Denver Law Review

Volume 34 | Issue 5 Article 2

May 2021

Federal Securities Act of 1933 - The Intrastate Exemption of Section 3(a)(11) - Fact or Fiction

Sanford B. Hertz

Recommended Citation
Sanford B. Hertz, Federal Securities Act of 1933 - The Intrastate Exemption of Section 3(a)(11) - Fact or Fiction, 34 Dicta 289 (1957).

FEDERAL SECURITIES ACT OF 1933 – THE INTRASTATE EXEMPTION OF SECTION 3(a)(11)—FACT OR FICTION?

By Sanford B. Hertz

Sanford B. Hertz received his B.A. degree from Pennsylvania State University in 1952 and his J.D. degree from the University of Michigan Law School in 1955. At law school he was Senior Editor of the Michigan Law Review and was elected to The Order of the Coif. From 1955 until mid-1957 he was an attorney with the Securities and Exchange Commission. He is a member of the Colorado, Denver, Federal, Michigan and American Bar Associations and presently is chairman of the Denver Bar Association Junior Bar Committee. Mr. Hertz is presently in private practice in Denver.

I. Introduction

As a general matter, section 5 of the Federal Securities Act of 1933, as currently amended, prohibits the *offer* of any security through the use of the mails or other means or instrumentalities of interstate commerce unless and until a registration statement has been *filed* with the Securities and Exchange Commission, and prohibits a *sale* of securities by federal jurisdictional means unless and until a registration statement is *effective* with the Commission.[1] Congress, however, recognized that with respect to certain securities and certain transactions involving securities, registration would be unnecessary in the public interest, and therefore provided a series of exemptions set forth in sections 3 and 4 of the Securities Act of 1933.[2] The purpose of this article is to discuss one of these exemptions, the intrastate exemption of section 3 (a) (11) of the 1933 Act,[3] with a view to pointing up some of the problems which arise and how these problems might be solved.[4]

---

[1] 48 Stat. 74 (1933), 15 U.S.C. § 77e (1956). Prior to the 1954 amendments to the Securities Act of 1933, it was unlawful to both offer and *sell* securities by interstate means or by the use of the mails unless a registration statement was effective with the Securities and Exchange Commission. It should be noted, however, that even before the 1954 amendments, the Commission recognized the necessity for dissemination of information about a security, distinguishing it from solicitation. Thus, the use of the "red herring prospectus" was encouraged, the Commission expressly holding that such use was not to be construed as an offer to sell securities prior to effective date. Former Rule 131 of General Rules and Regulations under the Securities Act of 1933. In 1954 this theory was codified by permitting offers but not sales, contracts of sale or contracts to sell prior to the effective date. See Loss, Securities Regulation 149 (1951), and Loss, Securities Regulation 51, 67 (1955 Supplement). See, also, S. Rep. No. 1036 at 15 and H. R. Rep. No. 1542 at 23, 83d Cong., 2d Sess. (1954), and SEC, Securities Act of 1933 Release No. 3519 (1954). 17 C.F.R. 230.433 contains the requirements for the preliminary prospectus to be used prior to effective date. This is the successor to the "red herring prospectus."

[2] 48 Stat. 74 (1933), 15 U.S.C. 77c & d (1956).

[3] 48 Stat. 74 (1933), 15 U.S.C. 77c(a)(11) (1956).

[4] For articles discussing other exemptions from the registration requirements, see, Hertz, *The Federal Securities Act of 1933: Revised Regulation A*, 33 DICTA 307 (1956); Mehler, *The Securities Act of 1933; "Private or Public" Offering*, 32 DICTA 359 (1955); 70 Harv. L. Rev. 1438 (1957).

The intrastate exemption found in section 3(a) (11) of the 1933 Act states:

"Except as hereinafter expressly provided, the provisions of this title shall not apply to any of the following classes of securities:

"Any security which is a part of an issue offered and sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within, or, if a corporation, incorporated by and doing business within, such State or Territory."[5]

It has generally been held that this exemption was designed to apply only to "local financing by local industries, carried out purely through local purchasing."[6] Thus, the initial intent in the enactment of this exemption is rather simple, recognizing the needs of purely local industry and in effect finding that registration would be unnecessary for the protection of investors and in the public interest. It should be noted, however, that the exemption applies only to the registration requirements of the 1933 act and not to the anti-fraud provisions of section 17.[7]

Despite the simple purpose of this section, it causes some serious language interpretation problems and creates others when we attempt to ascertain whether the exemption is available in any particular situation. Our efforts will be devoted to these problems. A brief resume of what we will subsequently discuss will prove helpful at this point. Extensive treatment will be devoted to the meaning of the phrase "resident within a single State or Territory . . ." as used in section 3(a) (11). The problem is particularly at issue in attempting to ascertain whether the above-quoted phrase is synonymous with the term "domiciled" and if so, what is the legal definition of this latter term. Particular attention has also been devoted to the problem of whether military personnel assigned to a particular state are "resident in" or "domiciled within" that state. Would a sale of securities to such a person be deemed a sale to a "non-resident"?

Another troublesome interpretive problem which will be treated, but less extensively, is the "issue" concept created by the use of the language "a part of an issue . . . ." in section 3(a) (11). Some standard will be suggested to determine when an offering of securities is part of an issue in order to ascertain when two separate offerings should be deemed integrated in arriving at a conclusion concerning the availability of this exemption.

Brief consideration will also be given in discussing the 1954 amendment to section 3(a) (11) which added the words "offered and" before the term "sold." The question arises specifically when an offer is made to a non-resident through the use of the mails or means of interstate commerce but no sale is consummated. Query, whether the availability of the exemption in such a situation would be destroyed. Further, a brief discussion will be made on the requirement that the issuer be "doing business within" the state where the offers and sales are to be made.

---

[5] 48 Stat. 74 (1933), 15 U.S.C. 77c(a)(11) (1956).

[6] SEC, Securities Act of 1933 Release No. 1459 (1937). See, also, Loss, Securities Regulation 374 (1951), and 379 (Supp. 1955).

[7] 48 Stat. 74 (1933), 15 U.S.C. 77q (1956). Loss, Securities Regulation 413 (1951).

Apart from the aforementioned problems which arise because of the language used in section 3 (a) (11), consideration will be given to other general questions. Among these will be the problem of an immediate resale by a resident investor to a non-resident investor, raising the question of *trading v. distributing*. If the contract to purchase and sell the securities is to be on the installment payment basis, what result if the purchaser moves from the jurisdiction prior to the time all payments have been completed? If securities are sold in joint names, need both co-owners be residents? What result if the resident co-owner pays the entire consideration for the securities?

II. Problems of Language Interpretation

The position has generally been taken that an offer alone, without the consummation of a sale, of securities to non-residents will vitiate the exemption.[8] This was so even prior to the 1954 amendment to the Securities Act of 1933 which added the words "offered and" before the term "sold." The necessity for this change was brought about because of the amendment to section 5 permitting offers, but not sales, prior to effective date. Since section 2 (3) of the 1933 act defined a "sale" to include an "offer," it became mandatory to change this definition to conform to amended section 5.[9] This was done by removing an "offer" from the integral part of a "sale" and by redefining an "offer" separate from a "sale," to include every at-

[8] Loss, Securities Regulation 375 (1951). SEC, Securities Act of 1933 Release No. 1459 (1937).
[9] 48 Stat. 74 (1933), 15 U.S.C. 77b(3) (1956).

tempt to dispose of a security for value. Once this had been accomplished, it was necessary to add the words "offered and" in section 3 (a) (11) to demonstrate the intent to limit both offers and sales of securities to residents of a single state or territory. Thus, as a practical matter, the 1954 amendment to section 3 (a) (11) did not change the law as it existed prior to the amendment, and an offer alone to a non-resident without a sale will vitiate the exemption.

The language "a part of an issue" used in section 3 (a) (11) has caused some concern and deserves special consideration. As a general matter it might be said at the outset that the entire "issue" must be sold to residents of only one state in order to insure that the exemption will be available.[10] The real dilemma comes when an attempt is made to define and ascertain just what is an "issue" of securities. Such a determination presupposes consideration of the question whether one offering of securities should be integrated with another offering. The most lucid way of examining this problem is by means of a variable hypothetical case:

> Assume that on February 1, 1957 the board of directors of *XYZ* Mining Company met to discuss the need for additional capital to expand their exploration and development program. The Board authorized the public sale of 1,000,000 shares of $1.00 par value stock at the market price, to be offered in two separate blocks at two separate times (six months separating each offering), the first block pursuant to Regulation A[11] in ten states, and the second block only to residents of the State of Colorado. All the proceeds from the first block sold are to be used in exploration; the proceeds from the second block to be used in advance exploration and in development, if warranted, on the same property. If the first block were entirely sold under Regulation A to residents of more than one state, could the second offering be made under the intrastate exemption? (Assume, for the sake of discussion, that all other factors of the intrastate exemption would be available if the "issue" question were resolved favorably for the company.)

The above hypothetical case directly raises the issue of whether two offerings will or should be integrated, i.e., the Regulation A and the purported intrastate offering of section 3 (a) (11). It is therefore essential to determine what elements should be examined in order to ascertain whether one offering is to be integrated with another. The following factors, among perhaps many others, seem relevant in determining the question of integration:

(1) The offerings are made at or about the same time.
(2) The offerings are part of a single plan of financing.
(3) The offerings involve issuance of the same class of security.
(4) The same type of consideration is to be received.
(5) The offerings are made for the same general purpose.

Certainly, if all these factors exist, the tendency would be to integrate the offerings into one single issue. If, however, one or

[10] SEC, Securities Act of 1933 Release No. 1459 (1937).
[11] 17 C.F.R. 230.251-62 (1956).

more factors are missing, all the circumstances must be considered and the relative value of the various factors weighed to determine the integration question.

Thus, if in our hypothetical case the offerings were part of a single plan of financing, involved the same securities for the same consideration, were made for the same general purpose, and were made at or about the same time, it probably would be found that the offering of the second block of stock would be part of the same "issue" as the first, and thus integrated. Since the offering under Regulation A was multi-state, the section 3 (a) (11) exemption would probably not be available for the second offering. It can be concluded, as a general matter, that because of the "issue" concept in section 3(a) (11), this exemption is incapable of combination with any other exemption under the 1933 act.[12]

However, varying the facts in our above hypothetical case in order to show that the securities were not identical, *e.g.*, the first block may be equity securities while the second block, debt securities; that the two blocks of securities were issued for different considerations, *e.g.*, the first block to the public under Regulation A for cash, and the second block to the public for property or equipment; that the second offering was made two years after the first and not six months after; that the purposes of each offering were entirely different and authorized at different times; then we might conclude that the offerings were not integrated and therefore the second block might be offered and sold under the section 3 (a) (11) exemption.

The conclusion, however, in each of the above cases was apparent. It might be a more difficult question to decide if the two offerings should be integrated where, *e.g.*, the types of securities were similar but the consideration of the sale different, or where the authorization of one plan of financing was given simultaneously, but a relatively long period of time elapsed between the two offerings. It seems safe enough to conclude that each case must be considered on its individual facts when attempting to ascertain whether two or more offerings should be integrated. The above are not the only facts which might be utilized in examining offerings to

[12] Loss, Securities Regulation 374 (1951).

ascertain if they are part of the same issue. The reader undoubtedly, as each case is presented, will arrive at his own standard to check against the facts of the case.

Another question related to the above problems is whether the private offering exemption of section 4(1)[13] can be combined with the exemption of section 3(a) (11) where the only securities issued under section 4(1) were issued to "insiders"—officers, directors and promoters. Should we treat the integration question any differently when insiders are involved?

At one time it was thought that to avoid integration of an offering to promoters with a cash public offering, it was necessary that the shares to the promoters be issued only for property or services. Thus, the crucial test applied was the consideration paid for the securities by the insiders and by the public. This strict qualification placed a difficult burden on the insiders since it was almost impossible to finance the initial steps of the venture without some cash expenditure. As a consequence there has grown the practice of recognizing the existence of a private offering exemption in connection with offerings to promoters for cash or otherwise, even though such offering is made at or about the same time as the offering to the public. From this it might be concluded that there would be no integration between the section 4(1) and section 3(a) (11) exemptions where the issuer upon organization issued stock to "non-resident" promoters and thereupon commenced a public offering relying on section 3(a) (11). However, each case must be examined on its own facts to reach any conclusion and the reader is cautioned of the pitfalls of generalization.

Still another variation of the problem arises in attempting to determine whether to integrate a section 3(a) (11) offering with a registered offering. It would appear that the same standards would be applicable as used in discussing integration with respect to two exempt offerings, and should all or some of these factors be present, the offering would be integrated and the exemption of section 3(a) (11) would not be available if the registered offering was multi-state. The foregoing leads to the conclusion that section 3(a) (11) is a one-way street—once it is used and relied upon, the "issue" concept makes it difficult to return without admitting possible liability for offering and selling unregistered and unexempt securities.

The "doing business within" concept is also worthy of some explanation. The issuer must be doing some business in the state where the securities are to be offered, but it has been the general view that it need not be confined to that state. The real issue revolves around the question: How much business must be done by an issuer to come within the intended meaning of the phrase in order to qualify for the section 3(a) (11) exemption? It would appear that the hypothetical mining company referred to above must be performing substantial operations and conducting substantial activities in the state of incorporation and "residence" in addition to bookkeeping and other functions before the "doing

[13] 48 Stat. 74 (1933), 15 U.S.C. 77d (1956).

business" concept would be satisfied. If all the properties were in a state other than the one of incorporation, it would not be unlikely that this requirement of the section 3(a) (11) exemption would be missing and the exemption, therefore, would be unavailable. Again, it is a factual matter to determine whether a company seeking to use this exemption is "doing business" within the state of incorporation and each case must be decided on an *ad hoc* basis.

The most difficult language interpretative problem that exists in section 3(a) (11) is the one brought about by the use of the term "persons *resident* within a single State or Territory."[14] It is essential to ascertain just what Congress meant by the use of the term "resident," and more particularly, whether it meant "resident" to be synonymous with "domicile." A discussion of some general propositions of law which define these terms is in order, and some discussion on the difference between them will also prove helpful.

It is axiomatic that "domicile" and "residence" as a general matter do not bear the same meaning.[15] Typically "domicile" has been defined as "a residence at a particular place accompanied with positive or presumptive proof of an intention to remain there for an unlimited time."[16] Thus, the key factor seems to be that a person have the necessary and requisite *intent* to make a certain place his "home" or domicile. Domicile then is more inclusive than residence, the latter referring to mere physical presence without an intent to remain in a place for an indefinite period of time and without an intent to make that place one's home or abode.

However, as in every area of the law where proof must be taken on the state of mind of an individual, to establish this intent physical and tangible evidence will be given credence, relying on the age old maxim that "what you do speaks louder than what you say." Thus, various factors are indicia of a person's intention to make a particular locale his home. The following have been held highly significant in attempting to ascertain intention to create a domicile:

(1) declaration and testimony regarding intent,

(2) place of voting,

(3) the nature of the position which brings one to or keeps one in a particular locale,

(4) the type of habitat one has, *i.e.*, has he purchased a home, rented an apartment, or lived at a hotel,

(5) the presence of his personal chattels, *e.g.*, furniture and pets,

(6) the presence of his family and other dependents,

(7) the nature and extent of his participation in the community, *e.g.*, church, club and lodge memberships,

---

[14] (Emphasis supplied.)

[15] District of Clumbia v. Murphy, 314 U.S. 441 (1941); Mitchell v. United States, 88 U.S. (21 Wall.) 350 (1874); Owens v. Huntling 115 F.2d 160 (9th Cir. 1940); Sweeney v. District of Columbia, 113 F.2d 25 (D.C. Cir. 1940), *cert. denied* 310 U.S. 631 (1940); Lyons v. Egan, 110 Colo. 227, 132 P.2d 794 (1942); Jain v. Bossen, 27 Colo. 423, 62 P.2d 194 (1900). See also, 1 Beale, Conflict of Laws c. 2 (1934); Reese, *Does Domicil Bear a Single Meaning*, 55 Colum. L. Rev. 589 (1955); Tweed & Sargent, *Death & Taxes Are Certain—But What of Domicil*, 53 Harv. L. Rev. 68 (1939); Annot., 148 A.L.R. 1413 (1944). However, in Fangman V. Movers, 90 Colo. 308, 8 P.2d 762 (1932) the court held that it was unquestionably true that generally speaking "domicile" and residence were identical. This isolated case does not appear to disturb the original conclusion, and it will be treated as only an isolated statement contrary to the great weight of authority.

[16] Mitchell v. United States, note 15 *supra*; District of Columbia v. Murphy, note 15 *supra*; Owens v. Huntling, note 15 *supra*; Sweeney v. District of Columbia, note 15 *supra*; 1 Beale, Conflict of Laws c. 2 (1934); Restatement, Conflict of Laws c. 2 (1934).

(8) the place of his financial investments, location of his savings and checking accounts, and location of the depository of his salary,

(9) his relationship to his former place of abode—what bridges has he kept and what has he burned,

(10) the retention of his former place of abode, and finally,

(11) the jurisdiction to which he pays taxes and the district where he files his federal income tax return.[17]

If one claims his "domicile" to be in the State of Colorado and his physical presence is in Michigan, he votes in Michigan, pays Michigan income tax, has a home in Michigan, belongs to no organizations or groups in Colorado but does in Michigan, and further demonstrates by other actions that Michigan is his real "home," the law will probably declare that his domicile is in Michigan despite the fact that he contends to the contrary. Where, however, an individual declares that his "domicile" is in a particular locale, this expression of his intent will be given great weight, and if his physical manifestations of this intent concur with his declaration, undoubtedly no one would contest the place of his "domicile."

Once it is ascertained, under the above standards, where a person's domicile is, determination must then be made of the legal consequences which flow from this. Again the law seems quite clear; a person may have only *one domicile* at *one time*.[18] There are some authors who feel that the term "domicile" does not bear a single meaning and is not a unitary concept. Thus, they argue that a determination of a person's domicile should be based upon the context of why we are attempting to determine his domicile, and that it may be different for different purposes. However, these authors do agree that a man may have only one domicile at a time under the law of one state.[19] This theory has not yet found its impact in the cases which the writer has read, and for all purposes of this paper we will assume what appears to be the weight of authority—*that a person may have only one domicile at one time for all purposes.*

If "domicile" is a combination of physical presence and the requisite intent, what of "residence"? This term has a far narrower meaning than "domicile" and does not encompass the exhaustive search into a man's mind to ascertain his intent. Professor Beale in his treatise[20] states that residence is merely a factual place of abode and that a residence might be acquired in any particular locality merely by physical presence, even for a short definite period of time with an intent to remain in the place for the time being. This proposition is generally borne out by the authorities.[21] Thus, "domicile" generally means a permanent status in a particular locale while "residence" means probably nothing more than temporary presence—regardless of the length of time of the temporary presence.

---

[17] See District of Columbia v. Murphy, note 15 *supra*; 1 Beale, Conflict of Laws § 41-A (1935); 61 Harv. L. Rev. 1232 (1948) (note discussing the evidentiary factors in the determination of domicile).

[18] See District of Columbia v. Murphy, 314 U.S. 441 (1941); Mitchell v. United States, 88 U.S. (21 Wall.) 350 (1874); Lyons v. Egan, 110 Colo. 227, 132 P.2d 794 (1942); Restatement, Conflict of Laws c. 2 (1934); 1 Beale, Conflict of Laws 87 (1935); Tweed & Sargent, *supra* note 15.

[19] See Reese, *supra* note 15; 61 Harv. L. Rev. 1232 (1948).

[20] Beale, Conflict of Laws c. 2 (1934).

[21] See note 15 *supra*. Also, Commissioner v. Swent, 155 F.2d 513 (4th Cir. 1946); Dwyer v. Matson, 163 F.2d 299 (10th Cir. 1947).

Flowing from this we note that as clear as the authorities are that a man may have only one domicile at one time, they are equally clear that he may have numerous residences at the same time.[22] Thus, a man with a home in New York, a winter home in Florida, and a summer home in Colorado may be resident in all three states but he may have only one domicile for legal purposes.

With this distinction between the terms "residence" and "domicile," the crucial issue must be faced as to which of these terms Congress meant in using the phrase "resident within a single State or Territory . . . ." If it meant "domicile," then an offering and sale of securities to a person who was a resident of Colorado but whose domicile was in Michigan by an issuer incorporated in Colorado would destroy the section 3 (a) (11) exemption. However, if Congress meant "residence," then a domiciliary of the State of New York who had a summer home in Colorado (assume enough to satisfy the residence test) may be offered and/or sold securities under this exemption. Likewise, this same issuer may offer or sell these securities to a Michigan domiciliary who was also a resident of Colorado under the section 3(a) (11) exemption. If this were carried to its logical conclusion, it would be possible to have securities holders domiciled in all forty-eight states in a company whose public offering was made under section 3 (a) (11). Surely this was not the Congressional intent in enacting the section 3(a) (11) exemption.

Perhaps the phrase "within a *single* State or Territory . . . ."[23] might be used to demonstrate that "resident within" is synonymous with domicile. The use of the word "single" makes the writer think that Congress intended to restrict the offer and sale of securities to people who were, as a matter of law, present and situate in only one state. The real purpose of this exemption, therefore, was to permit *local financing for local industry* without the necessity of filing a registration statement. Surely, then, if an issuer were permitted to sell in all forty-eight states to people who merely had a bare residence in the state of incorporation while domiciled elsewhere, the financing would not be local to those persons. However, if it can be concluded that since this was the purpose of the section 3(a) (11) exemption, it would follow that Congress really meant to restrict

[22] See District of Columbia v. Murphy, 314 U.S. 441 (1941); Dwyer v. Matson, note 21 *supra;* Lyons v. Egan, 110 Colo. 227, 132 P.2d 794 (1942); Restatement, Conflict of Laws c. 2 (1934); 1 Beale, Conflict of Laws, note 15 *supra;* Annot., 148 A.L.R. 1413 (1944).

[23] (Emphasis supplied.)

the sales to persons "domiciled" in the state of the issuer's incorporation. Since, as a matter of law, a person can have only one domicile at one time, it would seem that this concept would be more closely akin to the "single State or Territory" language in section 3 (a) (11). Unfortunately the writer has found no case interpreting section 3 (a) (11) on this issue and the above would only be argumentative to a court of law.

Even more unfortunate is that draftsmen of statutes and legal instruments do not always use the terms "domicile" and "residence" in their true legal sense. Thus, it is possible that where the term "residence" is used, the statute or instrument really meant "domicile"; of course, the reverse of the situation may also be true. The authorities bear out this interchanging use of these two terms and generally hold that in each instance where an interpretation is essential, the individual statute and facts must be examined to ascertain intent. "The word 'residence' is often used in statutes. When it is so used, there is room for difference of interpretation. As used in a statute, the word may mean a domicile; or it may mean a dwelling place, which lacks the legal requirements of domicile."[24] In *Sweeney v. District of Columbia*,[25] the court said, in discussing the use of the term "resident" in a statute, that "without more, its normal and usual meaning is 'domiciled.'"[26] In *Commissioner v. Swent*,[27] the court, in holding persons to be residents of the United States for income tax purposes, said that sometimes "residence" means "domicile" and since the residence of an individual is generally the same place as his domicile, they are frequently used as if they are synonymous, but they clearly are not identical. The Tenth Circuit held in *Dwyer v. Matson*[28] that the term "residence" may have many meanings and that the issue in each statute is to ascertain in what sense the word "residence" is used, *i.e.*, is it temporary residence or is it permanent or domiciliary residence that is required? A similar holding appears in *Downs v. Commissioner*,[29] where the court said, "The meaning of the word 'resident' is not always exactly the same, and its true meaning in a statute must be understood in connection with its context and with the legislative purpose."[30]

These cases would be helpful in explaining away the use of the term "resident" in the statute in an argument that Congress really meant "domicile" and with all the legal consequences which flow from a use of this term. Thus, an argument could be made that would free one from being held to the conclusion that when Congress used the term "resident within" they meant "residence" rather than "domicile." A combination of the argument setting forth the purposes of section 3 (a) (11) with these cases would possibly persuade a court that domicile in its strict legal sense was intended.

Professor Loss has stated that the Securities and Exchange Commission has construed residence to mean domicile in the con-

---

[24] See 1 Beale, Conflict of Laws 110 (1935).
[25] 113 F.2d 25 (D.C. Cir. 1940), *cert. denied*, 310 U.S. 631 (1940).
[26] *Id* at 27.
[27] 155 F.2d 513 (4th Cir. 1946).
[28] 163 F.2d 299 (10th Cir. 1947).
[29] 116 F.2d 504 (9th Cir. 1948).
[30] *Id.* at 507.

flict-of-laws sense.[31] He also has stated that since the statute does not define residence, and since the Commission's construction that "residence" really means "domicile" in the strict legal sense has been unchallenged for a number of years, no issue is anticipated to be raised at this time. Professor Loss also has asserted in the 1955 supplement to his treatise that the exemption has not been considered available unless the entire issue of securities were offered and sold exclusively to persons *domiciled* in the one state.[32]

However, a decision which might persuade a court to take a contrary position was found in *Owens v. Huntling*.[33] The court in this case was called upon to construe the terms in an Oregon statute "*resident within* the state of Oregon,"[34] and specifically whether it means "domicile" or "residence" in the strict legal sense. The court held that if the Oregon legislature intended "resident within the State" to mean "domicile within the state," it would have said so. The court went on to say that even the word "residence," which is sometimes considered synonymous with "domicile" was not used, and that "resident within" is equivalent to "residing within" and "domicile" was not intended. The above case is particularly significant in light of the fact that section 3(a) (11) also uses the language "resident within" a state. It certainly would be possible for a court

[31] Loss, Securities Regulation 379, n. 252 (1951).

[32] Loss, Securities Regulation 163, addition to note 247 (Supp. 1955). See, also, S. Rep. No. 1036 at 13 and H. R. Rep. No. 1542 at 22, 83d Cong., 2d Sess. (1954) where the legislative committee referred to persons "domiciled" in the one state.

[33] 115 F.2d 160 (9th Cir. 1940).

[34] *Id.* at 162 (emphasis supplied).

to follow the *Owens* case and hold that if Congress meant domicile, with all its legal consequences and significance, they would have said so.

However, the writer still believes that in light of the probable purpose of section 3(a) (11) and with the interjection of the term "single" to modify "State or Territory," an effective argument could be made to persuade a court to hold that domicile with all its legal consequences was intended.

Assuming, for argumentative purposes, that a court would agree that "resident within" means "domicile," attention must be given to the specific issue of whether military personnel stationed in a state acquire, by virtue of their presence, a domicile in that state. As a general proposition, the determination of the residence of military personnel is the same as that for non-military people. Thus, the physical presence in a particular locality coupled with the requisite intent will establish domicile. The peculiar problem which arises where the military are concerned comes when an attempt is made to determine if the mere presence of a soldier in a state where he is stationed for an indefinite period of time is sufficient to make him a domiciliary of that state.

It is generally held that the domicile of a person in the military service remains at the place where he entered the service, absent express intention to the contrary.[35] Thus, a soldier under orders at a particular camp with no express intent to remain in the state after his military service is over will generally not acquire domicile in that state. The real key seems to be that military personnel are in a particular place not voluntarily, but under orders, and thus the requisite intent probably has not been formed. There is also the fact that at any time a soldier might be ordered to a different military post, and thus his tenure in any particular locality is probably anything but permanent.

However, it is also clear that with the requisite intent a person in the military can change his domicile to the place where he is stationed. He must form the necessary intent and demonstrate this intent by sufficient physical acts to manifest such intent. Here, though, the demonstration of intent must be apart from his military status. Thus if he chooses to remain in the particular state where he is stationed, and if ordered elsewhere he intends to return, it is not impossible to acquire a domicile. Professor Beale says "he [speaking of military personnel] cannot acquire a domicile in an army post."[36] Therefore, if he is ordered to live within the military reservation in quarters provided, Beale says he cannot acquire domicile. The writer is of the opinion, unsubstantiated by competent authority, that this is carrying the intent concept beyond all bounds. Even if ordered to dwell on the post, it seems that the necessary intent could be formed and if the necessary acts demonstrate this intent, a soldier might very well be domiciled in the state. It seems easier to see the acquisition of domicile if the soldier lives with his family off the post at a place in the community where he chooses.

---

[35] Humphrey v. Fort Knox Transit Co., 58 F. Supp. 362 (W.D. Ky. 1945) (dicta); Wise v. Bolster, 31 F. Supp. 856 (W.D. Wash. 1939); Annot., 148 A.L.R. 1413 (1944); 28 Minn. L. Rev. 69 (1943); 1 Beale, Conflict of Laws § 21.2 (1935); Restatement, Conflict of Laws § 21 (1934).

[36] 1 Beale, Conflict of Laws 155 (1934).

However, this merely goes to the proof of establishing domicile and does not enter into the substantive issue of what will create domicile.

Thus, it seems fair to conclude that the physical presence of a soldier in a state does not *per se* operate to establish a new domicile —the necessary factor of intent must be formed and present to accomplish this.

One case in particular bears specific mention since it was decided first by the Supreme Court of Colorado and later reversed on appeal by the United States Supreme Court. In *Cass v. Dameron*,[37] the Treasurer of the City and County of Denver assessed the tangible personal property of Dameron, an officer stationed at Lowry Air Force Base in Denver. Dameron relied for his defense, in protesting the assessment, on the Soldiers and Sailors Civil Relief Act,[38] which in essence stated that a soldier shall not lose his domicile for personal property taxes because he is stationed at a particular place. The issue which the Colorado Supreme Court faced was whether Denver had jurisdiction over the person and property of Dameron to levy the tax. The Colorado court, after admitting that Dameron was domiciled in a state other than Colorado, concluded that the purpose of the Soldiers and Sailors Civil Relief Act was to avoid multiplicity of taxes and since Louisiana, Dameron's state of domicile, did not tax the property, Colorado was within its right to do so. Dameron appealed to the United States Supreme Court and in *Dameron v. Brodhead*,[39] that court reversed the Colorado court. The Supreme Court held that the avoidance of double taxation was not the intent of the Soldiers and Sailors Civil Relief Act, but rather it was to free servicemen from both income and property taxes imposed by any state by virtue of their presence as a result of military orders.

Admittedly this case is not on all fours with our issue but it might be indicative of the attitude of the Supreme Court, *i.e.*, that military personnel are not domiciliary citizens by virtue of physical presence under military orders. It is not unlikely that the same conclusion could be reached when the issue of the domicile of military personnel arises for purposes of section 3(a) (11).

An analogous situation is the status of persons who go to work

[37] 125 Colo. 477, 244 P.2d 1092 (1952).
[38] 58 Stat. 722 (1944); 50 U.S.C. Appendix 574 (1951).
[39] 345 U.S. 322 (1953).

for the federal government and by virtue of this live in the District of Columbia. Are they domiciled in the District or do they retain their original residence from whence they came? Of course, no categorical answer can be given. In *Sweeney v. District of Columbia*,[40] the court held that federal employees who come to work in Washington, D.C. would generally retain their domicile in the state from which they came, unless they give clear evidence of their intention to forego their state allegiance. The court thought it quite significant that federal duty and service requires residential presence in the District. In a dictum the court said that, "military and naval men, it was conceded, would retain domicile in the state of residence at the time of appointment."[41] So an argument by analogy in the military situation might be made to the effect that employment under orders or a requirement to live in a particular place would not create a domicile for the persons so ordered or employed.

A similar view was held by the United States Supreme Court in *District of Columbia v. Murphy*,[42] where this Court categorically stated that, "a man does not acquire a domicile in the District simply by coming here to live for an indefinite period of time while in the Government service."[43] Thus, if such is the view with respect to civilian employees who leave their state of original domicile, would not the same view be adopted with respect to military personnel?

Although restricted to the issue of voting and eligibility to public office, Article VII, §4 of the Constitution of the State of Colorado says that no person shall gain "residence" by reason of his presence while in the civil or military service of the state or of the United States. This might show a trend toward holding that military personnel, at least for some purposes, are not domiciled in Colorado. A similar view might be adopted under section 3(a) (11).

There is some authority which indicates that military personnel are unable to acquire domicile on a military reservation under the jurisdiction of the federal government although the reservation is situated within the borders of the state.[44] However, this would have very limited application since the soldier could probably acquire domicile in the state by forming the necessary intent coupled with physical acts to manifest this intent. This theory would have such limited application that it does not bear further consideration at this time.

Two final refinements on the residence issue remain to be discussed. First, what should be the effect of a subscription agreement used by an issuer attempting to rely on the section 3(a) (11) exemption, which states that the subscriber-purchaser warrants that he is a resident of a particular state and that if it should later be determined that the contrary is true, the sale and subscription is void? An agreement such as this would tend to demonstrate an awareness on the part of the issuer that section 3(a) (11) is quite limited in scope and must be restricted to persons "resident within a single State or Territory." However, the availability of the exemption depends upon the facts of the situation and despite any attempt to undo an

---

[40] 113 F.2d 25 (D.C. Cir. 1940), *cert. denied*, 310 U.S. 631 (1940).
[41] *Id.* at 29.
[42] 314 U.S. 441 (1941).
[43] *Id.* at 454.
[44] See Annot., 148 A.L.R. 1413 (1944).

offer and sale to a non-resident, such a sale would technically vitiate any exemption. A subsequent avoiding of the contract would merely demonstrate an attempt to comply but would not be a substitute for actual compliance. It would appear that the mere obtaining of residence and investment representations will not establish the availability of the exemption.

The second refinement arises where the securities are taken in joint names, either as tenants-in-common or as joint tenants with the right of survivorship. It would seem clear that if each co-owner paid his pro-rata share for his interest, both must be "residents" of the state of incorporation of the issuer. Merely because one is, will not excuse the other or change the concept of "residence" in order to claim the exemption. A problem comes when the securities are taken in joint names but the total consideration is paid by the "resident" purchaser. Here it might be concluded that the sale was made to the resident and a gift of an undivided interest of the securities was then given by such person to the non-resident. Since the Securities Act of 1933 does not contemplate jurisdiction with respect to gifts of securities, if such was the case, such a procedure would not vitiate the exemption. At least the equity in this latter case would be toward holding the exemption available.

The foregoing has attempted to point up a number of problems which exist in attempting to interpret the language used in section 3(a) (11), the most serious, of course, being the "residence" question. A conclusion of this problem is most difficult to draw, but it would appear that once a court was convinced that "resident within a single State or Territory" meant domicile in its legal sense, it would follow that all offers and sales must be to persons who live in only one state and who have intended to make such state their indefinite permanent place of abode—*i.e.,* domiciled within. With respect to the military problem, each case of an investor must be taken on an individual basis with a view toward examining the facts in order to ascertain his actual intent with respect to his domicile. Depending on the facts, arguments could be made either way.

Attention will now be directed to the problems caused by section 3(a) (11) which are other than language interpretation.

III. Miscellaneous Problems

A. *Trading v. Distributing*

A problem which is somewhat akin to the residence question is the one raised when the original issue is all sold to residents of one state and then an interstate market is subsequently created. Specifically, will the sale by the resident investors to non-residents vitiate the section 3(a) (11) exemption for the issuer or cause a registered broker-dealer to aid in violating section 5 of the Securities Act of 1933, as amended? In other words, when does the distribution end and the trading begin?

The first expression of official policy on this issue was promulgated by the Federal Trade Commission when this agency was charged with the obligation of administering the securities laws. A public release by this agency stated that "in order that the exemption of section 3(a) (11) may be available for securities of any issue, it is clearly required that the securities at the time of completion of ultimate distribution shall be found only in the hands of investors resident within the state. Ultimate distribution, in the opinion of the Commission, was declared to consist not only in the delivery of the bonds from the issuer to the underwriters, and the delivery of the bonds from the underwriters to sub-underwriters and to dealers, but also in the disposition of the bonds in the hands of investors in any secondary distribution which might take place pursuant to arrangements by the issuer or underwriters."[45]

[45] FTC, Securities Act of 1933 Release No. 201 (1934).

The only reported decision discussing this issue is found in *Brooklyn Manhattan Transit Corp.*[46] In this case the Brooklyn Manhattan Transit Corp. applied for the registering or listing of their bonds on the New York Stock Exchange and the Commission refused. In order to "clear the air" on the reason for this denial, the Commission held a hearing, obtained evidence, and issued the opinion in this case. Briefly, the facts found were that the Brooklyn Manhattan Transit Corp. desired to issue $8,000,000 in bonds through the use of the intrastate exemption of section 3(a) (11) in order to avoid the necessity of registering. A large block of these bonds was sold to four banking firms in New York City and these firms, in turn, sold a portion of them to approximately fourteen dealers, all in New York City, who purchased for their own account. These dealers and the four banking houses then proceeded to distribute the bonds to both residents and to non-residents, the former group also re-distributing to other non-residents. The Commission found that within one day after the bids were accepted, non-residents had title to the bonds and that approximately 15% of these bonds were held by non-residents within a short time after the sale commenced.

Counsel for the Brooklyn Manhattan Transit Corp. argued that the sale of the bonds to the four banking houses (who were admittedly underwriters) and then to the fourteen dealers was sufficient to give the bonds the character of "an issue sold only to persons resident within a single State [New York]."

The Commission in its opinion held that the 1933 Act is primarily concerned with distribution as distinguished from trading. It further went on to say that the position of the Brooklyn Manhattan Transit Corp. was "wholly untenable" since the adoption of their view would be a simple device of avoiding the registration procedures by making an original sale of a new security issue to one person residing in the same state as the issuer, followed by an immediate interstate distribution. The Commission went on to say this control over the *distribution* was essential and that it is the sales during the distribution which are to be taken into consideration in determining whether the issue is sold only to residents of one state. Thus, the holding in this case would lead one to conclude that the statute does not contemplate control over only original sales by the issuer but contemplates such control over all sales during the course of a distribution. However, the holding also indicates that the statute does not contemplate a consideration of every sale from the issue date to the time when the securities are retired by the issuer. The difficult question is at what point does distribution end and trading begin? "The point at which such distribution is completed is a question of fact to be determined in the light of all the circumstances of the offering."[47]

Fortunately, however, the Commission did suggest some standard on which to determine the point at which the distribution has ended. It said that since the third clause of section 4(1) of the 1933 Act requires the use of the prospectus for a period of one year (this has now been changed by the 1954 amendments to forty days)[48] after

[46] 1 S.E.C. Dec. 147 (1935).
[47] See note 46 *supra* at 162.
[48] 48 Stat. 74 (1933), 15 U.S.C. 77d (1956).

the first date the security was bona fide offered to the public by the issuer or by or through an underwriter, an analogous situation exists in determining when the distribution has or has not ended for section 3(a) (11) purposes. Thus, the inference can be drawn that after a year had expired, a sale by a resident to a non-resident would probably not destroy the section 3(a) (11) exemption.

Since, as stated above, the 1954 amendments changed the one-year period in section 4(1) to forty days, an interesting question arises as to whether the Commission would substitute, for the purpose of section 3(a) (11), the forty day period. Professor Loss says that it does not necessarily follow that this would be the Commission's policy.[49] Although conjecture is of little value, it would appear that the forty day period now found in section 4(1) of the 1933 act will not displace the one-year rule applied in the *Brooklyn Manhattan Transit Corp.* case.

From the foregoing it seems clear that if any underwriter, any distributing dealer, or any dealer purchasing with a view to resale, or even a substantial investor (not a person in the business of buying and selling securities for the account of others), purchased from the issuer, and within a relatively short period of time sold to non-residents, the distribution would still be continuing and the exemption of section 3(a) (11) defeated.[50] It certainly would appear that the development of an interstate market shortly after the initial offering would cast doubt upon the claimed exemption.

Short of this factual situation, as when a small investor resells to a non-resident after some time, more difficulty is encountered. The real question is one of fact to determine whether the securities have actually come to rest in the hands of residents who purchased without a view to further distribution. Once this conclusion is reached, the sales may be made to non-residents without affecting the section 3(a) (11) exemption—*i.e.*, at this point trading commences and the distribution is ended. All the facts must be taken into consideration, *i.e.*, the proximity in time between the purchase and sale, the character of the purchaser, whether he is a professional broker or dealer or merely an investor, and the amount of securities purchased, before we can ascertain whether the distribution has ended.

Unfortunately, no clear answer can be given to determine when a distribution ends and trading begins. All factors must be examined to permit one to conclude that the distribution went to only residents of one state.

B. *Installment Buying of Securities*

As in all other commodities on the market, the installment purchase program has reached securities. Thus, the issue is raised concerning a purchaser of securities on the installment plan who changes his residence or domicile after the original agreement to

---

[49] Loss, Securities Regulation 163, addition to note 248 (Supp. 1955).
[50] SEC, Securities Act of 1933 Release No. 1459 (1937).

buy the securities, but prior to the completion of all his payments. Will the continued acceptance of the payments by the issuer from this non-resident be deemed to be a sale to a non-resident so as to destroy the section 3(a) (11) exemption?

Again, the writer has found no authority to assist in answering this problem. The legal issue would seem to revolve around the terms and conditions of the original subscription agreement. If from a reading of this instrument it can be ascertained that the *total* sale was consummated at the inception, *i.e.*, while the purchaser was a resident, and that the contract was not severable or separable, it would appear that the subsequent move would not vitiate the section 3(a) (11) exemption even though the issuer continued to accept the payments as they came due. However, if it appears that the agreement is severable, so that each time the purchaser remits his payments a new sale is consummated, the continued acceptance of the installment payments would probably destroy the section 3(a) (11) exemption.

Thus, an agreement which sets forth a guaranteed surrender value for the money paid by the purchaser might lead one to conclude that a new sale takes place after each or a number of payments, and that the continued acceptance of the payments from this non-resident might destroy the exemption. Surely it would not be difficult to conclude that a new offer is made each time a payment comes due and a new decision is reached by the investor to purchase or not to purchase. Again, no definitive standard can be outlined but each agreement and case must be examined on an individual basis.

IV. Conclusion

The foregoing has attempted to point up some of the problems which exist in interpreting and analyzing section 3(a) (11). It should be obvious to the reader at this point that in very few instances can definite general conclusions be drawn when studying this section.

Each situation must be taken as an individual one and the problems decided on an *ad hoc* basis. The lack of any judicial decision on this section adds to our dilemma, and some definite standard to guide one's conduct in attempting to utilize section 3(a) (11) of the Securities Act of 1933, as amended, is sorely needed.