Ohio Securities Bulletin

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Issue 3 – 1982

CREAGER FOUND GUILTY OF 350 SECURITIES COUNTS

On July 21, 1982, Patric M. Creager was convicted on 401 charges by the Tuscarawas County Court of Common Pleas. In addition to the 350 securities law violations, the jury found Mr. Creager guilty on nine counts of passing bad checks and 42 counts of theft by deception. The conviction concluded a lengthy investigation by Scott Roberts, Staff Attorney at the Ohio Division of Securities.

Most of the charges stemmed from the business transactions of Mr. Creager's company, Creager Enterprises, Inc. Although the primary buisness of Creager Enterprises involved the purchase and sale of gold, silver, coins and collectibles, Mr. Creager also sold promissory notes. Mr. Creager represented to investors that he was investing the proceeds of the promissory notes in the gold and silver market when, in fact, he developed a practice of using the money to pay interest obligations on earlier notes. Promissory notes issued by Mr. Creager were thought to total between six and eight million dollars.

The amount of the notes varied from $1,000 to $900,000 and most notes were payable in thirty days. Interest on the notes was promised at rates up to and exceeding sixteen percent per month.

Many of the investors thought they were the only individuals lending money to Creager Enterprises and most of the approximately 150 investors involved, were residents of the Dover-New Philadelphia, Ohio area.

The investigation began in April of 1981, following a complaint by one of the investors.

During the course of his investigation, Mr. Roberts contacted over 100 investors by personal interview, phone, or by questionnaire/letter and subpoenaed hundreds of documents, compiling significant financial information which was previously unavailable, due to Mr. Creager's failure to keep books and records concerning his financial transactions.

Mr. Creager was questioned at a hearing before the Division and on August 25, 1981, the case was submitted to the Tuscarawas County Prosecutor, Ronald Collins who personally prosecuted the case.

Specifically, the securities violations on which Mr. Creager was convicted, included:

1) Selling securities without being licensed. [1707.44(A)]
2) Selling securities which were not registered with the Division and which were not exempt from registration. [1707.44(C)]
3) Selling securities with the knowledge that the company is insolvent and without disclosing such insolvency. [1707.44(D)]
4) Engaging in an illegal, fraudulent or prohibited act while selling securities. [1707.44(G)]
5) Making a false representation concerning a material and relevant fact for the purpose of selling securities. [1707.44(B)]

On all but eight counts, Creager was placed on probation. Terms of the probation provide that Creager cannot engage in the coin business and cannot borrow money except from commercial banking institutions during the next five years. On the remaining eight counts, Mr. Creager was sentenced to eight to forty years in prison.

The case also received attention because it was the first criminal trial in Ohio to be televised live from beginning to end on cable television. It was thought to be one of the first in the nation to be televised in its entirety.

The case was of particular interest in the Dover-New Philadelphia area and, reportedly, even televisions in the taverns in Tuscarawas County were tuned in to the trial.

The jury trial lasted seven weeks, and was thought to be the longest trial in the Tuscarawas County. The initial estimate indicated the trial cost Tuscarawas County over $20,000 including witness fees, sheriff's costs, and salaries of the county personnel involved in the trial. (Editor's Note: Attorney Scott R. Roberts left the Division's employ in November 1982 to engage in the private practice of law in Worthington, Ohio).

OHIO SECURITIES BULLETIN
Publication of the
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H. B. 822

On November 18, 1982, the Governor signed Sub. H.B. 822 into law. The Bill:

1. Increased the filing fee for §1707.03(Q) filings from $25.00 to $100.00 for the first filing in any calendar year and $50.00 for subsequent filings.
2. Created §1707.03(V) which permits the Division to exempt securities from registration requirements through rule making authority.
3. Reduced the filing fee for registration by description via §1707.06(A)(3) O.R.C. from $200.00 to $50.00
4. Imposed a consent to service of process requirement on registrations by description for out-of-state issuers through amendment to §1707.11 O.R.C.
5. Amended §1707.06(A)(1) to permit filings to be made by corporations which are not incorporated under the laws of Ohio.
6. Amended §1707.06(A)(2) to permit any corporation to register securities to be sold to a maximum of 35 persons, excluding from such limitation any purchaser who is a purchaser of $100,000.00 or more of the offered securities or who is an executive officer or director of the issuer.

Additionally, §1707.06(A)(2) was amended to permit the payment of up to 10% commissions to Ohio licensed dealers.

7. Amended §1707.06(A)(3) to permit any partnership, limited partnership, partnership association, syndicate, pool, trust fund or other unincorporated association to register securities for sale, to a maximum of 35 persons excluding from such limitation any purchase of $100,000.00 or more of the offered securities and excluding any trustee, General Partner, Director or Executive Officer of the issuer.

Up to 10% commission may be paid to any Ohio licensed dealer or salesman in connection with sales under this section.

8. Amended §1707.23(E) to enable county prosecutors to request that the Attorney General prosecute criminal violations of Chapter 1707.
9. Amended §1707.26 to enable the Division of Securities to seek injunctive relief for manipulative acts or practices in violation of Chapter 1707., requires the court to issue an injunction upon proof of violation and empowers the court to order such other equitable relief as the facts warrant.
10. Adopted new §1707.042 for the regulation of "control bids" (defined in §1707.01(V)]. This section was adopted in response to the U.S. Supreme Court decision in Mite v. Dixon which declared the Illinois takeover act unconstitutional. The section prohibits misleading, deceptive, fraudulent and manipulative acts and practices in connection with control bids. Violation is a fourth degree felony. The section contains an implied consent to service of process provision and a severability clause. Civil sanctions are incorporated by means of reference to §§1707.41 through 1707.45 O.R.C.
11. Amended provisions of Ohio Corporate law to provide a procedure for shareholder review of proposed control share acquisitions. Sections 1701.01, 1701.11, 1701.37 and 1701.48 were amended. Section 1701.831 was newly adopted.

These changes would require shareholder approval, prior to consummation, of control acquisitions at the 20%, 33 1/3% and 50% levels of ownership and permit shareholders to adopt a restriction on transfer of shares in connection with control acquisitions.

For the convenience of the reader, some changes to Chapter 1707., O.R.C. which were a part of Sub. H.B. 822 are printed on the following page of this Bulletin.

AVAILABILITY OF COPIES

Copies of Sub. H.B. 822 are available upon request at the cost of reproduction. The fee is $4.00. Direct all requests to Judy Bledsoe.

AVAILABILITY OF FORMS

New forms for §1707.03(Q) filings and registrations by description filings under §1707.05, 1707.06(A)(1), 1707.06(A)(2), 1707.06(A)(3), 1707.06(A)(3) O.G., and 1707.06(A)(4) are available upon request. Please direct all requests to Beth Miller, Division of Securities, Two Nationwide Plaza, Columbus, Ohio 43215.

RULES

The Division of Securities intends to adopt certain rules in connection with the changes implemented by Sub. H.B. 822. Copies of those proposed rules may be obtained upon request directed to Natalie Bissett, Division of Securities, Two Nationwide Plaza, Columbus, Ohio 43215.

THANK YOU'S

From start to finish, Sub. H.B. 822 was a joint effort by the Ohio Bar Association and the Division of Securities. Line by line, word for word, it was a negotiated and agreed bill. Beyond the significance of its changes in Ohio Corporate and Securities laws, its greatest importance may lie in the fact that the Division and Bar Association acted cooperatively to achieve common objectives. The staff of the Division sincerely hopes that this Bill is a harbinger of things to come.

The Division appreciates the efforts of all the members of its Advisory Committees who participated in the shaping of the Bill. A special debt of gratitude is owed to the following listed persons.

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CERTAIN SECTIONS OF CHAPTER 1707 O.R.C. CHANGED BY SUB. H.B. 822

Section 1707.01(V) & (W) (New language)

(V) "Control bid" means the purchase of or offer to purchase any equity security from a resident of this state if after the purchase of such security the offeror would directly or indirectly be the beneficial owner of more than ten per cent of any class of the issued and outstanding equity securities of the issuer.

(W) "Offeror" means a person who makes, or in any way participates or aids in making, a control bid, and includes persons acting jointly or in concert, or who intend to exercise jointly or in concert any voting rights attached to the securities for which such control bid is made.

Section 1707.03(Q)(5) (Amended) (Fee increase)

(5) The issuer pays a filing fee of one hundred dollars for the first filing and fifty dollars for every subsequent filing during each calendar year.

Section 1707.03(V) (New language)

(V) The sale of any security is exempt if the division by rule finds that registration is not necessary or appropriate in the public interest or for the protection of investors.

Section 1707.042 (New language)

(A) No person who makes or opposes a control bid to offerees in this state shall knowingly do any of the following:

(1) Make any untrue statement of a material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they were made, not misleading;

(2) Engage in any act, practice, or course of business which operates or would operate as a fraud or deceit upon any such offeree;

(3) Engage in any manipulative act or practice.

(B) Any person who makes or opposes a control bid to offerees in this state shall be conclusively presumed to have designated the secretary of state as its agent for the service of process in any action or proceeding under Chapter 1707. of the Revised Code. Upon receipt of any such process, together with an affidavit showing the last known address of the person who made or opposed the control bid, the secretary of state shall forthwith give notice by telegraph of the fact of the service of process and forward a copy of such process to such address by certified mail, with a request for return receipt. This section does not affect any right to serve process in any other manner permitted by law.

(C) Any person who makes or opposes a control bid is subject to the liabilities and penalties applicable to a seller, and an offeree is entitled to the remedies applicable to a purchaser, as set forth in sections 1707.41 to 1707.45 of the Revised Code.

(D) In case any provision or application of any provision of this section is for any reason held to be illegal or invalid, such illegality or invalidity shall not affect any legal and valid provision or application of this section.

Section 1707.06(A)(1) (Amended)

(1) The sale of its securities by a corporation may be so carried out when no part of the securities to be sold is issued directly or indirectly in payment or exchange for intangible property or for property not located in this state, and when the total commission, remuneration, expense, or discount in connection with the sale of such securities does not exceed three per cent of the initial offering price thereof.

Section 1707.06(A)(2) (Amended)

(2) The sale of its securities by any corporation may be so carried out when such securities are sold to not more than a maximum of thirty-five purchasers, the aggregate commission, discount, or other remuneration, excluding legal, accounting, and printing fees, paid or given directly or indirectly in connection with the sale of such security does not exceed ten per cent of the initial offering price, and such securities are issued and disposed of for the sole account of the issuer, in good faith and not for the purpose of avoiding sections 1707.01 to 1707.45 of the Revised Code, for the purposes of this division, neither of the following shall be included among the thirty-five purchaser maximum:

(a) Any purchaser of at least one hundred thousand dollars of the offered securities;

(b) Any director or executive officer of the issuing corporation.

Section 1707.06(A)(3) (Amended) (Fee reduced to $50)

(3) The sale of securities representing an interest in a partnership, limited partnership, partnership association, syndicate, pool, trust, trust fund, or other unincorporated association may be so carried out if the securities are sold to not more than a maximum of thirty-five purchasers, the aggregate commission, discount, or other remuneration, excluding legal, accounting, and printing fees, paid or given directly or indirectly in connection with the sale of such security does not exceed ten per cent of the initial offering price, and if such sale is made in good faith and not for the purpose of avoiding sections 1707.01 to 1707.45 of the Revised Code. For the purposes of this division, neither of the following shall be included among the thirty-five purchaser maximum:

(a) Any purchaser of at least one hundred thousand dollars of the offered securities;

(b) Any trustee, general partner, director, or executive officer of the issuer.

Section 1707.06(B) (Amended)

(B) An issuer engaging in any transaction specified in this section shall not be deemed a dealer. Any commission, discount, or other remuneration for sales in this state of securities specified in this section shall be paid only to dealers or salesmen licensed pursuant to Chapter 1707. of the Revised Code.

Section 1707.06(C) & (D) (New language)

(C) For the purpose of this section, each of the following is deemed to be a single purchaser of a security:

(a) Husband and wife;

(b) A child and its parent or guardian when the parent or guardian holds the security for the benefit of the child;

(c) A corporation, a partnership, an association, or other unincorporated entity, a joint stock company, or a trust, but only if the corporation, partnership, association, entity, company, or trust was not formed for the purpose of purchasing the security.

(D) A sale of securities registered under section 1707.09 or 1707.091 of the Revised Code or sold pursuant to an exemption under sections 1707.01 to 1707.45 of the Revised Code shall not be integrated with a sale pursuant to this section in computing the number of purchasers under this section.

ENFORCEMENT

Thomas Lynton Troyer — Criminal Referral

On November 12, 1982, in the Court of Common Pleas of Summit County, Thomas Lynton Troyer, of Stow, Ohio, was sentenced to two to five years in prison for grand theft and unlicensed sale of securities. That term will be served concurrent with a five year federal prison sentence imposed earlier upon Mr. Troyer for violation of federal commodities law.

Between 1975 and May, 1982, Mr. Troyer obtained money from northern Ohio investors for the purpose of dealing in the commodities market. Mr. Troyer did business under the name Commodity Concepts, and investors purchased "units" in Commodity Concepts, Managed Commodity Fund, which was a commodity pool. The "units" in Commodity Concepts, Managed Commodity Fund were securities which were not registered with the Ohio Division of Securities, and Mr. Troyer was not licensed by the Division as a broker-dealer. Thus, the capital formation activities of Mr. Troyer's commodity pool were violative of the Ohio Securities Act.

Mr. Troyer dealt with about 80 investors, who entrusted him with approximately $535,000. Of that amount, $185,000 was returned to investors as dividends and $85,000 was lost in commodities trading. The remainder was converted by Mr. Troyer to his own use.

In negotiated pleas, Mr. Troyer pleaded guilty as charged to one count of federal commodity law violation, unlicensed sale of securities under the Ohio Securities Act, and grand theft under Ohio law.

The Ohio Division of Securities referred its portion of the case to the Summit County prosecutor's office on August 6, 1982. The Division's action resulted from work done on the case by James Lummanick, Staff Attorney.

John Vasi/Joseph Cimino/Commercial Energy, Inc. — Criminal Referral

On June 21, 1982, John Vasi and his nephew, Joseph Cimino were found guilty on six counts each of selling securities without a license. They pleaded no contest to the charges before the Summit County Common Pleas Court. They were indicted on January 28, 1982, on eighteen counts of securities law violations for selling more than $75,000 in unregistered shares of stock to approximately 64 northeast Ohio residents. A pre-sentence investigation was ordered.

On August 9, 1982, John Vasi and Joseph Cimino were each placed on three years probation and ordered to make restitution to the northeastern Ohio investors. A $1,000 fine was imposed. If they violate probation, they would each face six to thirty years in prison.

Vasi and Cimino led investors to believe they were investing in Commercial Energy, Inc., an oil recycling project. They allegedly sold the stock by telling investors that the drums located at the Deerfield Dump, owned by Mr. Vasi, contained oil which could be recycled and sold as fuel.

Staff Attorney Nancy Ivers Ferguson and Investigator Karen Banks handled the investigation in this case on behalf of the Division.

Alan W. Lindsey/The First Columbus Fund — Criminal Referral

Alan W. Lindsey of The First Columbus Fund, was indicted on October 5, 1982 by the Richland County Grand Jury sitting in Mansfield on three counts, two counts of which were for selling unregistered securities and the third for being an unlicensed salesperson in such sales.

Allegedly, Lindsey sold unregistered notes to the public and subsequently defaulted on interest and principal.

Sid Silvian, Staff Attorney, testified before the Grand Jury in Mansfield and prepared the Division's case.

Nicholas A. Ross, Professional Resources Management Corporation and Ohio Resources Management Corporation — Injunction

A default judgment was entered on September 5, 1982, in the Common Pleas Court of Perry County in a pending lawsuit filed by the Division of Securities requesting injunctive and other relief against Nicholas A. Ross, Nicholas A. Ross dba Professional Resources Management Corporation, Professional Resources Management Corporation and Ohio Resource Management Corporation.

The complaint had alleged the failure of Ross and Professional to register and to be licensed to sell security interests in oil and gas wells, known as Lemley No. 1 Well (Vinton County), Harper No. 1 Well (Vinton County), and William J. Davis No. 1 Well (Gallia County). Additional alleged violations of the Securities Act included failure to comply with certain terms of the operating agreement on the Lemley No. 1 Well.

Ross was also alleged to be the sole shareholder of Ohio Resource Management and through that corporation duly registered security interests in an oil and gas well known as ORMC Thompson, et. al. No. 1 Well Joint Venture (Gallia County). The complaint alleged that terms of the offering circular were breached in that some of the investor funds were used to complete wells different from the wells for which the investment was made. All the investors in the wells involved in the suit were Ohio residents.

Ross and the other defendants failed to plead or otherwise defend. The default judgment enjoined the defendants from engaging in any act or practice prohibited by the Ohio Securities Act and from dissipating assets without a court order. Defendants are also to notify investors of rights of rescission under O.R.C. Section 1707.43.

The Division's action resulted from case work by former Division Staff Attorney, David LeGrand.

William T. Bowler

On November 9, 1982, the Ohio Division of Securities issued a Cease and Desist Order against William T. Bowler, doing business as Monton Mortgage Company and Norbert Financial Corporation in the Akron, Ohio area.

Mr. Bowler was found to have sold approximately five different types of securities without being licensed as a securities broker or salesman. None of the securities were registered with the Ohio Division of Securities.

Most of the transactions involved receipt of an advanced fee by Mr. Bowler in exchange for his promise to make a loan to certain individuals or to obtain a lender who would make a loan. The Commissioner found that the loan commitment agreement issued by Mr. Bowler was an "evidence of indebtedness" and thus a security as that term is defined in Section 1707.01, Ohio Revised Code.

Fred Johnson and Elayne Mitchell

The Common Pleas Court of Franklin County on December 2, 1982, upheld the validity of a Cease and Desist Order of the Division of Securities issued on June 29, 1982, against Fred Johnson and Elayne Mitchell and dismissed an appeal therefrom. The decision stated that the Order was "supported by reliable probative and substantial evidence and is in accordance with law." The finality of the order of the Common Pleas Court is subject to appeal to the Court of Appeals.

Both Fred Johnson and Elayne Mitchell were licensed to sell securities in Ohio and were employed by a licensed Ohio dealer. After investigation and upon written advice from the licensed dealer, the Division issued separate show cause orders alleging that securities were sold by each salesperson, with commissions being received, without the express consent of the dealer in contravention of Rule 1301:6-3-03(C)(1) of the Ohio Administrative Code. That rule provides for consent and supervision of the dealer over securities sales by its licensed salesmen. Such actions were prohibited by O.R.C. Section 1707.44(A).

A hearing was requested and held with the Cease and Desist Order being thereafter entered directed against the receipt of unlawful commissions in connection with the sale of such securities. Appeal was taken to the Common Pleas Court of Franklin County.

Scott Roberts, Staff Attorney, and M. Dale Barrett, Investigator, were responsible for the investigation of this case.

Structured Shelters, Inc.

On October 22, 1982, the Division issued an order to Structured Shelters, Inc. of Cincinnati, Ohio, to cease and desist from selling unregistered securities without a salesman or dealer's license in the State of Ohio. O.R.C. Section 1707.44(C)(1), requiring securities to be either registered or be subject to a claim of exemption, was one basis for the order. In addition, the cease and desist order was issued pursuant to O.R.C. Section 1707.44(A) because of failure to comply with sales licensing requirements. No appeal was taken from the order.

The securities transaction subject to the order concerned investment contracts involving the application of precedents established in S.E.C. v. W.J. Howey Co. et. al., 328 U.S. 293 (1946), and related cases. In addition to Ohio, sales were made in a number of other states and included the following four investment programs;

1) The Children's Classics Series
2) The Nitrol Shipping Container Program
3) Preservation Research Ltd.
4) The Free Enterprise Office Tower

Scott Roberts, Staff Attorney, conducted the extensive investigation in connection with this Division Order.

Compow'r Financial

A cease and desist order was issued on August 9, 1982, against Compow'r Financial of Akron, Ohio, for violations of O.R.C. Section 1707.44(A). The order was based on receipt of a sales commission at a time when Compow'r Financial was not a licensed securities broker-dealer. The order was issued following a hearing under the Administrative Procedure Act and no appeal was taken therefrom.

Scott Roberts, Staff Attorney, and M. Dale Barrett, Investigator, directed the investigation which resulted in the issuance of the Division Order.

Financial Alternative, Inc.

On August 17, 1982, Financial Alternative, Inc. of Kent, Ohio was ordered to cease and desist from selling securities without a dealer or salesman's license in contravention of O.R.C. Section 1707.44(A). The action was taken following filing of a Form 3-Q listing payment of a commission to the unlicensed company.

A show cause order was issued advising of an opportunity for hearing to establish that no violation had occurred. No hearing was requested and the final order was issued.

The action by the Division was based on investigaation by Scott Roberts, Staff Attorney, and M. Dale Barrett, Investigator.

Nova Care, Inc., Nova Care Marketing Limited, John M. Seidel

On December 8, 1982 the Common Pleas Court of Franklin County issued an injunction against Nova Care, Inc., Nova Care Marketing Limited and John M. Seidel in connection with sales in 1978 of partnership units in a Cincinnati health care plan. The action was based in part on allegations that the Form 3-Q filed with the Division failed to satisfy several provisions of Ohio Revised Code Section 1707.03 (Q) and thus violated Ohio Revised Code Section 1707.44. The alleged defects included late filing, sales to more than thirty-five purchasers and charging excessive commissions. Another allegation charged that the Offering Memorandum used by the issuer omitted material and relevant information concerning consent orders issued by the Securities and Exchange Commission pertaining to certain principals and active participants in the health care plan.

No pleading or defense was filed and asserted by Nova Care, Inc., Nova Care Marketing Limited and John M. Seidel. The judgment was entered following the filing by the Division of Securities of a motion for default judgment. The judgment is subject to appeal to the Court of Appeals.

The judgment entry provides that Nova Care, Inc., Nova Care Marketing Limited and John M. Seidel are permanently restrained and enjoined from selling the limited partnership interests in Nova Care Marketing Limited and from engaging in any act or practice which is declared to be illegal, defined as fraudulent or prohibited by the Ohio Securities Act.

NOTICES

Public Hearing Re: NASAA "Cheap Stock" Proposal

The Ohio Division of Securities will conduct a public hearing in room 2969 of the State Office Tower on Thursday, January 20, 1983 from 9:00 a.m. to 12:00 noon for the purpose of receiving testimony on the merits of the proposed "Cheap Stock" guidelines of the North American Securities Administrators Association. (See Ohio Securities Bulletin Issue II 1982). Copies are available upon request.

Written comments should be submitted to the attention of Hearing Officer, Greg Zelasko, Esquire.

Testimony and comments received will be transmitted to the appropriate committee of NASAA for its consideration.

Notice of Public Hearing

The Division of Securities, Department of Commerce, State of Ohio, will hold a public hearing at 9:00 a.m. on January 27, 1983 in the State Office Tower, 30 East Broad Street, Columbus, Ohio to consider the adoption of rules relating to the Ohio Securities Act, Chapter 1707., O.R.C.

The proposed rules, as filed with the Legislative Reference Bureau and the Clerk of the Senate, would amend rules 1301:6-3-06, 1301:6-3-03 and 1301:6-3-19 of the Ohio Administrative Code.

These amendments would:

1. adopt certain disclosure requirements in connection with offerings of securities made pursuant to registrations by description.

2. define "date of sale" for purposes of sections 1707.03 (O) and 1707.03(Q) O.R.C.

3. pursuant to 1707.03(V), exempt the sale of certain repurchase agreements and mortgage pool participation units by Banks and Savings & Loan Associations from registration requirements of Chapter 1707.

4. pursuant to 1707.03(V), exempt certain employee stock ownership plans from registration requirements of Chapter 1707.

5. adopt certain rules of conduct for licensed dealers and salesmen and prohibit certain acts or practices in connection with the sale of securities.

Information concerning the hearing, and copies of the proposed rules may be obtained from the office of the Commissioner of Securities, 3rd Fl., Two Nationwide Plaza, Columbus, Ohio 43215, thirty days prior to the date of the hearing. Copies will be mailed upon request as provided in Section 119.03 of the Revised Code.

Financial Structuring of Oil and Gas Programs

AMOUNTS AND FORMS OF COMPENSATION PERMISSIBLE AND/OR JUSTIFIABLE TO THE PROMOTER OF OIL AND GAS VENTURES

by RONALD K. LEMBRIGHT*

This issue's "Perspective" column has been submitted by Ronald K. Lembright, attorney in private practice in Independence, Ohio with Ronald K. Lembright & Associates. Prior to entering private practice, Mr. Lembright was an examiner of oil & gas registrations for the Ohio Division of Securities. He is presently a member of the Ohio State Bar Association Committee on Natural Resource Law, the Ohio Division of Securities Oil & Gas Advisory Committee and the Ohio Oil and Gas Association Legal Committee. The Division invites continued contributions from readers of the Bulletin of articles for publication on a space available basis.

Depending on the background and orientation of the person or entity desiring to promote and syndicate an oil and gas drilling program or venture, the amounts and forms of compensation to be paid to the promoter may vary substantially. Additionally, the number of investors being sought, the size and scope of the offering, and the nature and sophistication of the prospective investors will determine the type of offering which the promoter may be permitted to make. These factors dictate the market in which he will compete and which, if any, regulatory agencies will review the economic terms and conditions of the offering, including compensation, with a view to passing upon their fairness.

Persons wishing to become principals of an oil and gas venture usually evolve from two varied areas of expertise. Each class's background normally compels them to consider their main source of compensation as it relates to the services they have previously rendered.

The first class, for purposes of this discussion, is the person with the technical oil and gas background, familiar with lease acquisitions, turnkey operations, local contract drilling, and production operations of oil and gas wells.

With growth, these companies or persons may find themselves faced with a need to expand their capabilities with additional equipment, employees, or services, and seek to become independent for funding by promoting their own oil and gas ventures. Investor funding is many times the only viable approach to sustain a business oriented towards expanding such operations, particularly in times of tight credit and high interest rates. Consequently, the details of performing the functions connected with and the comprehension of the "venture capital" market are relatively unknown to the oil and gas technician, and the understanding of the forms of compensation or reimbursement of expenses for performing those functions are often treated as minor considerations. Many times, this person does not fully appreciate the actual expenses required to develop and maintain a marketing effort for raising funds, nor the continuing costs of administering the investor funds with the necessary follow-up to keep investors and governmental agencies informed and provided with professionally prepared reports and accounting services. Consequently, they sometimes neglect to take into account the amounts of compensation required to sustain this function.

The second class of promoter is from a background oriented towards promotional activities and fund raising who, for the first time, attempts to perform and function at the operating end of the oil and gas venture. Many times, through lack of experience in that area, they do not have a full appreciation or understanding of the risks inherent in performing some of the operating tasks. These include lease acquisition, well development, well supervision, the hiring of oil field services, and the screening and supervision of the necessary technical consultants required to give the added expertise for success.

In order to be competitive in the first-time promotional activity, either from the "operator" becoming the "promoter", or the "promoter" becoming the "operator", many of these costs or compensatory fees are mitigated or minimized to appear more favorable to investors. This approach can result in the failure to make the necessary compensatory arrangements for providing these services, therefore causing the promoter to either eliminate services or not perform them with the diligence required to maintain a successful operating program.

In a somewhat adversary position, the securities regulator concerned and involved in the review and approval of qualified registered programs, focuses on the promoter's possible attempt to be rewarded for services he will not actually render, or for services which he will render only in a very limited manner while actually hiring the services from independent third parties under subcontracts, and charging those additional costs against the venture's or partnership's general funds. In other words, the venture may be faced with paying excessive amounts of money for the services being performed or paying for the same services twice.

With a view to preventing the sale of what could be considered abusive programs, securities regulators, on a State level, have prepared guidelines for compensation which they will allow to promoters of oil and gas ventures. The type of offering will determine the forms and amounts of compensation which will be allowed under those guidelines.

The purpose of this article is to first review the Ohio Division of Securities' major consideration, known as the "40% Rule", under its adopted guidelines for Ohio programs. Next, an attempt will be made to highlight the North American Securities Administrators Association's guidelines (N.A.S.A.A.) focusing primarily on the area of conflicts of interest. These are also the guidelines adopted in Ohio for programs in excess of five wells, and by several of the surrounding states. For those programs that will not be subject to state examination for fairness, the next concern of this article is consideration of the competitive compensation for what are known as "private placements". The last section of the article is intended to bring to the reader's attention the controversy and vagueness of an area of compensation which is greatly misunderstood by regulators, practitioners, and promoters; that being, sales commissions, as direct and indirect compensation.

Before looking at these areas, a comment with regard to the confusion and miscommunication of the word "compensation" is in order. Many times, both regulators and investors, when speaking to a promoter, use the word "compensation" synonymously with "profit". It is only appropriate in an article about fair compensation to comment that when guidelines are applied by regulators or a program is questioned by investors, an understanding should be reached as to what is meant when using the words "profit", "compensation", "gross profit", or similar terms. Caution should be exercised not to interchange promoter compensation with profit. Frequently, investors and regulators alike tend to view a promoter's compensation as actual net profit. They fail to take into account that the person who is to receive the compensation for the present program, has had to maintain substantial overhead and administrative expenses in order to package and promote the program which he intends to sell, as well as having had to sustain costs and expenses for programs which were unsuccessfully promoted or ultimately rejected by the promoter. Many guidelines speak only in terms of compensation to promoters. Therefore, when speaking of compensation, it should be noted that this does not generally mean the same thing as "net profit", as the actual costs and charges incurred by the promoter are estimated and not known at the time of the offering and, many times, the promoter's participation may result in a loss to him.

Ohio Registered Oil and Gas Offerings

In Ohio, registered oil and gas offerings are subject to fairness determinations and guidelines as published in the Ohio Securities Bulletin, October 1973 issue. In Volume I, No. 2, of Energy Review, Spring, 1982, an article regarding oil and gas registrations was published as written by Mr. James Warneka, Examiner of oil and gas registrations at the Ohio Division of Securities. Mr. Warneka's article listed certain documents and exhibits required to be filed with an application for registration in Ohio, which documents and exhibits would disclose the types of compensation to be paid to promoters, subjecting them to a review for fairness.

The Ohio Division of Securities' guidelines are applied to Ohio programs, where the size of the anticipated program will not exceed the drilling and development of five oil and/or gas wells in the State of Ohio. These guidelines are primarily directed towards working interests programs, but by interpretation and adoption, will be applied for limited partnerships as well.

The standard used in Ohio for compensation to promoters is now commonly known as the "40% Rule". An analysis of this rule can be broken down on a functional basis in determining whether the compensation planned by the promoter is excessive. The total compensation arrangement is based upon the estimated budget costs for the proposed oil and gas wells, and that standard is determined by the submission to the Division of detailed estimates of costs of drilling and completion (including plugging and abandonment if required). Where the cost of the wells provided to the program is on a "turnkey" basis by independent third parties, the determination will be made upon that "turnkey" price. Turnkey contracts by affiliates of the promoter to the program will be subject to a request for budget estimates supporting the turnkey price and disclosing the amount of estimated gross compensation to the promoter or his affiliate for acting as turnkey operator. The examiner will review the submission or turnkey contract for comparison purposes, taking into account the area of development, the specific ramifications on the particular lease or drillsite (depth, etc.), and comparable submissions for operations in the same general geographical area to comparable geological formations.

Once the determination has been made by the examiner that the submission of the budget estimate or turnkey price is fair on a comparison basis, a specific formula is applied to allow for the "aggregate interests" in the well not to exceed a certain dollar limitation. Example: The estimate of the cost of the well is $165,000. The fixed multiplier applied to this amount if 166.67%, so that the aggregate interests in the well cannot exceed $275,000. The "aggregate interests" are comprised of the interests existing in the well, which are similar to those being offered to the investor, meaning that the dollar value of the aggregate interests includes the retained or carried interest by the promoter. This carried or retained interest by the promoter is one of the requirements of the Division's guidelines, and it must be at least 1/8th interest in the wells of the program. If the promoter wishes to sell 7/8ths of the well to the investors, and he charges $34,375 per interest sold "publicly", the amount of the offering would be $240,625. However, the aggregate interests in the well would be $275,000, which includes the monetary value of the promoter's interest. Therefore, the maximum allowable compensation, based on the 40% permitted under the published guidelines, is 40% of $275,000, or $110,000. This maximum allowable compensation is also to include the value of the interest being retained by the promoter, i.e., $34,375. In the instant case, the remaining $75,625 may be paid to the promoter or his affiliate in the form of cash. The calculation of this allowable cash compensation includes the estimated gross profit that the promoter or his affiliate expects to obtain from the turnkey drilling contract.

Also included in this calculation are any sales commissions, if the promoter or his affiliate are appropriately licensed, up to a maximum amount of 15% as allowed under Ohio law by interpretation. The statute states specifically that at least 85% of the proceeds must remain available to the issuer for the purposes of the offering; thus, the conclusion that a maximum of 15% is allowable for sales commissions and expenses. (O.R.C. 1707.09(J)).

The balance of cash compensation to the promoter may be in the form of management fees under the well estimates, or management fees paid to general partners in partnership programs.

A form of compensation to promoters that comes under particular scrutiny by the Ohio Division of Securities involves overriding royalty interests to be retained by promoters for leases held by them prior to formation of the venture or partnership. A standard has been provided indicating that if the promoter, issuer, or affiliate has maintained the lease in his inventory for at least three years, and the amount of override to be paid is competitive and comparable to that which is being provided from other oil and gas leasing companies, it may be allowed, even though the form of compensation is not on a comparable basis to that provided to the investor. The overriding royalty interest is treated at a greater value than the retained working interest or carried interest, and the minimum dollar amount attributed by the examiner to this override is at least twice that attributed to a working interest. Nevertheless, overrides, not only in Ohio but in other states, are looked upon with special scrutiny and disfavor.

Ohio's rules of fairness may be applied to limited offerings which are registered under what is known as "registration by description" under O.R.C. 1707.06(A)(3).

Should the proposed offering contain a use of proceeds which will be applied to the anticipated development of more than five wells, or to a non-Ohio drilling program, the Ohio Division of Securities will apply the N.A.S.A.A. guidelines for oil and gas programs. A non-Ohio drilling program is one in which the wells are to be developed outside the State of Ohio and would not be considered comparable or similar to the Ohio geological formations known as the "Clinton" or "Berea". In the area of compensation, the main difference between Ohio's and N.A.S.A.A.'s guidelines, deals with the functional sharing arrangement and in overall terms of fairness, the N.A.S.A.A. guidelines delve further into the potential self-dealing of the larger program with its promoter, general partner, or joint venture manager. Without going through each specific type of compensation outlined, permitted, or disallowed, the most scrutinized area involves conflicts of interest with the sponsor or promoter of the program.

Highlights of N.A.S.A.A. Oil and Gas Guidelines — Conflicts of Interest

The North American Securities Administrators Association, in executive session, September 22, 1976, and by amendments on October 12, 1977 and October 31, 1979, adopted oil and gas guidelines which are now utilized by many states' regulators. The allowable promotional consideration permitted to a sponsor or promoter of an oil and gas venture under these guidelines is based upon either a functional allocation or a subordinated interest benefit. The variations and specific limitations are set forth in those guidelines, and should be reviewed prior to preparation and filing of the offering circular. (CCH Paragraph 5222). Although it is possible that a state following the guidelines as adopted, may modify their application with proper supportive evidence as supplied by a sponsor, substantive compliance will still be required. However, in some states these guidelines will be strictly enforced.

In addition to the compensatory provisions of the guidelines, restrictions are imposed regarding areas where the regulators may deem a conflict of interest exists with the program's sponsor in transactions to be undertaken by the venture or program. Specifically, transactions with affiliates regarding the sale and purchase of partnership properties, oil and gas prospects, drillsites, etc., are closely scrutinized and subject to strictly applied conditions. For example, the sponsor of a program, in order to transfer or convey the oil or gas interest to the program, must disclose that fact in his offering circular or prospectus, and whether or not it will be sold from an existing inventory. If it is sold to the program, it must be at cost unless the seller has reasonable grounds to belive the cost is more than the fair market value of the property, in which case, the price to the program cannot exceed its fair market value (emphasis added).

The sponsor transferring an oil and gas interest to his program, must at the same time sell to the program an equal proportionate interest in all his other property in the same prospect. The sale or transfer of less than all of the interest owned by the sponsor to the program or venture is prohibited unless that interest retained by the sponsor is a proportionate working interest, and the obligations of the sponsor that attach to the retained interest are substantially the same as those of the program after the sale of the interest by the sponsor. Also, the sponsor's interest in the revenues cannot exceed the amount proportionate to his retained working interest.

The sponsor is not permitted to retain overrides or other burdens on the interest conveyed to the program, and may not enter into any farmout agreements with respect to his retained interest, except to non-affiliated third parties or other programs managed by the sponsor.

With regard to production purchasing programs, other considerations for sponsor's compensation are involved and should also be reviewed carefully prior to structuring.

There are certain restricted and prohibited transactions by a sponsor during the existence of the program, so the flexibility that a sponsor or promoter may have in connection with lease inventories, farmouts, farm-ins, and sales or transfers to the program are severely limited and instances of self-dealing are viewed with disfavor without adequate protection or restrictions to prevent excessive compensation or benefits to the program's sponsor.

Unlike Ohio, many states have not separately adopted their own guidelines, and tend to follow the substantive portions of the N.A.S.A.A. guidelines with possible variations. Ohio's neighboring states, Pennsylvania, Indiana, and Michigan fall into this category.

The promoter, then, is confronted with the issue of in which states he intends to undertake his selling efforts. If in more than one state, he must structure his program so that in each of the areas where compensation is to be allowed or reimbursement of expenses is to be made, each state's guidelines relating to those restrictions or limitations are followed. Variance from these guidelines, although possible, will depend on the flexibility of the examiner and the state's position on strict adherence to the published limitations and conditions, and would require, most probably, substantive supportive evidence as to why such a variance was undertaken. The ultimate objective of the examiner is to obtain for the investor substantially the same benefits and terms which are intended to be provided by compliance with those guidelines.

Private Offering Exemptions or Limited Exemptions — Not subject to examination or review by regulators.

If the proposed program of the promoter is not to be a registered offering subject to review and examination, the issue to be confronted and resolved by the promoter is: How much should the promoter be paid for the program as its sponsor and principal. The answer may be best determined by what services and functions the promoter is actually going to perform throughout the program, what experience he has had in these areas and what others with similar experience are charging for the same services. Some of the questions and considerations that may be proferred by informed investors or their representatives will seek to ascertain the education, background, experience, and expertise of the person performing the functions for which they will be paid. Even so, the promoter who is venturing for the first time into oil and gas operations, would do well to consider those charges being made by experienced persons with a substantial history of providing those services, and offer to perform the services at prevailing rates. Arbitrarily reducing prices against experienced operators could be a pitfall of the promoter and possibly the deal. Inadequate pricing can cause losses to the person performing the services, possibly causing his business failure, or in the lease, causing that promoter to not fully perform the services as represented because of inadequate incentive.

On the other hand, if the promoter states in his offering material that he will be compensated for providing certain services, when in fact, investigation and questioning will reveal he is actually subcontracting those functions and acting as a broker for those service, the collective amounts paid to the subcontractor and promoter, representing that he is performing the function, may appear to be excessive. In Ohio, a promoter charging a well supervision fee of $600 per month per well was deemed to be charging an excessive fee, particularly when the actual cost of a pumper was not included, which cost was added on at $150 per month per well.

With regard to both private and public offerings, the promoter should review the nature of services required to be rendered in connection with the program from start to finish. A checklist of functions required to be performed for the venture is a helpful safeguard for the delegation of authorities, responsibilities, and estimates. The checklist should start with the due diligence review and site selection for lease acquisitions and continue through the requirements for accounting and reporting services to be performed every year on behalf of the venture or partnership, once it is operating. It should be remembered that each time a function is provided by an outside party, who also expects to operate at a profit, the compensation and/or cost to the program increases. There are occasions when the promoter, by the nature of his operations, can provide services to the program at his cost. This obviously gives the competitive edge to that promoter who is able to do so. However, to be on a firm basis in deciding whether to render services to the program at cost, the promoter performing the service must have available accurate cost records of his operations to know for certain that he is able to provide such services at cost while being fairly compensated in other areas. Otherwise, that promoter may appear to be making money for his company, but subsequently determine that the cost of providing those services is greater than expected and, therefore, that he is actually incurring losses.

The Dilemma of Selling Commissions, Selling Expenses, Finders' Fees, and Similar Types of Compensation

A specific area of compensation which warrants separate discussion because of present concern involves payments to promoters or their affiliates which could be interpreted to be in connection with the sale of securities, and deemed to be commissions. Cash commissions paid to promoters or their affiliates, and specified as such for selling the securities, are easily identifiable and present no problem for interpretation. The caution to a promoter or affiliate receiving such compensation is that most states' laws require that person to be licensed as a securities salesman.

In Issue 2 — 1982 of the Ohio Securities Bulletin, the Ohio Division of Securities published an article written by Joseph C. Long, Professor of Law at the University of Oklahoma and Special Counsel for N.A.S.A.A., Inc., (Copyright 1982 by Joseph C. Long) in which specific discussion centered on the uncertain area where remuneration takes forms other than direct cash payment, and can conceivably be connected more directly with sales activities rather than other promoter functions. Professor Long points out the extreme Michigan case of Prince vs. Heritage Oil Company, 311 N.W. 2d 741 (Mich. App. 1981), whereby the promoter of an oil and gas tax shelter was deemed to have received indirect remuneration for the sale of the oil and gas interests by retaining his carried interest in the wells, a normal oil and gas promoter's participation. As it relates to the Ohio guidelines, the promoter of an oil and gas venture is required to retain such an interest to give him the same incentive that the investors have in seeing the well produce successfully. Under the Ohio guidelines, this form of compensation is appropriately counted as part of the promoter's overall compensation allowed in the above-described 40% Rule. However, serious concern relates to the idea or implication that because the promoter receives or retains such an interest, it is indirect remuneration for "sales" efforts rather than for his function as promoter and, therefore, retaining such an interest may require that he be a licensed securities salesman.

Other states have been more specific in treating the promoter as receiving indirect sales remuneration when he receives profits on services provided to the program in excess of those normally charged. In certain states, any payment made to a person connected with a program or venture, based upon a percentage of funds raised from investors, may be deemed as selling commission. Some states even indicate that the promoter selling his own deal, although being compensated for other functions such as management fees, will only be so compensated as a result of his own sales efforts; therefore, any compensation or part thereof is attributable to sales efforts.

The key to the determination of whether the consideration or remuneration is attributable to sales efforts seems to turn on whether the amount being paid to the promoter for the activity designated, such as management fees, is extraordinary or excessive to that which is normally charged by third parties performing the same basic functions in the same geographical areas.

Naturally, the factual situation regarding the activities of the promoter and his background, experience, and expertise will strongly indicate for what purpose the promoter is being compensated. If his forte is in the area of marketing and sales activities, although his compensation is labeled as a management fee, some regulators would want to attribute a portion of that management fee to his sales activities because basically, this is where he would normally direct his efforts. Alternatively, the promoter whose background is oriented towards operations and technical expertise should be deemed to be receiving compensation for those activities.

To label arbitrarily compensation or remuneration paid to a promoter as paid in connection with the sale of securities would be an inconsistent position and an obstacle to the present trend of encouraging small issuers to raise venture capital funds, as presently set by the S.E.C. (Energy Review, Volume I, No. 3, Summer, 1982). Compensation or remuneration inappropriately charged as sales commissions place a substantial additional burden upon the promoter by possibly requiring him to become a licensed broker-dealer in the jurisdiction where sales are made. Additionally, the benefit of certain states' registration exemptions may not be available because of a requirement that there be no sales commissions paid, direct or indirect.

The dilemma continues and the arguments will most likely be resolved by specific fact situations rather than by standardized law, but the promoter is cautioned that this area of compensation, either paid to him or his affiliates or even paid to third parties, could render this position more vulnerable for disallowance of either the compensation or a registration exemption.

Summary. There are many detailed specific areas of compensation, reimbursement of expenses, and remuneration that the oil and gas promoter is likely to consider and determine whether appropriate. Equitable differences exist between the legitimate promoter attempting to be justly compensated for services he renders, in good faith and after the incurring of expenditures, and the regulator seeking to stop the unscrupulous promoter from paying himself excessive amounts by self-dealing. Indeed, there are promoters who have taken substantial amounts of money for services never performed and in some instances, for wells which were never drilled. Most of those circumstances constituted fraud. Nevertheless, there are genuine ambiguous areas involving compensation and its regulation. So long as legitimate promoters are able to substantiate their costs of doing business, be willing to display by disclosure their reasonable gross profit, and regulators approach their duties with openmindedness, flexibility, and good judgment, the oil and gas industry should be able to raise venture capital funds, and develop economically viable programs for the investor. Regardless, it will be the duty of these promoters, their counsel, and all persons participating in the planning and preparation of the venture to set and maintain equitable standards.

USE OF PROCEEDS

by Clyde C. Kahrl

The recent surge of the stock market has brought about a rush to market by a number of non-public companies with recent histories of significant revenues and profits. (Many of the companies are in the computer software, service, and marketing industries.) At a certain stage of development, promoters will take a company public, to free the corporation from the financial limitations of being a closely held corporation and to obtain a large capital gain by selling shares at premium prices. In the haste to take advantage of market conditions, promoters will often seek more capital than the corporation can effectively employ. Consequently, the stated use of proceeds could often be summarized as: "We don't know." The "catch words" for the above thought are:

1. "Additions to working capital;"
2. "Possible acquisitions of businesses;"
3. "General corporate purposes."

Often, the use of proceeds section is qualified by stating that: "Pending use, the proceeds will be invested in short-term, high-grade, interest bearing securities." (This qualification raises some concerns regarding possible applications of the Investment Company Act of 1940.)

This trend toward sterilization of the "use of proceeds" section is particularly disturbing because the purpose of such a section is to provide the offeree with a conceptual basis for a projection of future earnings. When intended uses of capital are undisclosed, this kind of analysis is impossible. Allocation of proceeds to "general corporate purposes and working capital" implies that the issuer can absorb and effectively employ the capital to the same degree of profitability as it has in the past. When relatively massive amounts of new capital are sought, the issuer's ability to use such capital effectively is open to serious question.

In arriving at a determination as to whether such capital can be effectively employed, the Division examines:

(a) magnitude of asset expansion resulting from the offering;

(b) ratio of capital to non-capital costs;

(c) dilution of public shares;

(d) nature of the product market; including market share, market niche, possible geographical market expansion and diversity of product lines;

(e) flexibility of the product mix.

These five factors are highly inter-related and cannot be viewed in isolation. They form the analytical hub for determining whether the issuer can effectively expand into a large public company. While virtually any firm can expand ten to twenty percent, few if any have the available excess labor, management, or market to expand by factors of two, three, or four within a short time.

The most critical factors in this analysis are available market and available expertise. Without a market one cannot sell, without expertise one cannot build. Market research becomes critical when a firm has a narrow product line or a rigid product mix. Management expertise becomes critical when a firm has a service or marketing orientation, or is technology or labor intensive.

The Division objects, upon a disclosure basis, to the unspecified use of massive amounts of capital. The standard instructions for filing under the Securities Act of 1933 and the Securities and Exchange Act of 1934 are found in Regulation S-K, 17 C.F.R. §229 (1982). The provisions discussing the standards for use of proceeds are found in Reg. §229.504, 5 Fed. Sec. L. Rep. (CCH ¶71,054 (4/21/82). The general rule is: "State the principle purposes for which the net proceeds to the registrant from the securities to be offered are intended to be used and the approximate amount intended to be used for each such purpose. Where registrant has no current specific plan for the proceeds, or a significant portion thereof, the registrant shall so state and discuss the principle reasons for the offering." The thrust of this provision is that the reason for the offering must be stated.

The Ohio Guideline regarding use of proceeds is: "A proposed public offering of the equity securities of a promotional company is considered to be grossly unfair to public investors under this standard if the issuer intends to allocate and use in its business enterprise more than twenty-five percent (25%) of the aggregate net proceeds of the offering for working capital or other unspecified purposes." Ohio Securities Bulletin, June, 1973, at 14; See, Excerpts from the 1973 "Ohio Securities Bulletin" Section III. (B), at 7 (available from the Division at $2.00 per copy).

Taken together, these two standards reject the notion that the statements (a) "working capital and general corporate purposes" or (b) "we don't know," constitutes disclosure of the use of proceeds.

Before registering securities for sale in Ohio, the Division must affirmatively find (among other things) that "the plan of issuance and sale of the securities referred to in the proposed offer or disposal would not defraud or deceive, or tend to defraud or deceive, purchasers . . ." (O.R.C. §1707.09) Accordingly, issuers are cautioned that inadequate disclosure of "use of proceeds" may cause denial of applications for registration.

REGISTRATION BY COORDINATION
Continuation of the Policy Statement On Shelf Registration

In the previous Ohio Securities Bulletin, Issue 2, 1982, the Division adopted a policy statement with respect to shelf registrations that are filed with the Securities and Exchange Commission in accordance with Rule 415. The SEC voted to extend the period of effectiveness of Rule 415 until December 31, 1983. Likewise, the Division has decided to continue its present policy on shelf registrations, with one change, until December 31, 1983.

Because it has been shown to be impractical to require the filing of the final documents at least two business days prior to entry into the market, the Division's policy statement has been altered to require such filing simultaneously upon entry into the market. The policy statement, with the substantive modification underlined, is as follows:

Only those registrants which qualify for filing a Form S-3 under the Federal Securities Act will be able to qualify for an Ohio shelf registration. The Division will not grant a shelf registration to registrants which are required to file Federal Forms S-1 or S-2. The Division will grant a two year period of effectiveness for qualifying shelf registrations.

The shelf registration statement shall be filed pursuant to Ohio Revised Code (O.R.C.) Section 1707.091. The information provided must be sufficiently definite and complete so as to enable the Division to adequately review the registration statement. The registration statement shall be deemed sufficiently definite and complete if all information concerning the registrant and material terms of the transaction are submitted and the only open items are price, interest rate and underwriter's compensation. As required by O.R.C. Section 1707.091(C)(3), the maximum offering price or the maximum interest rate and the maximum underwriting commissions must be specified before the registration statement can be declared effective. If the securities sought to be registered pursuant to the new shelf registration process are debt securities, the registrant may specify up to six alternative types of debt financing plans and indicate the impact of each upon the issuer. To minimize complexity of the offering document if there are more than six different forms of debt financing plans, a separate primary registration statement shall be prepared and submitted for additional financing plans in excess of six.

The fees for shelf registrations shall be determined as provided for by O.R.C. Section 1707.091(C)(4) and shall be paid at the time of the initial registration. The fee shall be based upon the aggregate dollar amount of all securities which are anticipated to be sold within the two year period for which effectiveness will be granted.

The Division Order granting effectiveness to the shelf registration will recite that the Division has made the following findings:

1. That the business of the issuer is not fraudulently conducted;
2. That the proposed offer or disposal of securities is not on grossly unfair terms;
3. That the plan of issuance and sale of the securities, referred to therein, would not defraud or deceive, or tend to defraud or deceive purchasers.

Registrants are cautioned that during the period of effectiveness there exists an obligation under Rule 1301:6-3-09 (H) to notify the Division of any material change, including the following changes:

1. Any material adverse change in the financial condition of the issuer;
2. Any material change in the compensation agreement between the issuer and a dealer licensed to sell its securities;
3. Any material change in the proposed use of proceeds;
4. The occurrence of any event or series of events which has caused any statement contained in the prospectus or offering circular to be false or misleading in any material respect.

If a registrant is required to notify the Division of a material change in accordance with Rule 1301:6-3-09(H), the registrant will be required to request a written confirmation of continued effectiveness five business days before entry into the market.

<u>Simultaneously upon entry into the market</u>, the registrant will be required to file with the Division all post effective amendments, stickered supplements and a copy of the registrant's most recent forms 10K and 10Q not already submitted. The registrant shall state that there have been no material changes within the ambit of Rule 1301:6-3-09(H). The registrant shall notify the Division by telex or graphic scanner each time a block of securities is sold.

A registrant that qualifies for a shelf registration under Rule 415 but not for Ohio shelf registration must file with the Division in the same manner as any other non-shelf registration. The registrant must file another U-1 with accompanying exhibits and filing and qualification fees, each time a block of securities is offered or sold. The Division Order will specify a period of effectiveness for the block of securities registered only on those terms and at the price specified.

OHIO SECURITIES CONFERENCE, OCT. 14, 1982 CONFERENCE SPEAKERS

Nina Klarich

The conference luncheon speaker was Ms. Nina Klarich, the Vice-President and chief regional economist for the First National Bank of Chicago. Ms. Klarich obtained a Bachelor of Science degree from the St. Louis University, a Master of Arts degree from Boston College and a Masters in Business Administration from the University of Chicago.

Ms. Klarich's message was that while the recession on a national basis may be ending, the great lakes region will continue to experience economic misery and is not poised for a significant take-off in the near term. This region of the country has been hardest hit by the recession and has experienced the highest jobless rate primarily because of its dependence upon durable goods manufacturing, particularly the automobile, glass and steel industries. As the national economy continues its shift from a goods producing economy to a service economy, this region will continue to experience a loss of jobs and an outward migration of its labor force.

Despite a relatively slow regional population growth and relatively modest increase in its labor force, the regional economy has not created new jobs at an adequate pace to absorb new entrants into the labor pool or those made jobless by declining manufacturing. As an example, she noted that Ohio has experienced a loss of 276,000 goods-producing jobs during the past year while creating only 99,000 new jobs in the service industry.

Although she forsees manufacturing to rebound during the next few years, manufacturing related employment in the region may never reach the level of a few year ago. To prosper, the region must tap its relatively well educated work force and educational and scientific strengths to develop sufficient numbers of service economy jobs and high technology industries.

Marc Morgenstern

In his presentation, Marc Morgenstern stated that, the extraterritorial application of the federal securities law is an evolving concept, the principals of which continue to be defined and redefined by courts as new factual patterns emerge. An extraterritorial securities sale is one in which facets of the transaction take place outside of the United States. The Securities Act of 1933 defines interstate commerce to include commerce between a foreign country and a state, territory or District of Columbia. Accordingly, the registration provisions of Section 5 of this Act are by their terms applicable to public offerings of securities in the United States by foreign issuers which "use any means or instruments of transportation or communication in interstate commerce or of the mails".

For those United States issuers selling securities abroad, the SEC states in Securities Act Release No. 4708 that even though the use of jurisdictional means may be involved in an offering whereby a United States issuer sells securities to foreign investors, the SEC would not take action against such issuers for failing to register the securities, so long as the offering is made under circumstances reasonably designed to preclude distribution or redistribution of the securities within, or to the nationals of, the United States.

Mr. Morgenstern also discussed under what conditions United States courts have asserted subject matter jursidiction over an extraterritorial securities transaction and have applied Section 10(b) of the 1934 Securities and Exchange Act and Rule 10(b)(5) to such transactions. A leading case on this point is Bersch v. Drexel Firestone, Inc., 519 F. 2d 974 (2d Circuit 1975). In this case Judge Friendly applied the antifraud provisions of the federal securities law to securities sales made by a foreign issuer to American residents in the United States irrespective of whether fraudulent acts (or a culpable failure to act) occurred in this country and also to securities sales made by a foreign issuer to American residents abroad, if the fraudulent acts (or a culpable failure to act) occurred in the United States.

C. A. Peterson

C. A. Peterson, Executive Vice President of The Ohio Company discussed the realm of successful investment products to be offered in the 1980's. While giving no endorsement to any particular product, Mr. Peterson outlined the key beneficial elements provided by investment products, and what factors shape the composition and packaging of these products.

The investment banker has always, and will always, sell three basic products: 1) income, 2) growth, and 3) tax postponement or avoidance. The key to finding the appropriate investment vehicle is determining the balance between the investor's greed and fear. This balance is dependent upon who is the investor. The maturing of the baby-boom generation and the explosion of the number of aged in our society would suggest a bifurcated investment consumption market because of the substantially different needs of the young and the aged. How these groups wish to invest will be based upon the real state of the economy (which has absorbed more than 7 million new workers over the past five years while 11 million are still out of work) and upon the perceived state of the economy (which is dramatically influenced by the press and the White House). Perceptions will always lag events, thus, the majority consensus will rarely illuminate the correct state of affairs.

Successful innovation in investment products is usually based upon government action. Money market funds are a direct result of government regulation of the banking industry. Many new investment products will be created in response to government action.

Projecting slow growth and subsiding inflation, Mr. Peterson sees little change in actual investment products in the 1980's but substantial changes in the delivery systems. A deregulated banking industry will not be a large factor immediately because of the unfamiliarity of bankers with marketing skills. Hybridization of services – banking, insurance, investment, credit – is the current trend.

John Evans

Mr. John Evans, of Graydon, Head & Ritchey spoke on the legal considerations encountered by banks in providing financial products and services to its customers.

By way of history, Mr. Evans pointed out that prior to the depression the American banking industry and the security industry worked hand-in-hand. After the stock market crash, legislators were aware of the many abuses of this closeness of functions and enacted legislation which attempted to protect not only the state of the economy but also the integrity of the institutions.

Today, new legislation has emerged which will presently allow banks to co-exist or compete with the securities industry resulting in a greater spectrum of financial products and services to the public.

Byron Krantz

Byron Krantz spoke on "Limited Partnership Law, New Proposals-Old Problems". He pointed out that the first limited partnership law was enacted in New York in 1822, amended somewhat in 1828 and copied word for word by Ohio in 1846. The Uniform Limited Partnership Act with a few minor differences was enacted into Chapter 1781 O.R.C. in 1957. After discussion of the advantages of the limited partnership form of business, Mr. Krantz suggested that the Act should be reviewed prior to drafting a limited partnership agreement as many agreements in circulation today violate the Act.

The many considerations necessary to formation were covered. A very comprehensive outline was included with the conference materials.

A limited partnership must file a certificate in the office of the County recorder where the principal place of business is located and every other county in which the partnership has places of business. Fourteen points must be covered by this certificate. O.R.C. Section 1707.02(A) prescribes the requirements.

A large measure of his presentation was spent discussing the danger of ignoring the Uniform Partnership Law and how its various provisions should be dealt with when drafting a limited partnership agreement. To avoid making the limited partners jointly and severaly liable, as in one agreement filed last year, or some other omission or mistake, the statute should be thoroughly examined.

N. Beverly Tucker

Mr. N. Beverly Tucker, Jr., Senior Vice President of The Fifth Third Bank of Cincinnati, Ohio, described the trend of banks becoming increasingly involved in the securities business, primarily due to the substantial loss in deposits to money market funds. Hence, the banking industry is anxiously awaiting the President's signature upon the Depository Institutions amendments of 1982 which will allow banks to offer to their depositors a competitive product. The computerization of the banking industry will enable banks to "sweep" accounts nightly and transfer excess funds into their product.

Mr. Tucker sees no reason why this recent trend of banks offering securities "services" to their customers should not continue, particularly since banks enjoy a distinct advantage over dealers in terms of purchaser convenience and familiarity with the investing public.

Donald Antrim

Complex securities litigation is not for the novice or the weakwilled. That was the principal message of Donald Antrim of the Columbus law firm of Carlisle, Patchen, Murphy & Allison. Mr. Antrim, who spent many years with the Ohio Attorney General's office litigating such matters on behalf of the Division of Securities before entering private practice, offered a number of suggestions to would-be litigators in this area.

The most important point for the lawyer to recognize, according to Mr. Antrim, is that securities litigation is a highly technical practice, which can quickly become both time-consuming and expensive. Mr. Antrim urged litigators to team up with corporate law specialists and to have adequate support staff lined up before even commencing action.

The plaintiff's litigator should also realize that success in such actions is tied directly to speed and anticipation of the other side's moves. Mr. Antrim advised that all research and pleadings be completed before the complaint is ever filed, and that discovery demands accompany the complaint. In most such litigation, time is critical. The key to success, said Mr. Antrim, is to recognize and anticipate pitfalls at the earliest possible time.

Nodine Miller

Nodine Miller of the law firm of Zacks, Luper & Wolinetz Company began the afternoon program with an introduction to commodities regulation. Following a brief history of the applicable federal statutes, Ms. Miller reviewed the specific commodities regulated and identified those individuals participating in the sale of commodities who must be registered with the CFTC.

Ms. Miller also discussed various remedies for investors who are defrauded in a commodities transaction and reviewed the occasionally overlapping jurisdictions of the SEC, Ohio Division of Securities and the CFTC.

R. Jeff Andrews

R. Jeff Andrews, Director of Regulatory Affairs for The Deltona Corporation, spoke on the topic of real estate time-share programs. He noted that Florida has by far the most time-share units in the United States. After offering a brief description of the typical time-share buyer, he described the Florida time-share statutes, specifically addressing both the strengths of the statutes (such as requiring a management entity with fiduciary responsibility) and the greatest weakness (the cooling off period may be waived by the purchaser). He also explained some of the problems with time-share exchange programs, noting that such programs are in their infancy and are unregulated. In concluding, he noted that Florida had taken its time-share act from a model act and that given its experience in this area, other states proposing such an act would be wise to tap that experience.

STAFF CHANGES

Kenneth Krouse – After serving as Commissioner of Securities from July 1, 1979 to July 15, 1982, Kenneth E. Krouse resigned to accept appointment as Superintendent of Banks within the Department of Commerce.

Charles McClenaghan – In September, 1982, Attorney Charles McClenaghan was appointed Commissioner of Securities. He formerly served as Superintendent of Real Estate within the Department of Commerce.

Scott Roberts — Enforcement Staff Attorney, Scott Roberts resigned from his employment with the Division of Securities in 1982 to enter the private practice of law in Worthington, Ohio.

Donald E. Meyer — On December 31, 1982, Registration Attorney, Donald E. Meyer will terminate his employment with the Division of Securities to accept a position with the law firm of Cravath, Swaine & Moore in New York City.

Michael Miglets — On November 24, 1982, Attorney Michael Miglets began his employment with the Division of Securities, in the Enforcement Section.

—IN MEMORIAM—

With the untimely death of Joan McGowan Page on December 9, this Division sadly bid farewell to one of its outstanding employees of twenty years of dedicated State service.

JOAN PAGE

Lovely lady, exemplary mother, able worker and valued colleague, completed her wrestle of life with honor and class.

All of us who knew her are the better for the experience.

We say goodnight with love and respect.

"Age is the mind's one movie,
telling the bones where they've been,
it's how the genes wind on the reals.
God watches and loves the show".

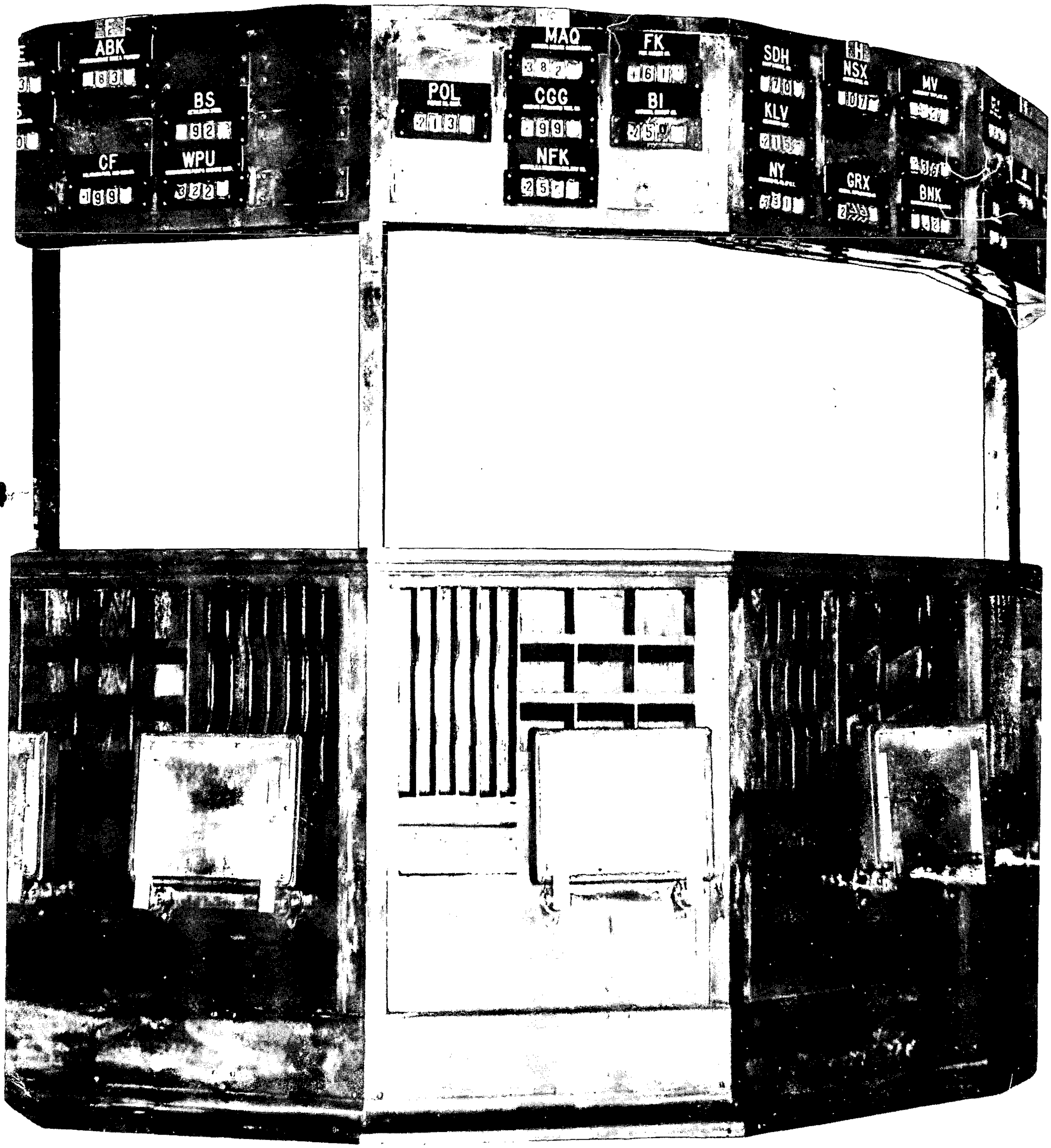
Kenneth K. Krouse with and for a host of friends and fellow workers. Superinendent of Banks, formerly Commissioner of Securities, Department of Commerce.

STATE OF OHIO
DEPARTMENT OF COMMERCE
DIVISION OF SECURITIES
Two Nationwide Plaza - 3rd Fl.
(Corner Chestnut & High Sts.)
Columbus, Ohio 43215
Equal Opportunity Employer

THIRD ANNUAL

OHIO SECURITIES CONFERENCE

COLUMBUS – THURSDAY – OCTOBER 14, 1982



PICTURED ABOVE: A Booth at *The New York Stock Exchange* - Compliments of *COSI*

ABOUT THE CONFERENCE

On October 14, 1982, the Ohio Division of Securities will hold its 3rd annual securities conference at the Hyatt Regency Hotel in Columbus.

The division's advisory committees will meet in the morning at 9:30 a.m. and the conference program will begin with the luncheon at 11:30 a.m.

The luncheon speaker will be Nina Klarich, Economist, First National Bank of Chicago on the subject of the general economic outlook for the Midwest for the next 18 months.

The afternoon program will cover a wide range of topics and speakers, as outlined on the adjoining page in the program schedule.

The cover photo is of a former trading station from the floor of the New York Stock Exchange. This station is currently on display at the Center of Science and Industry (COSI) at 280 East Broad Street, Columbus, Ohio.

REGISTRATION COUPON

MAIL TO:

Ms. Debra Chafin
Ohio Division of Securities
Two Nationwide Plaza - 3rd Floor
Columbus, Ohio 43215
Phone: 614-462-7371

Enclosed is my check for $ __________ to reserve a luncheon and conference seat for __________ persons(s), at $20.00 per person, made payable to the Ohio Division of Securities. (Use a separate sheet of paper for additional names.)

Name(s) ______________________________

Firm Name ______________________________

Address ______________________________

____

Office Telephone: (____) ______________

☐ Check box if you want to receive the Ohio Securities Bulletin which is distributed without charge.

PROGRAM SCHEDULE

LUNCHEON: 11:30 a.m. – 1:00 p.m.
Delaware Room

Introduction & Welcome . . . . Charles H. McClenaghan
Commissioner of Securities

Department of Commerce . . . . J. Gordon Peltier, Director

Luncheon Speaker . . . . Nina Klarich
First National Bank of Chicago

AFTERNOON SESSION: 1:00 p.m. – 5:30 p.m.
Franklin Room

Pork Bellies For Fun and Profit (Commodities Actions) . . . . Nodine Miller
Zacks, Luper & Wolinetz

Extraterritorial application of the federal securities laws . . . . Marc N. Morgenstern, Esq.
Kahn, Kleinman, Yanowitz & Arnson Co., L.P.A.

Through a looking glass - Reflections On Banks & the Securities Business . . . . N. Beverley Tucker, Jr.
Senior V.P., the Fifth Third Bank, Cincinnati, Ohio
&
John L. Evans, Esq.
Graydon, Head & Ritchey

Time Sharing - the new real estate . . . . R. Jeff Andrews
Director of Regulatory Affairs
The Deltona Corporation

Limited Partnership Law New proposals - old problems . . . . Byron S. Krantz, Esq.
Kadish & Krantz Co., L.P.A.

Complex Civil Securities Litigation . . . . Donald A. Antrim, Esq.
Carlile, Patchen, Murphy & Allison

Investment Products of the 80's . . . . C.A. Peterson, Executive V.P.
The Ohio Company

RECEPTION: 5:30 p.m.
Hospitality Suite

Sponsored by: The Industry and the Bar.

Ohio Division of Securities
Two Nationwide Plaza - 3rd Fl.
(Corner Chestnut & High Streets)
Columbus, Ohio 43215