



COMPTROLLER OF PUBLIC ACCOUNTS

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Comptroller

September 8, 2004

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OPINION COMMITTEE

The Honorable Greg Abbott
Attorney General of Texas
Post Office Box 12548
Austin, Texas 78711-2548

FILE # MC-43929-04

I.D. # 043929

Re: Whether Section 74.401 of the Texas Property Code permits "private" sale of unregistered stock as required by federal law

Dear General Abbott:

On behalf of the Texas Comptroller of Public Accounts, I respectfully request your opinion whether Section 74.401 of the Texas Property Code, which generally requires public sale of all unclaimed personal property, permits a "private" sale of unregistered, privately held stock shares to qualified institutional buyers as required by federal law. Our office construes Section 74.401 consistent with federal law to permit such a sale.

As you know, the Comptroller is authorized to dispose of unclaimed personal property, including securities, delivered to her pursuant to chapter 74 of the Property Code. With the exception of money and marketable securities, the Comptroller must sell such property in the first instance at a public sale:

(a) Except as provided by Subsection (c)¹ or Section 74.404,² the comptroller shall *sell at public sale* all personal property, *other than money and marketable securities*, delivered to the comptroller in accordance with Section 74.301. The comptroller shall conduct the sale in the city in this state that the comptroller determines affords the most favorable market for the particular property.

(b) The comptroller shall sell the property to the highest bidder. If the comptroller determines that the highest bid is insufficient, the comptroller may decline that bid and offer the property for public or private sale.

TEX. PROP. CODE ANN. § 74.401(a), (b) (Vernon Supp. 2004) (emphasis added).

From time to time, the Comptroller receives unclaimed, privately held shares of stock that would not be properly classified as "marketable securities." Chapter 74 does not define

¹ The Comptroller is not required to offer for sale if the property belongs to a person with an address outside the state or if the probable sales costs will exceed the value of the property. TEX. PROP. CODE ANN. § 74.401(c) (Vernon Supp. 2004).

² The Comptroller must deliver military awards or decorations to the adjutant general's department. *Id.* § 74.404(b).

“marketable securities.” However, the term generally means stocks and bonds that can be readily sold to the public on stock exchanges or over-the-counter markets. *See, e.g.*, BLACK’S LAW DICTIONARY 875 (5ed. 1979). The privately held shares in the Comptroller’s custody are not registered with the Securities and Exchange Commission (“SEC”) and, therefore, cannot be sold on stock exchanges or over-the-counter markets. 15 U.S.C.A. § 77e (West 1997). But under a strict reading of Section 74.401 of the Texas Property Code, the private shares must be publicly auctioned.

An offer by the Comptroller to sell these shares publicly at an auction would, in most instances, violate Section 5 of the Securities and Exchange Act of 1933 (the “Act”), 15 U.S.C. § 77e. *See id.* Section 5 of the Act prohibits the initial issuance and sale by the issuer or resale by a subsequent holder of securities unless the securities are registered by providing that: “Unless a registration statement is in effect as to a security, it shall be unlawful for any person . . . to sell such security . . .” *Id.* Absent an exemption, Section 5 of the Act precludes the Comptroller from reselling the unclaimed, unregistered securities in her possession notwithstanding her duty under chapter 74 to sell such securities to the extent the state may realize revenues from the sale.

As a matter of federal law, the private shares must be sold in accordance with an authorized exception to Section 5 of the Act. There are several exceptions, but the only one available to the Comptroller for the sale of the stock shares here is the section 4(1) resale exception. Section 4(1) provides that “[t]he provisions of section 5 shall not apply to --- (1) transactions by any person other than an issuer, underwriter, or dealer.” *See id.* § 77d. The Comptroller is clearly not an issuer and there are specific exceptions for dealers, so the only relevant question is whether the Comptroller would be acting as an underwriter in reselling the securities at issue here. Rule 144A adopted by the SEC under Section 4(1), establishes a nonexclusive “safe harbor” for resale to “Qualified Institutional Buyers” (“QIBs”). *See* 17 CFR 230.144A (2003) (Private Resale of Securities to Institutions). “Persons selling securities in compliance with Rule 144A who are not issuers or dealers are deemed not to be engaged in a distribution [of securities], and therefore not underwriters, thus exempting such sales from the registration requirements of Section 5 of the [1933] Act.”³ Rule 144A specifies the entities that constitute QIBs, which include large institutions that own and invest on a discretionary basis at least \$100 million in securities of unaffiliated issuers; registered dealers and brokers; investment companies; entities owned by QIBs; and certain banks, savings and loans, and similar institutions. *See* 17 CFR 230.144A (2003). In addition to the QIB restriction, Rule 144A contains other requirements such as the securities eligible for resale and issuer information. *See id.*

Section 74.401 of the Texas Property Code must be construed consistent with the Act and Rule 144A. There are two possible readings of Section 74.401: (i) it may be read to not address the sale of unmarketable securities, such as those at issue here; or (ii) by default, it may be read as classifying such non-marketable securities as “personal property” that must be sold at a public sale.

³ Jeffrey S. Hoffman, *Rule 144 & 144A* 295, 343, in PRACTICING LAW INSTITUTE, UNDERSTANDING THE SECURITIES LAWS (2003).

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In the first instance, because state law does not address the sale of such non-marketable securities specifically, but does generally require that the Comptroller dispose of abandoned or unclaimed property by sale unless it belongs to a person with an address outside the state or its value is commercially insubstantial, then the inescapable conclusion is that the securities must be sold in accordance with federal law, i.e., private sale. *See* U.S. CONST. art. VI, cl. 2 (the laws of the United States "shall be the supreme Law of the Land . . . any Thing in the Constitution or Laws of any State to the Contrary notwithstanding."); TEX. GOV'T CODE ANN. § 311.021(Vernon 1998) (Code Construction Act) (presumes that legislature intended compliance with federal and state constitution, entire statute to be effective, just and reasonable result, and result feasible of execution). This would be consistent with the provisions of section 74.401 of the Texas Property Code that permits the Comptroller to hold private sales if all bids at a public sale are rejected as inadequate. *See id.* § 74.401(b) (Vernon Supp. 2004).

In the second instance, because a sale to the public (as opposed to a private sale to QIBs) of unregistered securities would directly conflict with Section 5 of the Act, Section 74.401 of the Texas Property Code is preempted and ineffective to the extent of the conflict. *See id.*; *Hyundai Motor Co. v. Alvarado*, 974 S.W.2d 1, 4 (Tex. 1998) (federal law may preempt state law expressly or implicitly if federal statute's scope indicates Congress intended federal law to occupy field exclusively or when state law actually conflicts with federal law). Again, the securities must be sold at a private sale consistent with federal law.

We have found no case law or attorney general opinions construing Section 74.401 of the Texas Property Code or addressing the interplay between Section 74.401 and the federal securities law. However, based on the application of established principles of statutory construction, we believe the Comptroller may sell non-marketable securities to QIBs in a private sale without first offering the securities to the general public.

If you have any questions or require additional information, please call me at 936-4446.

Sincerely,



Timothy Mashburn
General Counsel