 (D.C. Cir. Nov. 7, 2014).

The States' position to constrain the Commission's authority to define "qualified purchaser" is not only contrary to the express authority stated Section 401(b) of the JOBS Act and 15 U.S.C. 77r(b)(3), it would create an absurd result by limiting the capital formation Congress intended to create, while reducing investor protection by driving businesses to seek capital under Regulation D and other private offering exemptions that are less costly,[2] and where there is greater opportunity for some issuers to defraud investors because there is typically no regulatory review of the offering before money is taken or where there are no or

[2] *See*, GAO Report at 18, finding that imposing State registration requirements on future Regulation A Offerings:

> may deter future use by small businesses. As previously discussed, addressing and complying with securities registration requirements of states can be costly and time-consuming, according to several stakeholders with whom we met. ... As a result, even with the increased attractiveness of the $50 million ceiling, blue sky requirements may still dampen small business' interest in Regulation A.

fewer required disclosure requirements or required audited financial statements, *see, e.g.*, 17 C.F.R. § 230.502.

After considering comments from, and meetings with, representatives in the securities industry, businesses, State Regulators, and NASAA, which advocated the NASAA Coordinated Review Program, the Commission found that preemption for Tier 2 Offerings was justified, in part, because the:

> Amended Regulation A removes the requirement of state qualification for Tier 2 offerings, thereby eliminating the cost and other burdens of the duplicative review under existing Regulation A.

Regulation A Amendment, 80 Fed. Reg. 21806 at 21865 (Apr. 20, 2015). These findings are justified, not only for reasons stated in the Regulation A Amendment, but also for unstated reasons known by securities law practitioners.

The NASAA Coordinated Review Program requires issuers to meet "Disclosure" and much more complicated "Merit" review standards imposed by each State the offering will occur. NASAA Form CR-3(b)(2)-1 identifies 21 Disclosure Review Jurisdictions and 28 Merit Review Jurisdictions. Disclosure Review Jurisdictions follow the Commission's disclosure requirements under Regulation A, which now require initial and annual audited financial statements, and narrative disclosures under SEC Form 1-A or Part I of SEC Forms S-1 or S-11 (the same initial disclosures required for fully registered issuers), as well as semiannual and material event disclosures.

The NASAA Program for Merit Review Jurisdictions presents a much more complicated set of disclosure requirements. In addition to meeting the Commission's disclosures requirements, each Merit Review Jurisdiction has adopted a myriad of NASAA Statements of Policy, which include at least 6 "General Statements of Policy for Registration of Securities," plus at least 10 "Statements of Policy for Specific Types of Securities." *See, NASAA Adopted Statement of Policy Index*.[3] At least 5 of the General Statements of Policy have separate lists of additional disclosure items, and allow the Administrator to deny approval of an offering if the issuer fails to demonstrate that their "long-term business plan will improve the issuer's financial condition." NASAA Statement of Policy Regarding Unsound Financial Condition at III.A. This would allow each Merit Review Jurisdiction to deny applications from issuers in other States where the Administrator is not as familiar with the issuer, and its product and market.

Further, States can differ in their interpretation of what satisfies each NASAA Statement of Policy disclosure item, and States differ on determining when NASAA Statements of Policy for Specific Types of Securities apply. For example, Virginia is believed to look at whether investors have an interest in the business property, while Ohio has stated it uses the four-factor test used to

[3] This Index and copies of the NASAA Statements of Policy are incorporated into this Brief by reference, and are available to the public at:
http://www.nasaa.org/regulatory-activity/statements-of-policy/

differentiate between corporations and partnerships. These differences can result in issuer forum shopping to avoid more onerous program requirements, beginning with a requirement for sponsors to invest at least $1.3 million before making an offering, *see, e.g.*, NASAA Omnibus Guidelines at II.B, and a requirement to develop separate investor suitability standards that must consider at least 12 factors, *see*, *id*. at III.A.

While many of the disclosure items in NASAA Statements of Policy have become part of market practices (i.e. escrow requirements), they also raise the complexity, time, and cost to prepare an offering, and will delay time for approval that will be perceived as substantial to smaller businesses that lack resources available to larger business, and add at least $30,000 in State registration fees for national offerings.

Businesses seeking to limit delays under the NASAA Program will be forced to incur additional costs to prepare detailed letters to the NASAA Coordinator that outline where each NASAA Statement of Policy disclosure item has been incorporated into Offering Circulars that must conform to SEC Form 1-A, Part II, or Part I of SEC Forms S-1 or S-11. This process will add further delay in submitting Offering Statements when expedited approval is needed.

The State's claim that State registration will protect investors does not make sense because objective data from the Commission's EDGAR database shows that

there were only 26 Regulation A Offering qualified by the Commission in years 2012 to 2014, with none appearing to be a national offering under NASAA Program, while the number of Regulation D filings in 2014 that qualified under old Regulation A exceeded 557, and the total Regulation D offerings in 2014 exceeding $1 Trillion, *see, e.g.*, Regulation A Amendment, 80 Fed. Reg. at 21869.

There is significant evidence that our securities laws will discriminate geographically and economically, and in a manner not intended by Congress if Tier 2 Offers are not preempted from the burdens and costs imposed by State registration. The increased costs of Regulation A will force issuers to use Regulation D, which cannot be advertised unless limited to "Accredited Investors" who must incur costs to verify their status, *see* 17 C.F.R. § 230.506(c). It is common knowledge that investors like to "kick-the-tires," and Angel/Venture Capital Proximity studies available in the SSRN database have found that 60% of investors invest in businesses located within a 3 hour drive from their location, and 18% of investors invest in businesses located within their own zip code. *See*, Brent Goldfarb, et al, *Does Angel Participation Matter: An Analysis of Early Venture Financing* at 11 (Apr. 4, 2008). Slides presented by the Angel Capital Foundation to the "SEC Advisory Council on Small and Emerging Companies" on September 17, 2013, report that in 2012, 268,000 investors funded approximately $22.9 Billion in about 68,000 deals (2/3rds early-stage), and that Venture Investors in

2007 had an "Average IRR=27%" on these investments.[4] These reports demonstrate that smaller businesses located away from higher concentrations of Accredited Investors near the Coasts face greater difficulty and higher costs to obtain investment capital, and that Accredited Investors have earned an average return of 27% on investment opportunities the lower 93% of U.S. Households were not allowed to participate, *see, e.g*. Section 4(a)(2) of the Securities Act, Regulation D, and Regulation A Amendment.

III. Conclusion

We ask the Court to find in favor of the Commission. The States will not be able to provide greater investor protection under Tier 2, Regulation A Offerings because empirical evidence demonstrates that issuers will use lower cost Regulation D, where there is little regulatory oversight before investor funds are taken. The only persons who will benefit by imposing State registration or an Accredited Investor definition on Tier 2 Offerings are brokers and dealers who can command higher fees based on the prohibitions against general solicitation under Regulation D, 506(b) Offerings, and Private Equity Groups (Accredited

[4] *See*, David Verrill, ACA Chairman, and Marianne Hudson, ACA Executive Director, *Angel Investors – Critical Initiators of Startups and Job Creation* at 2 and 24 (Sept. 17, 2013)

Investors) who do not have to compete with non-accredited investor for investments that generate average returns near 27%.

Respectfully submitted,

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CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because it contains 13,926 words, excluding the parts exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

I also certify that this brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5)(A) and the type-style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally spaced typeface—Times New Roman, 14 point—using Microsoft Word.

/S/ Ford C. Ladd
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CERTIFICAT OF SERVICE

I certify that the above document will be served on October 13, 2015, by electronic notice for registered counsel and a copy will be served by first-class mail, postage pre-paid, for non-registered counsel.

/s/ Ford C. Ladd
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