OHIO SECURITIES BULLETIN

A QUARTERLY PUBLICATION OF THE OHIO DIVISION OF SECURITIES

George V. Voinovich
Governor of Ohio

Donna Owens
Director of Commerce

Thomas E. Geyer
Acting Commissioner of Securities

Holderman Steps Down as Securities Commissioner

Effective June 7, 1996, Mark V. Holderman resigned as Commissioner of the Ohio Division of Securities. Holderman had held the post since 1986. Holderman stepped down to head up the Securities Registration Depository, or "SRD" system, which is the state level electronic filing counterpart to the SEC's EDGAR system.

Holderman's goal was balancing investor protection and capital formation. His tenure was marked by firm but fair regulation. Some of his most high profile enforcement efforts came in the battle against Ohio-based penny stock dealers. State court criminal convictions against individuals affiliated with Dublin Securities, Inc., and Worthington Investments, Inc., as well as state civil actions against Columbus Skyline Securities and M.C. Capital Corporation highlighted Holderman's efforts to rid the securities industry of fraudulent practices. Holderman was also instrumental in the passage of House Bill 488 which became effective on October 11, 1994 and eradicated the penny stock dealer problem by requiring virtually all Ohio-licensed dealers to also register with the SEC and become members of the NASD.

Holderman's efforts in connection with House Bill 488 also resulted in deregulation by eliminating the filing requirements and related fees for claims of exemption under R.C. 1707.02(B) and 1707.03(O). Holderman also utilized technology to trim the Division staff and budget by 25%, while

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An Overview of Rule 144A Offerings

by Edward W. Moore, Esq.

Editor's Note: O.A.C. 1301:6-3-09(D)(12) prohibits an "investment company" from investing more than fifteen percent of its total assets in securities which are "illiquid." Effective January 21, 1996, the Division amended the administrative rule to exclude "securities eligible for resale pursuant to Rule 144A" from the definition of "illiquid." See O.A.C. 1301:6-3-09(D)(12)(a).

Introduction

Since its adoption in 1991, Rule 144A has transformed the private placement market in the United States. Billions of dollars in debt and equity capital are raised each year by issuers through Rule 144A offerings. This article provides an introduction to the applicability and mechanical aspects of Rule 144A offerings, describes the disclosures customarily included in a Rule 144A offering memorandum and discusses post-closing registration and disclosure requirements.

Applicability of Rule 144A

Although it has become customary to refer to many private placements as "Rule 144A Offer-

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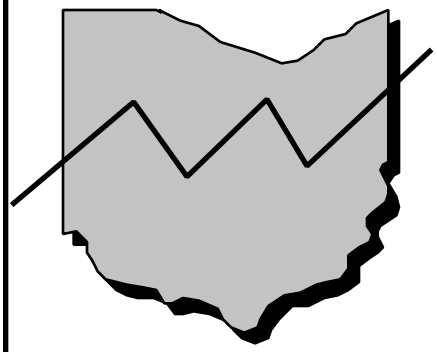

Ohio Securities Bulletin

Issue 96:2

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Holderman

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overseeing an increase in the number of salesmen licensed by the Division from roughly 44,000 in 1986 to over 78,000 at March 30, 1996.

Holderman also implemented a daily review of salesman license applicants. Using the Central Records Depository system, the Division reviews salesman license applicants and their disciplinary histories against the "good business repute" standard set out in R.C. 1707.16. The Division undertakes a similar daily review of dealer license applicants.

Holderman is proud of the level of sophistication that the Division has attained in both registration and enforcement matters. On the registration side, the Division continues to apply its merit standards to increasingly complex offerings. On the enforcement side, the Division has recently tackled a number of sophisticated matters including: the cases against Dublin Securities, M.C. Capital and Columbus Skyline; cases against Prudential Securities and PaineWebber for improprieties in the sale of limited partnerships; the revocation of Government Securities Corporation's dealers license for the sale of unsuitable derivative securities to Ohio counties; and being the first securities regulator to take action, and to find the existence of a security, in the Lloyd's of London matter.

As the President of SRD, Holderman will oversee the transition of the system from a NASAA pilot program to a privately operated corporate entity. He is in the process of moving the corporate headquarters from Arlington, Virginia, to Columbus. Holderman plans to update SRD's technology by making it an Internet-based system. Holderman expects that the SRD will offer efficient, cost effective "one stop shopping" for state blue sky filings.

To take Holderman's place, Director of Commerce Donna Owens has appointed Thomas E. Geyer as Acting Commissioner. Geyer had been a Staff Attorney in the Division's Enforcement section since January 1994 and had also served as Attorney Inspector on an interim basis. He received his undergraduate degree in business administration from the University of Notre Dame and his law degree, with honors, from the Ohio State University College of Law. Mr. Geyer was in private practice in both Columbus and Cincinnati before joining the Division.

144A Offerings

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ings," Rule 144A simply provides a mechanism by which certain securities may be resold without registration under the Securities Act of 1933 (the "Securities Act") to a limited class of investors known as "Qualified Institutional Buyers" ("QIBs"). Included in Rule 144A's definition of QIBs are banks, insurance companies, investment companies, broker-dealers and other institutional accredited investors with specified amounts of money invested in securities (generally $100 million, although a broker-dealer may qualify as a QIB with as little as $10 million invested in securities).

Since Rule 144A is a resale rule, all of the requirements traditionally applicable to private placements under Section 4(2) of the Securities Act continue to apply to offerings structured to take advantage of Rule 144A.

What makes Rule 144A so advantageous is the fact that it helps reduce the significant liquidity problems that have historically plagued the private placement market. Under the Securities Act, in order for an issuer's offering to satisfy the requirements for the private placement exemption, all investors must purchase the securities for investment, and not with a view to further distribution. Because of this requirement, resales of privately placed securities without registra-

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OHIO SECURITIES BULLETIN

Thomas E. Geyer, Esq., Editor

The *Ohio Securities Bulletin* is a quarterly publication of the Ohio Department of Commerce, Division of Securities. The primary purpose of the *Bulletin* is to (i) provide commentary on timely or timeless issues pertaining to securities law and regulation in Ohio, (ii) provide legislative updates, (iii) report the activities of the enforcement section, (iv) set forth registration and licensing statistics and (v) provide public notice of various proceedings.

The Division encourages members of the securities community to submit for publication articles on timely or timeless issues pertaining to securities law and regulation in Ohio. If you are interested in submitting an article, contact the Editor for editorial guidelines and publication deadlines. The Division reserves the right to edit articles submitted for publication.

Ohio Division of Securities

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Adjustable Lease Arrangements under the Ohio Division of Securities Guidelines for the Sale of Securities on Bank Premises

In April 1996, in *Ohio Securities Bulletin* Issue 96:1, the Division promulgated Guidelines for the Sale of Securities on Bank Premises (the "Guidelines") to clarify certain applicable provisions of the Ohio Securities Act and related administrative rules. The Guidelines *do not* establish new laws or administrative rules. Rather, the Guidelines are a collection of the Division's interpretations of the provisions of the Ohio Securities Act and rules that are already applicable to the sale of securities on bank premises. Consequently, the Guidelines outline a "safe harbor" with respect to the Ohio securities regulatory standards.

Among the issues that the Guidelines address is the compensation arrangement between a dealer and a bank. The Guidelines point out that O.A.C. rule 1301:6-3-19(A)(7) ("Rule 19(A)(7)"), which has been in effect since 1983, prohibits a dealer from sharing "any commission, discount or other remuneration from the purchase or sale of a security with any person not licensed as a dealer or salesman in Ohio or in the jurisdiction where the purchase or sale of the security took place." As the Guidelines discuss, this rule establishes a flat prohibition on the sharing of any transaction-based compensation with any unlicensed "person" (as defined in R.C. 1707.01(D)), without regard to whether the unlicensed person is exempt from the definition of dealer or otherwise not required to be licensed.

The Guidelines also point out that a strict lease arrangement, with a fixed lease payment, does not violate the commission sharing prohibition of Rule 19(A)(7). Further, the Guidelines state that the Division views a bona fide adjustable-type lease as acceptable subject to some general conditions. First, the adjustment must not consist of "commission, discount, or other remuneration from the purchase or sale of securities." However, adjustments based on factors like actual expenses incurred, assets on deposit with the dealer, dealer revenue, dealer net income, or other factors not consisting exclusively of transaction-based compensation are permitted. Second, the Guidelines suggest that the more often the lease payment is adjusted, the more it may appear that the adjustable lease payment is an attempt to circumvent the Rule 19(A)(7) prohibition. Third, the parties to the agreement should examine the facts and circumstances surrounding an adjustable lease to determine whether the arrangement is intended to circumvent the Rule 19(A)(7) prohibition. Dealers and banks should ensure that the agreements they enter into are bona fide lease arrangements, rather than agreements designed to share "commission[s], discount[s], or other remuneration from the purchase or sale of securities."

Division Adopts NASAA Guidelines for Registration of Asset-Backed Securities

by Mark R. Heuerman, Esq.

The North American Securities Administrators Association ("NASAA") has adopted statements of policy, or guidelines, for the registration of asset-backed securities.[1] The Division of Securities will apply these guidelines to the merit review of public offerings of asset-backed securities that fall within the parameters of the policy statements.[2]

Asset-backed securities are defined in the guidelines to include securities that provide a stated rate of interest and a return of principal to security holders from the payment of the eligible assets.[3] The merit review standard that the Division normally applies to debt offerings appeared inflexible in permitting certain issuers to conduct public offerings of these securities. That merit review standard requires issuers to demonstrate a ratio of earnings to fixed charges or a ratio of earnings to combined fixed charges and preferred stock dividends (calculated in accordance with Regulation S-K, Item 503, under the Securities Act of 1933) of at least 1.0 for the three most recent fiscal years and the latest interim period preceding the date of effectiveness of such public offering.[4] However, most of the issuers of asset-backed securities are start-up entities with no record of past earnings to comply with this policy statement. Adoption of the NASAA guidelines gives the Division a more appropriate standard of review for these particular issuers.

Assets eligible for inclusion in asset-backed securities generally include accounts receivables, loans or other assets providing a payment obligation to the owner of that asset. Many of the assets may not have been identified for purchase. Consequently, the Division would be unable to evaluate each particular asset or obligor of the asset under the "earnings to fixed charges" merit standard to ensure that there are earnings sufficient to meet the fixed charges obligations. As mentioned, the NASAA guidelines pro-

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144A Offerings

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tion traditionally created significant legal problems. This requirement also made it difficult for investment banking firms to act as principal in private placements, thus making these transactions more cumbersome.

In adopting Rule 144A, the Securities and Exchange Commission ("SEC") essentially sanctioned the development of a secondary market for privately placed securities consisting exclusively of QIBs. From a legal standpoint, Rule 144A accomplishes this objective by providing that any person who resells securities in compliance with its provisions will not be deemed to be engaged in a distribution of such securities for purposes of the Securities Act.

In addition to limiting resales to QIBs only, Rule 144A contains other limitations on its use. The most notable of these is a provision prohibiting reliance on Rule 144A for resales of securities that are fungible with securities traded in the public market.

Mechanics of a Rule 144A Offering

In many ways, Rule 144A offerings mirror public offerings, with the important exception of SEC involvement.

The investment banker retained by the issuer will distribute a preliminary offering memorandum to potential investors, organize road shows and "one-on-ones" and generally engage in marketing efforts similar to those involved in a public offering. Because of concerns regarding the need to avoid general solicitation, these marketing efforts will be targeted exclusively to QIBs, institutional accredited investors and foreign investors.

The investment banking firm and the issuer will enter into a purchase agreement that is quite similar to an underwriting agreement for a public offering. That agreement will provide for the purchase of the securities by the investment banking firm at a discount and their resale to investors. The agreement will contain representations and warranties similar to those found in underwriting agreements, and will also call for legal opinions, comfort letters and closing documents similar to those called for by most underwriting agreements.

Disclosure Requirements Applicable to Rule 144A Issuers

In order to take advantage of its resale provisions, Rule 144A requires that investors and their transferees have the right to acquire the following information from an issuer that is not already subject to the reporting requirements of the Securities Exchange Act of 1934: (i) a brief statement of the nature of the issuer's business and the products and services that it offers; and (ii) the issuer's most recent balance sheet and profit and loss and retained earnings statements and similar financial statements for such part of the two preceding fiscal years that the issuer has been in operation (which should be audited to the extent reasonably available).

The required information must be "reasonably current." If the description of the issuer's business is as of a date within 12 months of the date of the resale, the balance sheet is as of a date within 16 months of the date of the resale and the other financial statements are for the 12 months preceding the date of the balance sheet, the information will be deemed to be reasonably current. However, if the balance sheet is more than 6 months old, interim financial statements for the period from its date to a date within 6 months of the date of resale also must be furnished.

While the information required in order to rely on Rule 144A for resales is quite limited, offerings contemplating the use of Rule 144A generally contain much more extensive disclosures, including:

Financial Statements - For offerings by non-reporting issuers, it is customary to include financial statements. The extent of financial information required will vary depending upon marketing requirements. Unlike public offerings, pro formas and acquired company financial information typically are not included in the offering memorandum, unless a registered exchange offer is contemplated.

Projections - Projections are sometimes included in the offering memorandum, although this is not a good practice if a registered exchange offer is contemplated.

Business Description - An extensive discussion of the issuer's business is typically included in the offering memorandum, as a result of concerns regarding disclosure of material information and because of marketing requirements.

Risk Factors - It is customary to include a risk factors section in the offering memorandum.

Description of Securities - The offering memorandum will include a lengthy description of the securities being offered.

MD&A - If a registered exchange offer or shelf registration is contemplated, the offering memorandum will generally include an MD&A section.

Other Disclosures - Other areas as to which disclosure is typically included in a Rule 144A offering memorandum include applicable restrictions on transfer, the plan of distribution and the anticipated use of the proceeds of the offering.

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Post-Closing Registration

Rule 144A securities are almost always registered under the Securities Act shortly after their original issuance. This is because of the need for many institutional investors to have securities that are "marketable" under state legal investment laws and other statutes. The type of registration statement filed by the issuer will vary depending on the nature of the securities in question.

Shelf Registration - If the securities sold by the issuer are common stock, convertible debt, or non-investment grade preferred stock, a shelf registration statement will be used to register the securities for resale by investors.

In a shelf registration, the identities and amounts of securities owned by each investor will need to be disclosed, and the investor will be required to deliver a copy of the prospectus to each purchaser.

As a result of the need to have a current prospectus to deliver, the issuer will generally be required to maintain an "evergreen" prospectus for a three- year period or until such time as the investors have disposed of their securities.

Registered Exchange Offer - If the securities sold by the issuer are non-convertible debt, investment grade non-convertible preferred stock or certain other types of securities, investors may exchange their securities for identical securities in a registered exchange offer.

There are several advantages to investors of the registered exchange offer approach. First, investors will receive freely transferable securities in the transaction and will not be required to deliver a prospectus to any person who purchases from them. Second, the investors need not disclose their holdings in the registration statement.

From the issuer's perspective, a significant advantage of the registered exchange offer is that there typically will not be a requirement to maintain an "evergreen" prospectus.

Post-Closing Registration Disclosure Requirements

While the registration form to be used will vary depending on whether the securities will be registered for resale or in an exchange offer, much of the disclosure requirements will be the same.

In any registered offering, a non-reporting issuer will be required to include in its registration statement disclosures relating to the following matters: (i) five years of selected financial data, three years of audited finacial statements, pro forma and acquired company finacial statements (if an acquisition has occurred or is "probable"); (ii) a risk factors section; (iii) a description of the business; (iv) an MD&A section; (v) a section identifying the issuer's directors, executive officers and principal stockholders; (vi) compensation tables describing compensation arrangements for the issuer's CEO and its other four most highly compensated executive officers; (vii) a description of transactions with related parties; and (viii) a description of the securities to be offered.

As noted above, if the securities are registered for resale, the identity and holdings of each of the investors will also need to be disclosed in the registration statement.

Conclusion

Since most Rule 144A transactions will ultimately result in the need to prepare and file a registration statement, an issuer may well ask what makes Rule 144A an attractive option. The answer to this question is that while the issuer will be required to incur the costs and delays associated with registration of the securities, it will only have to do so after it has received the proceeds of the offering. From an issuer's perspective, Rule 144A is best viewed as providing a mechanism for bringing offerings to market much more quickly than through pre-sale registration, and with better pricing than would be available in a private placement.

Edward W. Moore has been a partner with Calfee, Halter & Griswold in Cleveland since 1990. He started with Calfee in 1982 after graduating from Case Western Reserve University Law School and Miami University of Ohio. Mr. Moore specializes in counseling privately and publicly held corporations with respect to federal and state securities law compliance.

This article is based on materials Mr. Moore prepared for the 1995 Ohio Securities Conference. Mr. Moore would like to thank John J. Jenkins, also a partner at Calfee, for his assistance in the preparation of this article.

NASAA Guidelines

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vide a more flexible standard of review in this area.

The following discussion highlights some of the requirements for issuers conducting public offerings of asset-backed securities.

First, an issuer must purchase "eligible assets."[5] Those assets must be financial or commercial assets that are homogenous and subject to reasonable objective valuation.[6] They must be self-liquidating or easily liquidated and capable of generating a predicable cash flow.[7]

Second, the sponsor must be able to demonstrate a sufficient level of experience in the origination, servicing or pooling of the assets.[8] The Division will require the servicer or sponsor to have at least

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NASAA Guidelines

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three years experience in servicing the eligible assets similar to those to be acquired by the issuer.[9]

Third, the issuer must be a "special purpose entity"[10] with the purpose of making one or more offerings. If an issuer plans on conducting more than one offering, the asset backed securities must be secured by a distinct pool of assets.[11] The trustee of the distinct pool of assets must be a qualified financial institution and independent from the servicer, sponsor or issuer.[12]

Fourth, the issuer must obtain an ownership interest or perfected security interest in the eligible assets.[13] The Division may also require an opinion of counsel that the transfer of eligible assets would be treated as a "true sale" or that the disclosed procedures will result in a perfected security interest in those assets.[14] The offerings must prohibit cross-collateralization and cross-defaults.[15]

Fifth, the Division will evaluate the fees and expenses. Obviously, the cash flow generated must be sufficient to cover the fees, expenses and provide the purchasers with the stated rate of return and principal.[16] Offerings must clearly state how interest is computed and payments are made in order for the Division to review the cash flow of the issuer. To fulfill principal and interest obligations, sponsor guarantees or credit enhancements may be required where the cash flow is speculative.[17] All guarantees or credit enhancements must be appropriately disclosed.

Finally, investors must meet the suitability requirements specified in the NASAA guidelines. Investors must have a minimum annual gross income of $45,000 and a net worth of $45,000, or have a net worth of $150,000.[18] The Division may also require that an investment not exceed 10% of an investor's liquid net worth.[19]

Only certain requirements have been discussed herein for offerings of asset-backed securities. Asset-backed offerings that are rated "investment grade" by a rating agency will have fewer requirements under the guidelines.[20] However, the issuer must bear the cost of having the rating monitored at least annually.[21] Issuers and their counsel should thoroughly review the guidelines while planning the offering. The guidelines are published by Commerce Clearing House in the North American Securities Administrators Association Reports.

Endnotes

[1] Registration of Asset-Backed Securities. Adopted October 25, 1995.

[2] NASAA Guideline I.A.2. The contents of this Statement of Policy shall be referred to herein as "Guidelines."

[3] NASAA Guideline I.B.7.

[4] *See Ohio Securities Bulletin* (July 1986)

[5] NASAA Guideline I.B.12.

[6] *Id.*

[7] *Id.*

[8] NASAA Guideline II.A.

[9] NASAA Guidelines I.B.27.; IV.A.

[10] NASAA Guideline I.B.30.

[11] NASAA Guideline III.A.2.

[12] NASAA Guidelines I.B.33.-35.; V.A., C. A trustee may serve as the issuer.

[13] NASAA Guideline III.B.

[14] NASAA Guideline III.C.

[15] *Id.*

[16] NASAA Guideline II.D.

[17] NASAA Guideline II.C.

[18] NASAA Guideline VI.B.

[19] NASAA Guideline VI.B.1. provides that the administrator may require higher suitability standards.

[20] NASAA Guidelines I.B.13., 25.; II.C.1.(a), D., I.2.; III.A.2., B.1., D., G.; IV.A.1., B.1-3., C., D.1.(a),(c); VI.A.1.(a); VII.A.1., C., D.2., E.; VIII.A., B., C.2.,3., D., E.; IX.B.3.

[21] NASAA Guideline III.H.

Mark R. Heuerman, Esq., is an Attorney/Examiner in the Division's Registration Section.

Technology Advisory Committee Added

On-line prospectuses, Internet Investment Advisors, EDGAR and Broker-Dealer Web sites. Those are just some of the results of the increased impact of technology on the securities industry in recent years. In response to the explosion of technological issues in securities regulation, the Ohio Division of Securities has announced the establishment of a Technology Advisory Committee.

Initial items on the Technology Advisory Committee's agenda will include considering policy positions and the possible need for rules in response to new sales techniques and marketing programs on the Internet. The committee will review the positions of NASAA and other states regarding Internet offerings, examine the adequacy of current requirements for broker-dealers offering services over the Web, and generally consider the implications of emerging telecommunications systems for securities regulation.

The committee will also review the Division of Securities Web site with an eye toward additions and improvements in the Division's newest tool for improving investor and industry communication. "http://www.securities.state.oh.us" is the gateway for immediate on-line access to the Ohio Division of Securities.

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Columbus attorney Robert Schwartz of Schwartz, Warren and Ramirez, and William Leber, Counsel to the Commissioner, will serve as co-chairs of this new committee. In conjunction with the establishment of the Technology Advisory Committee, Thomas E. Geyer will take over as co-chair of the Takeover Advisory Committee.

If you are interested in serving on the Technology Advisory Committee, the Takeover Advisory Committee, or the other Advisory Committees of the Ohio Division of Securities, please contact the Division of Securities at (614) 644-7381. The Registration and Exemption Advisory Committee, the Licensing Advisory Committee, and the Enforcement Advisory Committee will meet in conjunction with the Ohio Securities Conference on Monday, November 4, 1996 (*see page 14*), along with the Technmology Advisory Committee and the Takeover Advisory Committee.

Investor Education

On April 25, 1996, Director of Commerce Donna Owens announced the availability of *The Informed Investor* publications to assist investors and prospective investors in making financial decisions. The publications were written by the North American Securities Administrators Association Investor Education Committee and the Council of Better Business Bureaus in cooperation with the Division.

The title of the guides and a description of each is as follows:

Questions for Informed Investors — addresses questions that investors should ask prior to investing, such as: Do you have money to invest? What are your investment goals? How much risk are you comfortable with?

Mutual Funds — provides an overview on how mutual funds work and answers the most frequently asked questions from prospective mutual fund investors.

Who's Who in the Financial Planner and Investment Adviser Field — describes the services provided by financial planners and investment advisers, as well as how they are paid for their services. A chart is provided to describe the major professional designations in these fields, including the prerequisites and testing requirements.

How to Spot a Con Artist — provides information on how con artists try to lure victims and provides tips on how to avoid falling prey to their schemes.

Copies of the publications may be obtained from the Division. The response to the Director's announcement has been tremendous and hundreds of these new publications have been mailed to Ohio residents.

Danaher Corporation v. Acme-Cleveland Corporation: Federal District Court Suggests Amendment of R.C. 1701.01(CC)(2)

As reported in the last issue of the *Bulletin*, Danaher Corporation, a Washington, D.C., based tool manufacturer filed with the Division on March 7, 1996, a Form 041 to pursue a control bid for shares of Cleveland based Acme-Cleveland Corporation, a telecommunications, electronics and precision products concern. In connection with the control bid, Danaher filed in the U.S. District Court for the Southern District of Ohio a complaint for restraining order, preliminary and permanent injunction and declaratory judgment, attacking the constitutionality of portions of both the Ohio Control Bid Statute, R.C. 1707.041, *et seq.* and the Ohio Control Share Acquisition Act, R.C. 1701.831, *et seq.* (case no. C2-96-0247 S.D. Ohio, filed March 7, 1996). At a status conference before Judge James L. Graham on March 7, 1996, counsel for Danaher acknowledged that the attack on the Control Bid Statute would be moot if the Division failed to suspend the control bid, which is what happened in this case. However, the attack on the Control Share Acquisition Act remained.

R.C. 1701.831 provides that a "control share acquisition" of shares of an "issuing public company" may be made only with the prior authorization of the shareholders of the issuing public company at a special meeting of the shareholders called for such purpose. The statute imposes a dual quorum requirement for the special meeting: both a majority of the shares entitled to vote in the election of directors and a majority of non-"interested" shares must be present in person or by proxy. The statute similarly imposes a dual voting requirement: the offer must be approved by a majority of the voting shares and by a majority of the voting non-"interested" shares.

Specifically, Danaher's complaint attacked the constitutionality of the definition of "interested shares" set out in R.C. 1701.01(CC)(2), which primarily encompasses shares acquired after the announcement of the control share acquisition. Danaher claimed that R.C. 1701.01(CC)(2) was preempted by the Williams Act. Danaher also asserted that R.C. 1701.01(CC)(2) violated the commerce clause in that it prevents the consummation of certain interstate tender offers and imposes a burden on interstate commerce that is not justified by any purported local benefit. Danaher further argued that the issue was controlled by the deci-

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Division Proposes New Mutual Fund Regulation

by Deborah Dye Joyce, Esq.

The mutual fund industry is growing by leaps and bounds. Millions of investors use mutual funds as their primary investment vehicle. Despite the increasing amount of money placed in mutual funds—more than one trillion dollars by the mid-1990s—investor protection remains as necessary as ever.

For decades, both state governments and the federal government have worked together to oversee mutual fund practices. The dual regulation focuses on investor protection while endorsing competition, capital formation and investment innovation by the mutual fund industry. The federal government provides important oversight on a national basis, creating a general, stable environment of oversight. On the other hand, the various state governments are closer to their constituencies, and afford state residents on-sight regulation. Together, the general federal oversight coupled with the more familiar supervision given by the states, provides investors with as much protection as possible in the investment arena.

Taken alone, neither the federal government nor the various state governments can do the job as well as both regulators working together. The federal government is too distant to provide a detailed review of each and every mutual fund application and is not familiar with the state constituency. However, the state governments are in a position to review each and every filing and are familiar with their constituency.

The Division believes that certain sectors of the government, industry, and the investing public are losing sight of what should be the regulatory focus; first and foremost, investor protection. Secondly, facilitating competition and capital formation by removing barriers. Lastly, encouraging innovation. Protecting the investing public does not mean competition, capital formation and innovation are forsaken. The concepts are not mutually exclusive and are, in fact, interdependent.

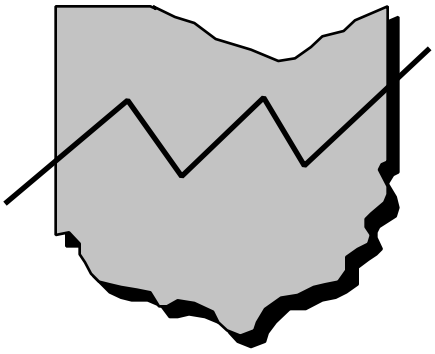
In order to facilitate satisfactory dual regulation, it is necessary to continuously monitor the applicable rules and regulations. Based on such a review, the Division believes that certain changes need to be made to current mutual fund regulations in Ohio so as to permit a more cohesive dual review. The introduction of the Fields Bill and its subsequent revision makes it even more important for state regulators to act promptly—otherwise an important source of investor protection may be lost.

The changes proposed by the Division will dramatically change the face of the mutual fund regulation in Ohio. Gone will be specific limitations pertaining to diversification and investments in voting securities, illiquid securities, and other investment companies. In their stead, the Division is focusing on broader concepts and disclosure. In essence, the Division proposes to adopt guidelines created by the North American Securities Administrator Association ("NASAA") regarding investments in debt securities, master/feeder programs, periodic payment plans and telephone transactions. These revisions should assist the Division in providing more comprehensive regulatory oversight of mutual funds for Ohioans.

In addition, the various state jurisdictions are also working together to establish a coordinated review program for initial filings. Involvement in this program will allow issuers to receive coordinated comments faster, thereby permitting faster resolution. The Division is committed to the viability of such a program and Ohio's participation will commence as soon as the proposed regulatory changes are implemented.

The Division intends to adopt the NASAA guidelines as administrative rules, as described in the accompanying Public Notice. While this represents a significant change in Ohio's regulation of mutual funds, the Division believes it will permit more comprehensive regulatory oversight of mutual funds.

Deborah Dye Joyce, Esq., is an Attorney/Examiner in the Division's Registration Section and currently reviews the mutual funds filings made with the Division.



PUBLIC NOTICE

At 10:00 a.m. on October 16, 1996, the Ohio Division of Securities will hold a hearing regarding proposed changes to rules of the Division. The hearing will be held in the offices of the Ohio Division of Securities, 77 South High Street, 22nd Floor, Columbus, Ohio 43215.

The Division of Securities has proposed that Ohio Administrative Code ("O.A.C.") Rule 1301:6-3-09 be amended.

Synopsis: As described in the article accompanying this public notice, O.A.C. Rule 1301:6-3-09 will be amended to revise a series of requirements applicable to the securities of companies subject to registration under the Investment Company Act of 1940 (*i.e.* mutual funds) in order to bring the provisions of the Ohio rule into greater conformity with the standards of the Securities and Exchange Commission and of other states.

Purpose: The Ohio Division of Securities is seeking to cooperate with the securities administrators of the other states and the Securities and Exchange Commission to achieve maximum uniformity in the form and content of registration statements, applications, reports, and overall securities regulation with respect to Investment Company (mutual fund) securities.

Copies of the proposed amendments to O.A.C. Rule 1301:6-3-09 may be obtained by contacting the Ohio Division of Securities, 77 South High Street, 22nd Floor, Columbus, Ohio 43266-0548.

Division Enforcement Section Reports

Administrative Orders

Shisler & Associates, Inc., and Douglas R. Shisler

On April 15, 1996, the Division issued Division Order 96-061, an order suspending the sale of certain securities purported to be registered by Shisler & Associates and Douglas R. Shisler of Canton, Ohio. The suspension was issued pursuant to R.C. 1707.13.

The order resulted from a 6(A)(1) filing made by Shisler & Associates on January 4, 1996, purporting to register by description certain transactions in promissory notes. The filing was incomplete in a number of respects. By letter dated January 10, 1996, the Division notified Shisler of the deficiencies in the filing and requested the correction of those deficiencies. However, Shisler did not respond to the comment letter. Consequently, the Division issued the suspension order under authority of R.C. 1707.13, which suspended the registration by description of any securities and the right of any issuer or dealer to buy, sell or deal in those securities.

R. Future, Inc., and James L. Binge

On April 15, 1996, the Division issued Division Order 96-062, suspending the sale of certain securities purported to be registered by R. Future and James L. Binge of Canton, Ohio. The suspension was issued pursuant to R.C. 1707.13.

The order resulted from a 6(A)(1) filing made by R. Future on January 4, 1996 purporting to register by description certain transactions in promissory notes. The filing was incomplete in a number of respects. By letter dated January 10, 1996, the Division notified

Danaher Corp.

Continued from page7

sion in *Luxottica Group S.p.A. v. United States Shoe Corp.*, 919 F. Supp. 1085 (S.D. Ohio 1995), where Judge Graham held that R.C. 1701.01(CC)(2) was preempted by the Williams Act.

In response, the State argued that the *Luxottica* decision did not control and that the Control Share Acquisition Act was not preempted because, among other reasons, Congress has not expressly indicated an intent to preempt, compliance with both the Williams Act and the Control Share Acquisition Act is not impossible and the Control Share Acquisition Act does not frustrate the purpose of the Williams Act. The State further argued that the Control Share Act does not offend the commerce clause because it does not discriminate against interstate commerce or subject activities to conflicting state regulations, and any incidental burden imposed is rationally related the Control Share Acquisition Act's legitimate purpose.

The litigation became moot when Danaher and Acme-Cleveland announced on June 3, 1996, that they had struck a deal for Danaher to acquire Acme-Cleveland for $30 per share, which represented a three dollar premium over the control bid price of $27 per share. Upon reaching the agreement, the parties moved Judge Graham to dismiss the legal proceedings. However, the State filed a motion to impose appropriate terms and conditions on the dismissal, specifically asking the Court to rule on the constitutionality of the Control Share Acquisition Act.

Judge Graham granted the motion to dismiss but declined to rule on the constitutionality of the Control Share Acquisition Act. In a written order dated July 1, 1996, he noted that the parties sought dismissal of the proceeding before the hearing on the constitutionality of the Control Share Acquisition Act was completed, leading him to state that "[i]t would not be appropriate for the court to make a final determination of that issue on an incomplete record."

However, Judge Graham concluded his order with the following commentary:

> This court's decision in *Luxottica Group S.p.A. v. The United States Shoe Corporation*, 919 F. Supp. 1085 (S.D. Ohio 1995), as well as the arguments raised in this case and the court's rulings during the aborted preliminary injunction hearing show that there are serious issues relating to the interpretation of certain provisions of the Ohio Control Share Acquisition Act which result from the wording of Ohio Revised Code §1701.01(CC)(2). The state should consider amending the statute to resolve the resulting confusion.

The Division intends to facilitate a discussion of this issue at the meeting of its Takeover Advisory Committee held in connection with the Ohio Securities Conference.

Binge of the deficiencies in the filing and requested the correction of those deficiencies. When Binge did not respond to the comment letter, the Division issued the suspension order under authority of R.C. 1707.13. The order suspended the registration by description of any securities and the right of any issuer or dealer to buy, sell or deal in those securities.

R. J. Morrow & Assoc., Inc. and Joseph D. Morrow

On April 25, 1996, the Division issued a final Cease and Desist Order, Division Order No. 96-063 against R. J. Morrow & Assoc., Inc. and Joseph D. Morrow, of Colorado Springs, Colorado.

An investigation by the Division revealed that in 1993, Morrow sold stock in R. J. Morrow & Assoc., Inc. to an Ohio resident for a total of $50,000. However, the records of the Division contained neither a registration nor claim of exemption for the transaction. Consequently, the shares were sold in violation of R.C. 1707.44(C)(1).

On January 30, 1996, the Division had issued to Morrow Division Order No. 96-018, a Notice of Opportunity for Hearing, setting forth the Division's allegations and describing the right to request an administrative hearing on the matter. The Division was unable to perfect service through certified mail and published notice of the notice order, as required by R.C. Chapter 119. After the statutory publication requirements were satisfied and Morrow did not request an administrative hearing, the Division issued the final order, which orders Morrow and his company to cease and desist from violations of the Ohio Securities Act.

United Production, Inc. and Thomas Duke

On April 26, 1996, the Division of Securities issued a final Cease and Desist Order, Division Order No. 96-064, against United Production, Inc., a Delaware corporation with a business address in East Norwich, New York, and Thomas Duke, the vice-president of United Production, Inc. (collectively "Respondents").

An investigation by the Division revealed that in 1994, Respondents sold to an Ohio resident an interest in an oil well located in Morrow County, Ohio. The interest fell within the definition of a security, set out in R.C. 1707.01(B). The records of the Division contained neither a registration nor a claim of exemption for the transaction. Consequently, the shares were sold in violation of R.C. 1707.44(C)(1). Further, Respondents never delivered to the Ohio investor the actual working interest, as represented at the time of the sale. Therefore, Respondents also violated R.C. 1707.44(B)(4).

On December 4, 1995, the Division had issued to Respondents Division Order No. 95-090, a Notice of Opportunity for Hearing setting forth the Division's allegations and describing the right to request an administrative hearing on the matter. Copies of the notice order sent to each Respondent via certified mail were returned to the Division undelivered. Subsequently, the Division published notice of the notice order, as required by R.C. Chapter 119. After the statutory publication requirements were satisfied and neither Respondent requested an administrative hearing, the Division issued the final order which orders Respondents to cease and desist from violations of the Ohio Securities Act.

Steve Phillips

On April 26, 1996, the Division issued Division Order No. 96-065, a final Cease and Desist Order against Steve Phillips of Cincinnati, Ohio.

Phillips is a self-described golfer who is seeking to gain tour qualifying status as a member of the Professional Golfers Association. To raise money to finance his efforts, Phillips sold to Ohio residents "Sponsorship Agreements," which bound the sponsor to provide financial assistance to Phillips in return for a share of the income that Phillips may generate. The sponsorship interests met the definition of securities set out in R.C. 1707.01(B). However, the records of the Division contained no registration or claim of exemption for the sale of the sponsorship interests. Thus, the sponsorship interests were sold in violation of R.C. 1707.44(C)(1).

On January 17, 1996, the Division issued to Phillips Division Order No. 96-004, a Notice of Opportunity for Hearing, which set out the Division's allegations and gave Phillips the opportunity to request an administrative hearing on the matter. However, service could not be perfected through certified mail and the Division was forced to publish notice pursuant to R.C. Chapter 119. After the statutory publication requirements were satisfied and Phillips did not request an administrative hearing, the Division issued the final order which orders Phillips to cease and desist from violations of the Ohio Securities Act.

PaineWebber Incorporated

On June 6, 1996, the Division issued Division Order No. 96-078, a final Cease and Desist Order against PaineWebber Incorporated of New York, New York. In connection with the Cease and Desist Order, the Division and PaineWebber entered into a consent agreement, in which PaineWebber waived its right to an administrative hearing and consented to the issuance of the final order.

The final order was based on PaineWebber's improprieties in connection with the sale of limited partnership interests to Ohio residents. The improprieties included violation of the Division's administrative rules prohibiting the sale of unsuitable securities, fraud in sale of securities, failure to reasonably supervise salesmen and the requirement to maintain specified books and records. Because the improprieties in the sale of the limited partnership interests was a nationwide problem, the North American Securities Administrators Association had negotiated a model settlement agreement with PaineWebber. The Division's order is based on the model settlement agreement.

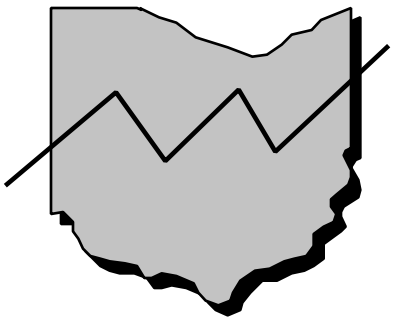
In connection with the settlement with the Division, as well as settlement with other states and the federal Securities and Exchange Commission, PaineWebber agreed to pay substantial fines and also to set up a claim fund to permit recovery by aggrieved investors. Investors may call 1-800-222-2780 to find out if they are eligible to participate in the claim fund, and eligible investors may call 1-800-320-9951 for more information regarding the settlement and restitution process. In addition, PaineWebber agreed to implement certain compliance procedures to prevent the future occurrence of the improprieties that led to this action.

TransGlobal Capital Company f/k/a Greystone Capital Group, Inc.

On June 20, 1996, the Division issued Division Order No. 96-085, a final order revoking the Ohio securities dealer license of TransGlobal Capital Company f/k/a Greystone Capital Group, Inc. of Columbus, Ohio.

On May 16, 1996, the Division had issued to TransGlobal Division Order No. 96-071, an order suspending TransGlobal's Ohio securities dealer license for certain violations of Ohio securities law. Specifically, TransGlobal failed to have a licensed principal in place and also had been suspended from membership in the National Association of Securities Dealers.

The suspension went into effect on May 16, 1996, when Division Order No. 96-071 was issued. Division Order No. 96-071 also gave TransGlobal the opportunity to request an administrative hearing. However, TransGlobal did not request an administrative hearing to contest either the suspension or revocation. Subsequently, the Division issued the final order, revoking TransGlobal's Ohio securities dealer license as of June 20, 1996.



Civil Cases

Victor E. Steinfels, III v. The Division of Securities

On April 12, 1996, Victor E. Steinfels, III, of Dublin, Ohio, filed with the Franklin County Court of Common Pleas a Notice of Appeal pursuant to R.C. 119.12 to appeal from a final order issued by the Division.

As reported in *Bulletin* Issue 96:1, on March 29, 1996, the Division issued against Steinfels Division Order No. 96051, a Final Order to Cease and Desist. The Final Order was based on the Division's finding that Steinfels violated R.C. 1707.44(B)(4) by making false representations of material facts in connection with the sale of limited partnership interests in Vesmont Partners Limited.

The Notice of Appeal alleges that the Division abused its discretion in issuing the Final Order.

William Milton Donald DeArman v. Ohio Department of Commerce, Division of Securities

In June 1996, William Milton Donald DeArman of Houston, Texas, filed with Franklin County Court of Common Pleas a Notice of Appeal pursuant to R.C. 119.12 to appeal a final order issued by the Division.

On June 7, 1996, the Division issued to DeArman Division Order No. 96-080, an order denying DeArman's application for an Ohio Securities Salesman License. The Division issued the order after an administrative hearing had been held on the matter pursuant to the remand order of the Franklin County Court of Common Pleas in *William Milton Donald DeArman v. Ohio State Department of Commerce, Division of Securities*, No. 94CVF-03-1409, (Franklin Co. C.P. Nov. 23, 1994).

In issuing the denial order, the Division rejected the Hearing Officer's

report which recommended that DeArman be licensed, and found that DeArman was not of good business repute.

As previously reported in *Bulletin* Issues 94:2 and 94:4, the Division originally issued an order denying DeArman's application in February 1994 (Division Order No. 94-025). DeArman appealed that order to the Franklin County Court of Common Please. In November 1994, the Court remanded the case to the Division for further proceedings.

On remand, the parties filed with the Hearing Officer a set of stipulations including an agreement to waive oral argument and submit the case in writing. Pursuant to these stipulations, DeArman and the Division filed briefs with the Hearing Officer in November and December 1995. The Hearing Office issued his report and recommendation on April 30, 1996. As mentioned, the Division issued its denial order on June 7, 1996, which rejected the recommendation of the Hearing Officer.

In the matter of: R.W. Sturge Ltd., Falcon Agencies Ltd. and Tim Coleridge ("Lloyd's of London")

On June 7, 1996, the Division issued a Final Order to Cease and Desist, Division Order No. 96-079, against R.W. Sturge Ltd., Falcon Agencies Ltd. and Tim Coleridge (the "Respondents"), agents of the Lloyd's of London insurance market. The Final Order adopted the report and recommendation of Hearing Officer William Martin issued on March 7, 1996. The Hearing Officer found that participation interests in insurance syndicates sold by Respondents to Ohio investors, or "Names," constituted "securities" as defined in R.C. 1707.01(B). Since no filing for registration or claim of exemption had been made with the Division, the securities were sold in violation of R.C. 1707.44(C)(1). Since none of the Respondents was licensed by the Division, the securities were also sold in violation of R.C. 1707.44(A).

The Division's order represented the first finding in the United States that state securities laws had been violated in connection with the solicitation of and investment by U.S. residents in the Lloyd's of London insurance market. The order ordered Respondents to cease and desist from future violations of the Ohio Securities Act. Nonetheless, on June 13, 1996, the Respondents obtained from the Franklin County Court of Common Pleas, a Stay against enforcement of the final order (Case no. 96CVF-06-4367, June 13, 1996). The court accepted Respondent's argument that without a Stay, unusual hardship would result to the Respondents, the Lloyds insurance market and innocent Ohio citizens.

In addition to the Motion for Stay, Respondents also filed a Notice of Appeal to appeal the Division's final order pursuant to R.C. 119.12.

Criminal Cases

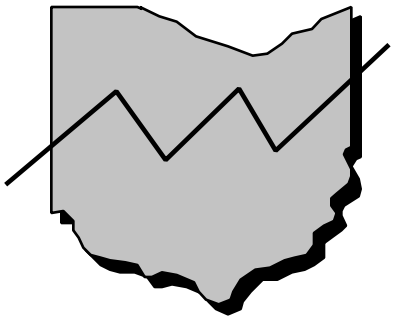
Michelle R. Leuschen

As reported in *Bulletin* Issue 95:1, on March 28, 1995, Michelle R. Leuschen, a former salesperson for Dublin Securities, Inc., was indicted by a Franklin County Grand Jury on 11 counts of misrepresentations in the sale of securities in violation of R.C. 1707.44(B)(4) and 11 counts of material omissions in the sale of securities in violation of R.C. 1707.44(G). The indictments were based on Leuschen's improprities in the sale of three penny-stock issues —Confluence Apparel, Inc., Lifeline Shelter Systems, Inc., and Reitz Data Communications — to nine Ohio investors.

On June 10, 1996, before Judge Cain in the Franklin County Court of Common Pleas, Leuschen pleaded guilty to one count of misrepresentation in the sale of securities. Judge Cain ordered a presentence investigation, which is to include a determination of the amount of restitution Leuschen would be required to pay to investors.

Gary Kannegiesser

On April 30, 1996, Gary Kannegiesser, aka Gary Christopher, was indicted by a Lorain County grand jury on four securities counts and two theft counts. The securities counts consisted of one count each of selling unregistered securities in violation of R.C. 1707.44(C)(1), selling securities without a license in violation of R.C. 1707.44(A), making false representations in selling securities in violation of R.C. 1707.44(B)(4), and fraud in the sale of securities in violation of R.C. 1707.44(G). The indictment was based on Kannegiesser's sale of stock in his own company, GCK&D Inc. dba Avon Lake Travel. Rather than using investors' funds as working capital for the company, Kannegiesser allegedly used the money to repay his own loans to the company. He also allegedly made fraudulent misrepresentations and omissions of material fact to induce Ohio residents to purchase stock in the company.



1996 OHIO SECURITIES CONFERENCE

November 4, 1996
Columbus Marriott North
6500 Doubletree Ave.
Columbus, Ohio 43229

Luncheon Speaker: Mary Keefe, *Director, Midwest Regional Office, Securities and Exchange Commission, Chicago, Illinois*

8:00 to 8:30 a.m. ..... Conference Registration

8:30 to 10:30 a.m. ..... Topic: Securities Laws in *Cyberspace*

Introduction to the Internet
Cary Dachtyl, *Ohio Division of Securities*

Central Records Depository ("CRD")
Jay Cummings, *NASD*

Securities Registration Depository ("SRD")
Mark Holderman, *SRD*

Panel Discussion:
Regulation of Securities Offerings on the Internet

Mark Holderman, *Moderator*
Mark Heuerman, *Ohio Division of Securities*
Robert Bertram, *Pennsylvania Securities Commission*
Catherine Kilbane, *Baker & Hostetler*

10:45 to 11:15 a.m. ..... Topic: Federal Securities Legislation
Neal E. Sullivan, *Executive Director, NASAA*

11:15 to 11:45 a.m. ..... Topic: The Prosecution of the Dublin Securities Case
James Phillips, *Vorys, Sater, Seymour and Pease*

11:45 a.m. to 1:00 p.m. ..... Lunch
Mary Keefe, SEC Regional Director, *Luncheon Speaker*
Developments in Federal Securities Enforcement and Regulation

1:00 to 1:30 p.m. ..... Topic: Guidelines for the Sale of Securities on the Premises of Financial Institutions
Thomas Geyer, *Ohio Division of Securities*

1:30 to 3:00 p.m. ..... Topic: Developments at the Ohio Division of Securities

Michael Miglets, *Registration Supervisor*
Caryn Francis, *Attorney Inspector*
William Leber, *Counsel to the Commissioner*
Thomas Geyer, *Acting Commissioner*

3:00 to 5:00 p.m. ..... Advisory Committee Meetings

5:00 to 7:00 p.m. ..... Reception

Enrollment Fee is $175 per person in advance, $200 at the door.
The Division has applied for five hours CLE credit and for CPE credit for accountants.

1996 OHIO SECURITIES CONFERENCE ENROLLMENT FORM

Name: _____

Firm/Organization: _____

Address: _____

City: _____ State: _____ Zip: _____

Telephone: _____ Amount Enclosed: _____

Choice of Luncheon Entree: Beef o Chicken o Vegetarian o
Do you plan to attend an Advisory Committee Meeting? Yes o No o
If "yes", which Advisory Committee? _____
For special accommodations, please contact Rich Pautsch at (614) 752-9448 before October 15, 1996.

Make checks payable to: "Ohio Securities Conference Committee, Inc." Send Enrollment Form and Payment to: Rich Pautsch, Ohio Division of Securities, 77 South High Street, 22nd Floor, Columbus, Ohio 43266-0548. Enrollment Deadline is October 25, 1996.

Registration Statistics

The table to the right sets out the number of registration filings received by the Division during the second quarter of 1996, compared to the number received during the second quarter of 1995, as well as the number of registration filings received by the Division through the second quarter of 1996, compared to the number received through the second quarter of 1995.

1707	*2Q'96*	*YTD '96*	*2Q'95*	*YTD '95*
.03(Q)	244	523	251	627
.03(W)	30	73	23	61
.04	0	0	0	0
.041	2	3	0	1
.06(A)(1)	23	50	27	62
.06(A)(2)	15	22	6	18
.06(A)(3)	4	11	10	15
.06(A)(4)	7	11	6	12
.09	84	205	119	255
.091	968	1,949	876	1,720
.39	6	13	14	27
.391/.09	0	1	0	0
.391/.091	2	8	4	13
.391/.03(O)	4	10	46	165
.391/.03(Q)	33	73	31	79
.391/.03(W)	2	3	0	0
.391/.06(A)(1)	0	0	0	0
.391/.06(A)(2)	1	1	0	0
.391/.06(A)(3)	0	0	0	0
.391/.06(A)(4)	0	0	0	0
Totals	1,425	2,956	1,413	3,055

Licensing Statistics

The table below sets out the number of Salesmen and Dealers licensed by the Division at the end of the second quarter of 1996, compared to the same quarter of 1995, as well as the number of Salesmen and Dealers licensed by the Division at the end of the first quarter of 1996 compared to the same quarter of 1995 and the third, and fourth quarters of 1995, compared to the same quarters of 1994.

	End of Q3 1995	End of Q3 1994	End of Q4 1995	End of Q4 1994	End of Q1 1996	End of Q1 1995	End of Q2 1996	End of Q2 1995
Number of Salesmen Licensed:	72,062	72,045	71,658	70,642	78,890	69,143	81,795	70,580
Number of Dealers Licensed:	1,891	1,894	1,863	1,759	1,928	1,837	2,011	1,873

OHIO SECURITIES BULLETIN

Ohio Division of Securities
77 South High Street
22nd Floor
Columbus, Ohio 43266-0548

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