

*126th Legislature
Senate of
Maine
Senate District 8*

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TESTIMONY of PRESIDENT JUSTIN ALFOND

In Support Of

L.D. 1512, "An Act To Increase Funding for Start-ups"

Senator Gratwick, Representative Treat and esteemed members of the Joint Standing Committee on Insurance and Financial Services, my name is Justin Alfond. I am a resident of Portland, I am honored to serve as President of the Maine Senate and proud to represent Senate District 8, which includes most of Portland and the islands of Peaks, Cliff and Great Diamond. Today, I am pleased to appear before you as the sponsor of LD 1512, "An Act To Increase Funding for Start-ups."

Maine has many things to be proud of one of which is its entrepreneurial spirit. From Aroostook County to York County, business innovators abound. Promising startup businesses in Maine support our economy through job creation and innovation.

While resources exist to assist entrepreneurs with many aspects of business development including mentorship and educational programs, there is an area that remains problematic for Maine startups as well as existing small businesses – the ability to raise capital. In the wake of the Great Recession, access to capital for startups and small businesses became more limited due, in part, to changes in lending policies and regulations including increased collateral requirements. Consequently, more startups are considering raising equity to replace or supplement loans.

L.D. 1512 presents an opportunity to address this need by providing startups and other businesses with the ability to issue up to \$1 million in securities by filing a short-form registration statement with the Maine Office of Securities and making key information available to investors. Businesses will be allowed to solicit investors within Maine using various methods including social media and the internet.

The ability to seek investors using social media and the internet is a form of crowdfunding. Most of us are familiar with the concept of crowdfunding where individuals and businesses raise money over the internet or through social media in exchange for some type of reward. For example, online platforms such as Kickstarter and Indiegogo allow businesses to post an online campaign explaining the funding

they are seeking. Individuals can pledge financial support in exchange for some type of tangible reward such as services or products. Equity crowdfunding, on the other hand, would allow businesses to offer a share in the company instead of some other type of reward.

L.D. 1512 provides an opportunity to engage in a type of equity crowdfunding whether by newspaper, social media, internet or some other form following the filing of a simplified registration with the Office of Securities. The bill provides this opportunity in a way that preserves important investor protections.

As you likely know, equity crowdfunding is a concept that is being implemented at the federal level as well. Upon final adoption of rules by the Securities and Exchange Commission, businesses will be able to use equity crowdfunding to raise up to \$1 million in capital without registration of the underlying securities. On October 23, 2013 the SEC published and is seeking comment on a 585 page proposed rule which would implement a process for engaging in equity crowdfunding.

Unlike the SEC approach which exempts securities sold through crowdfunding from registration, the approach proposed by L.D. 1512 provides for registration of the securities offering on a short form intended to be simplified enough for a startup to complete without the need to hire securities counsel. Critical disclosures will be provided potential investors so that investors can make informed decisions before investing. It is expected that the simplified registration under L.D. 1512 will be more cost effective than the SEC proposal. Simply put, the proposal provides a way for startups to raise capital with a reduced regulatory burden while at the same time preserving key investor protections.

Unlike the SEC approach, which preempts state regulation of crowdfunding, L.D. 1512 preserves the authority of the Office of Securities to receive and review the offering documents and avoids preemption by relying upon an existing federal registration exemption rather than the crowdfunding registration exemption. By requiring a simplified registration, the Office will be provided with information that can be shared with investors who call to check on an offering before deciding to invest. Under the SEC crowdfunding approach, the Office of Securities will have no information on a crowdfunding offering to provide to potential investors given state preemption.

To be clear, L.D. 1512 does not replace the SEC crowdfunding exemption. Once the SEC finalizes rules permitting the exemption, Maine startups can elect to comply with the SEC requirements or rely on the Maine short-form registration. The Maine registration expands the capital raising options for Maine startups but in no way limits opportunities for Maine businesses.

Securities Administrator Judith Shaw will be testifying after me. She will walk you through the finer points of the proposal and further distinguish the SEC approach from the proposal before you.

I encourage your support for L.D. 1512 and will answer any questions you may have.

**Proposed Draft Amendment to LD 1512,
An Act to Increase Funding for Start-ups**

Amend the bill by striking out everything after the title and before the summary and inserting in its place the following:

Emergency preamble. Whereas, Acts of the Legislature do not become effective until 90 days after adjournment unless enacted as emergencies; and

Whereas, this bill promotes and encourages the growth of Maine small businesses by facilitating the ability of a business to raise capital by selling small amounts of equity to a wider pool of small investors with fewer restrictions; and

Whereas, the enactment of this bill will provide immediate access to capital and streamline regulation for Maine small businesses without diminishing the regulatory protections for investors; and

Whereas, In the judgment of the Legislature, these facts create an emergency within the meaning of the Constitution of Maine and require the following legislation as immediately necessary for the preservation of the public peace, health and safety; now, therefore,

Be it enacted by the People of the State of Maine as follows:

Sec. 1. 32 MRSA § 16304, sub-§ 6-A is enacted to read:

6-A. Maine seed capital short-form registration. The administrator may adopt, by rule, a form to be used as a short-form registration statement for securities being registered under this section and sold in offerings in which:

A. The issuer of the security is a business entity formed under the laws of the State and registered with the Secretary of State;

B. The aggregate amount sold to all investors by the issuer is not more than \$1,000,000;

C. The aggregate amount sold to any investor by the issuer, including any amount sold during the 12-month period preceding the date of the transaction, does not exceed \$2,000, or such greater amount as the administrator may provide by rule or order, unless the investor is an accredited investor as defined in 17 Code of Federal Regulations, Section 230.501 (2013);

D. The offering meets the requirements of the federal exemption for limited offerings and sales of securities not exceeding \$1,000,000 in 17 Code of Federal Regulations, Section 230.504 (2013);

E. The issuer files with the administrator, provides to investors, and makes available to potential investors an offering circular setting forth the following:

(1) The name, legal status, physical address, and website address of the issuer;

(2) The names of the directors, officers, and any persons occupying a similar status or performing a similar function;

(3) The name of each person holding more than 20 percent of the shares of the issuer;

(4) A description of the business of the issuer and the anticipated business plan of the issuer;

(5) A description of the financial condition of the issuer, including, the following:

(a) For offerings that, together with all other offerings of the issuer within the preceding 12-month period, have, in the aggregate, target offering amounts of \$100,000 or less:

(i) The income tax returns filed by the issuer for the most recently completed year, if any; and

(ii) The financial statements of the issuer, which shall be certified by the principal executive officer of the issuer to be true and complete in all material respects;

(b) For offerings that, together with all other offerings of the issuer within the preceding 12-month period, have, in the aggregate, target offering amounts of more than \$100,000 but not more than \$500,000, financial statements reviewed by a public accountant who is independent of the issuer, using professional standards and procedures for such review or standards and procedures established by the administrator, by rule, for such purpose; or

(c) For offerings that, together with all other offerings of the issuer within the preceding 12-month period, have, in the aggregate, target offering amounts of more than \$500,000, audited financial statements;

(6) A description of the stated purpose and intended use of the proceeds of the offering sought by the issuer with respect to the target offering amount;

(7) The target offering amount, the deadline to reach the target offering amount, and regular updates regarding the progress of the issuer in meeting the target offering amount;

(8) The price to the public of the securities or the method for determining the price, provided that, prior to the sale, each investor shall be provided in writing the final price and all required disclosures with a reasonable opportunity to rescind the commitment to purchase the securities; and

(9) A description of the ownership and capital structure of the issuer including:

(a) The terms of the securities of the issuer being offered and each other class of security of the issuer, including how such terms may be modified, and a summary of the differences between such securities, including how the rights of the securities being offered may be materially limited, diluted, or qualified by the rights of any other class of security of the issuer;

(b) A description of how the exercise of the rights held by the principal shareholders of the issuer could negatively impact the purchasers of the securities being offered;

(c) The name and ownership level of each existing shareholder who owns more than 20 percent of any class of the securities of the issuer;

(d) How the securities being offered are being valued, and examples of methods for how such securities may be valued by the issuer in the future, including during subsequent corporate actions; and

(e) The risks to purchasers of the securities relating to minority ownership in the issuer, the risks associated with corporate actions, including additional issuances of shares, a sale of the issuer or of assets of the issuer, or transactions with related parties;

F. The issuer sets aside in a separate bank account all monies raised as part of the offering to be held until such time as the minimum offering amount is reached. If the minimum offering amount is not met within one year of the effective date of the offering, the issuer must return all funds to investors; and .

G. The issuer must comply with such other requirements set forth by rule adopted or order issued under this chapter.

Notwithstanding section 16304, subsection 3, the administrator may provide, by rule, that a registration statements filed under this subsection is immediately effective upon filing.

or becomes effective within some other stated period after filing, conditionally or otherwise.

Emergency clause. In view of the emergency cited in the preamble, the Act takes effect when approved.

SUMMARY

This amendment is being presented by the bill's sponsor to replace the bill and to add an emergency preamble and emergency clause. Like the bill, the purpose of the amendment is to promote and encourage the growth of Maine small businesses by facilitating the ability of a business to raise capital by selling small amounts of equity to a wider pool of small investors with fewer restrictions.

This amendment provides for a streamlined registration process and simplified registration statement if the issuer and the offering meet certain conditions including:

1. The issuer of the security must be a business entity formed and registered under Maine law;
2. The size of the offering may not exceed \$1,000,000;
3. The amount sold to any single investor does not exceed \$2,000 unless the investor is an accredited investor as defined in rules adopted by the federal Securities and Exchange Commission;
4. The offering meets the requirements for a federal exemption from registration for small offerings as set forth in rules adopted by the federal Securities and Exchange Commission;
5. The issuer files with the administrator and provides to investors and prospective investors an offering circular meeting the requirements of the statute and any rules adopted or orders issued by the administrator; and
6. The issuer sets aside in a separate bank account funds received from investors until such time as the minimum offering amount is raised.