

ohio securities bulletin

State of Ohio
John J. Gilligan, Governor

Department of Commerce
Dennis Shaul, Director

Division of Securities
William L. Case III, Commissioner

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COMMENTS OF THE COMMISSIONER

1. *Division Adjusts to Changes in Emphasis for 1974:* As I indicated in my comments on page 4 of the December, 1973, issue of the **Bulletin**, the calendar year 1974 was designed to be "a different kind of year" for the Division than the one which preceded it. During the first six months of this year, the primary emphasis of Division activities has been shifted from a concentration upon increase in efficiency and responsiveness (especially in the processing of registrations and licenses) and upon policy institutionalization (the proposed new securities law, the **Bulletin**, and the development of rules, guidelines and procedures) to the pursuit of more aggressive regulation through active enforcement (principally in connection with intra-state broker/dealer practices and foreign real estate sales, but also with respect to fraudulent activities in all other areas of the local securities markets). This change in emphasis has represented a natural progression in the implementation of the administrative program of the Division, the ultimate objective of which is to create in a corporate form an agency capable of performing a more aggressive and more responsible regulatory function.

In an organization such as the Division, characterized by an inelastic supply of human and financial resources, any significant change in emphasis creates important organizational and displacement problems. As a result, major administrative adjustments have to be made. Moreover, in a government context, changes in policies or activity levels generate industry reactions which are directed back at the agency and at higher authorities. The rationale of the changes being made must be effectively communicated to all of those who share accountability for the agency's operations. During the past two months, a major portion of the time of the administrative staff of the Division has been devoted to handling these problems of transition.

Although enforcement activity has been increased dramatically during the past six months and concrete results have been achieved on several fronts, a severe strain was, as a product of this process, placed upon the Broker/Dealer and Foreign Real Estate Sections and, in particular, upon the Enforcement Section of the Division. (Although during the past year the enforcement resources of the Division have been doubled it is clear that in the future a redoubling or tripling of these resources will be an absolute necessity.) Due to this strain, the offices of the Chief Counsel and Counsel for Policy Development (originally designed to concentrate upon statutory interpretation and policy development matters) became crisis management and communications centers relating to enforcement matters, and as a result the development of rules and guidelines came almost to a standstill and publication of the **Bulletin** practically ceased. In addition, a severe bottleneck developed in terms of the capacity of the Office of the Attorney General to act upon the large volume of administrative actions and court proceedings being generated by the Division.

On Monday, June 10, a major reorganization of key personnel of the Division was effectuated to deal with the problems created by the increase in enforcement activity. This reorganization was designed to utilize more effectively the combined talents and energies of all members of the Division staff and to restructure the areas of responsibility and the lines of authority and communication so that enforcement, crisis management and line supervision, and policy development functions could all proceed, separately and more efficiently. At about the same time several new attorneys were added to the staff in key positions to fill vacancies which had developed during the past ten months and had remained unfilled pending a determination of the Division's budget allocation for fiscal 1975. As a result of these adjustments, the Division is presently better organized and better staffed than it has been in some time.

In connection with the recent Division reorganization, new priorities have been set, both long and short term, with regard to enforcement and policy institutionalization objectives. During the remainder of 1974 and the first few months of 1975, the Division will proceed with a balanced pursuit of its objectives in both of these areas. At that point, the proposed new securities law and legislation relating to Department structural reforms will probably regain the focus of attention.

2. The Reorganization of Key Personnel: In connection with the reorganization of key personnel of the Division mentioned above, the following new position assignments have been made: Robert J. DeLambo is the new Deputy Commissioner and as such is responsible for supervising the normal line functions of the five operating Sections of the Division. As the crisis management center, his office is in charge of making initial determinations and in most cases final dispositions with respect to the variety of operating problems arising from the Registration, Broker/Dealer, Foreign Real Estate, Credit Union, and Consumer Finance Sections. William C. Phillippi, as the new Staff Attorney for Administration, will assist the Deputy Commissioner in this crisis management function.

Jack D. Jester is the new Attorney-Inspector of the Division, in charge of all concrete enforcement activities. His office is now the focal point for communications with the Office of the Attorney General, Special Counsel, the various county prosecutors, and the other Section supervisors with respect to enforcement matters and is the control point for all court proceedings, administrative actions, and criminal prosecutions initiated by the Division. In addition to Larry Carlini, Alan B. Smith III and Kathleen H. Ransier have been added as Division enforcement attorneys to assist the Attorney-Inspector.

Ann H. Casto is the new Chief Counsel. She is in charge of the policy unit of the Division, which is responsible for statutory interpretations and opinions, new legislation, rules, guidelines and procedures, and publications of the **Bulletin**. Karl E. May has been added as a Staff Attorney for Policy to assist the Chief Counsel with the policy development function and an additional attorney will be added to the policy staff in the near future. Alan P. Baden is now Special Counsel for Policy Matters and as such will be assisting the Commissioner with the proposed new securities law and other special projects.

Bernard G. Boiston is the new Supervisor of the Registration Section, which now has all new team captains. Daniel L. Rosenfield, Ronald K. Lembright, and Jeffrey D. Ginther are in charge of the Non-corporate, Intra-State Corporate, and Inter-State Corporate Registration teams, respectively. James C. Warneka is the new Supervisor of the Broker/Dealer Section and R. Michael Jones is the new Supervisor of the Foreign Real Estate Section. For biographical information regarding new Division personnel, see the "Other Developments" Section of this issue of the **Bulletin**.

3. The Division Agenda for 1974: During the remainder of this year, the following enforcement and policy development projects will be given the highest priority and com-

pleted to the extent that human and financial resources will allow:

A. Enforcement: (1) the foreign real estate suspension project (failure to file or inadequate 90-day reports, fraudulent, deceptive, or misleading advertising, and failure to perform in accordance with contractual obligations); (2) the foreign real estate denial project (continued implementation of new standards of fairness and disclosure in connection with new registrations, amendments, price increases, and advertising with particular emphasis upon offering circular and advertising requirements); (3) the intra-state broker/dealer suspension project (failure to comply with the existing DS Series of Regulations, especially with respect to the maintenance of books and records, the filing of financial statements, and the maintenance of minimum net capital); (4) the violation screen project (searching court house records for real estate limited partnerships and oil and gas interests sold without registration and reviewing newspaper advertising for unregistered investment solicitations); (5) the Form 6 project (suspension of registrations by description violating basic fairness and disclosure requirements); (6) the continuation of major litigation (The Cathedral of Tomorrow, Welfare Finance, Ohio Real Estate Investment Trust, etc.); (7) the initiation of new litigation (in connection with several fraud cases currently in various stages of preparation); and (8) other matters of importance relating to enforcement which may arise during the course of the year.

B. Policy Development: (1) the proposed new Ohio Securities Act (review and revision for purposes of reintroduction into the 111th General Assembly next year); (2) new Department legislation relating to structural reorganization, funding, and civil service reform; (3) Foreign Real Estate regulations; (4) new Broker/Dealer regulations (unfair and deceptive practices as well as financial responsibility requirements); (5) Administrative regulations (substantive and procedural matters not dealt with by the Administrative Procedure Act); (6) Statutory Interpretation Guide (containing the Division's interpretation of the most significant provisions of the existing statute requiring clarification); (7) new Credit Union legislation for 1975 (house-keeping amendments); (8) new Credit Union regulations (amendments relating to investment restrictions and mandatory audit requirements); (9) new Investment Company Guidelines (to replace Regulation Q-3); (10) Guidelines for the sale of consumer finance company securities; (11) offering circular and advertising guidelines (governing contents and use); (12) suitability guidelines (for general application); (13) stock option and purchase plan guidelines; (14) real estate investment trust guidelines; (15) take-over bid guidelines; and (16) acquisition and merger guidelines.

4. Real Estate Syndications — Chickens Coming Home to Roost: The number of potential enforcement actions coming to the attention of the Division based upon possible securities violations in connection with the sale of interests in real estate limited partnerships has risen dramatically during the recent months. It is not surprising that, with current economic conditions in the real estate industry being what they are, investors in many real estate syndications would be somewhat disgruntled at the fact that

operating results have not matched the optimistic projections developed at an earlier time for the promotion of their respective ventures. But an analysis in retrospect of the manner in which many of these investment packages were put together reveals that the problem is much more basic to the fundamental precepts of securities regulation than a mere question of economics.

As the limited partnership form of investment vehicle has proliferated in Ohio during the past five to ten years, obligations to the public investor have been taken far too lightly as a general matter, with developers and syndicators and the attorneys and accountants whom they employ concentrating primarily upon the creation of ever more cute and intricate legal and financial structures for siphoning off fees and commissions to promoters and managers and for exploiting the artificial economics of tax-motivated ventures to the point where investments are in many cases so complicated that it is almost impossible for a prospective purchaser to understand what he is getting into, even where a good faith attempt at full disclosure has been made.

In several cases, a thorough investigation of the facts has exposed patterns of conduct on the part of the general partners and their affiliates evidencing a total disregard by such persons of their obligations under the securities and partnership laws in dealing with the public (in particular their obligation to fully disclose all facts material to a meaningful investment decision). These cases have characteristically involved webs of self-dealing, conflicts of interest, secret understandings between affiliates, large distributions of cash to insiders in the form of fees and commissions, and, in general, questionable business practices more calculated to serve the special purposes of the individuals involved rather than the interests of the limited partnership and its public investors. If prospective purchasers had had a full understanding of the true state of the facts in these cases, prior to making a financial commitment, most would have chosen not to invest.

Vigorous enforcement action by the Division in this area is important not only as a measure to protect the interests of investors in the specific cases under consideration, but also as a valuable precedent for reaffirming the obligations of general partners, affiliates, attorneys and accountants in connection with public real estate limited partnerships, a type of issuer which has grown to a position of considerable significance in the local securities markets of Ohio. Enforcement resources of the Division are currently being channeled into this important area and concrete results should be forthcoming.

William L. Case, III

POLICY DEVELOPMENTS

Interpretation of DS Series Regulations

I. Introduction.

Although the Ohio Division of Securities intends to promulgate new rules to supersede the existing body of dealer and salesman regulations, the Division will continue to apply

the regulatory framework now in effect until the new rules have been adopted. The existing series of Dealer/Salesman regulations, which is designed to enable the Division to supervise the financial responsibility, record keeping, and reporting obligations of licensed dealers in every type of "security" as that term is defined in Ohio Revised Code Section 1707.01(B), is being interpreted and applied in the manner set forth below.

The Division is charged with the responsibility for determining the qualifications of an applicant for a dealer's license by Section 1707.15. Once the license has been issued, the Division continues its supervision through the annual renewal process (Section 1707.17), the auditing process (by Division examiners), and the financial reporting requirements of Regulation DS-9 [now designated COs-1-07(I)]. The Division is expressly authorized to prescribe rules and regulations for the conduct of business by licensees [Section 1707.19(I)], and to define "fraudulent, evasive, deceptive, or grossly unfair practices or devices in the purchase or sale of securities" (Section 1707.19).

II. Financial Responsibility.

Regulations DS-4 [now designated COs-1-07(D)], DS-5 [COs-1-07(E)], and DS-10 [COs-1-07(J)] provide, respectively, for (A) standards of financial responsibility to be observed by applicants for dealer's licenses, (B) continuing requirements designed to safeguard the capital of dealers, and (C) methods for adjusting financial statements to eliminate or reduce the value of certain assets of doubtful or illiquid character for the purposes of determining a dealer's net worth.

A. Financial Requirements for Dealers

Regulation DS-4 generally requires an applicant to reflect an adjusted net worth of \$10,000 in order to obtain a license. But this regulation allows the Division considerable flexibility in accepting (on proper showing) a net worth of less than \$10,000, although the net worth may never be less than \$5,000. In the case of Issuer-Dealers, the Division may waive the net worth requirements altogether. These determinations are entirely discretionary, and are based on what the Division considers in each individual case to be adequate protection for investors doing business with such dealers.

The Division is authorized to accept in lieu of the net worth requirement a surety bond which is "satisfactory to the Division" and covers "all obligations to his [the dealer's] customers." Almost all of the surety bonds used in Ohio and other states have provided that the surety will assume the obligations of the principal for violations of the applicable statute. It is questionable whether a bond that insures only against statutory violations would be broad enough to cover all customer obligations required by DS-4;

Ohio Revised Code Chapter 1707 is basically a licensing and anti-fraud statute, and the case could arise in which the dealer has failed to meet an obligation to a customer and yet has not violated any statutory provisions. Such actions would not invoke the guarantee of the surety. Since the regulation appears to demand a *financial guarantee* by the surety that the amount of the bond will be available to

customers when the principal dealer has exhausted his own resources, the Division is forced to question the adequacy of a surety bond which purports to provide coverage only in the event of a statutory violation. It is the Division's position that the surety must serve as the financial guarantor of the principal dealer to the extent of the bond. If the dealer can in any way jeopardize customer funds without violating Chapter 1707, Revised Code, the standard surety bond or any bond covering only statutory violations will be considered inadequate to serve in lieu of the net worth requirements.

A surety bond satisfactory to the Division must incorporate the following conditions:

(i) The amount of the surety bond must be available to meet all obligations regarding securities transactions with the dealer's customers, including but not limited to obligations arising through violation of Section 1707.01 to 1707.45, inclusive;

(ii) The bond must not be cancellable except upon 30 days written notice to the principal and the Division;

(iii) The surety must be bound throughout the statutory period of limitations, i.e., 2 years following the sale or disposition.

B. Safeguarding Dealers' Capital and Segregation of Customers' Funds and Securities.

Regulation DS-5 establishes the basis for continuous supervision of dealers by the Division. It places an affirmative duty on a dealer to perform periodic examinations of its financial condition, and to maintain the standards of financial responsibility prescribed in the regulation.

There are two standards of financial responsibility with which the dealer must comply: (1) its adjusted net worth cannot be less than \$10,000; and (2) its total indebtedness cannot exceed 15 times (1500%) its net worth. When the dealer's financial condition violates either of these requirements investors will not be adequately protected; therefore the dealer must segregate customers' funds and securities in the manner specified in the regulation. However, DS-5 does not apply to an Issuer-Dealer selling its own securities, or to a dealer who has furnished a satisfactory surety bond.

In computing net worth (defined as the difference between total assets and total indebtedness) the regulation requires that certain adjustments be made to "eliminate or adjust assets of doubtful or uncertain value and to reflect true liabilities". This adjustment provision tracks the net worth requirement for applicants in DS-4.

The dealer with an inadequate net worth who fails to follow the procedure for segregating customer funds and securities or whose net worth falls below \$5,000 is deemed to have committed a "grossly unfair practice" which constitutes grounds for suspension or revocation of a license under Revised Code Section 1707.19.

C. Adjustments to Financial Statements.

DS-4 and DS-5 both mandate adjustments in computing net worth; these adjustments are determined according to the schedules provided in DS-10. Under this regulation, certain asset items (listed therein) must be demonstrated as having a "liquidating value" by appropriate substantiation or they will be disallowed as an asset in the net worth computation. Other assets must be reduced or increased in value, but are includable in net worth.

Assets which are disallowed unless a liquidating value is substantiated are the following:

1. Furniture and fixtures;
2. Prepaid items or expenses;
3. Unsecured notes or accounts receivable from salesmen, officers or partners; and
4. Other unsecured notes or accounts receivable.

The rationale behind exclusion absent substantiation is that these items, although assets in the balance sheet sense, would not be readily available to investors or convertible into cash for their benefit without significant delay. Therefore, inclusion of these items in computing net worth would render the statutory net worth requirements inadequate to serve their intended purpose of protecting investors. [Similarly, SEC Rule 15c3-1(c)(2) mandates an exclusion from net worth of assets which cannot be readily converted into cash, including "real estate; furniture and fixtures; exchange memberships; prepaid rent; insurance and expenses; good will; organization expenses; all unsecured advances and loans; customers' unsecured notes and accounts . . ." Although the SEC rule completely disallows the above assets, the Ohio regulation would permit inclusion of most of them in a net worth computation provided there is adequate substantiation to uphold the valuation.]

What constitutes a "liquidating value" which, if substantiated, will permit inclusion of the scheduled assets in computing net worth is unclear. It may be the cash value of the asset as established by an independent broker or an actual market, or it may be the value which would be realized in a forced sale upon seizure of the items.

Asset items listed in DS-10 which can be included in computing net worth, but which must be reduced or increased in value, are the following:

1. Securities owned by the dealer (adjusted to market value);
2. Stock exchange seats (adjusted to market value); and
3. Accounts receivable which are secured by securities with a market value below the value of the account receivable (adjusted to equal the market value of the pledged securities).

Most disputes concerning asset adjustments arise with respect to securities owned by the dealer for which there is a thin or non-existent market. Securities with no trading market ordinarily do not have the capability or expectation of liquidity contemplated by this regulation. See John W. Yoeman, Inc., SEC Rel. No. 34-7525 (1965), '66-'67 CCH FED. SEC. L. REP. paragraph 77,202. In the absence of an organized market, the regulation contemplates clear proof of convertibility into cash. See Brown & Co., Markoff, Steinman & Gowell, Inc., SEC Rel. No. 34-8160 (1967), '66-'67 CCH FED. SEC. L. REP. paragraph 77,471. Therefore, only a firm bid by an independent person would provide an acceptable evaluation for nonmarketable securities.

Similarly, DS-10 permits real estate owned by the dealer to be included as an asset, but the valuation must be supported with appraisals by competent, disinterested persons. While it is often argued that this imposes a hardship on the dealer, the Division has no discretion to accept either a non-independent value or a valuation of the real estate at cost; the assumption that land would not now be valued below the original purchase price is not recognized by the regulation. The appraisal is simply a necessary business expense of the dealer.

Significantly, the regulation does not address itself to the adjustment of liabilities of the dealer. The Division views all such liabilities, where found to be a legal obligation of the dealer, to be a necessary component of the net worth computation.

The Division will permit the inclusion of a loan of cash or marketable securities in a net worth computation so long as the terms of the loan adequately subordinate the lender's interest to the interest of all other customers and creditors of the dealer. What constitutes an adequate subordination agreement will be determined in light of the definition contained in SEC Rule 15c3-1(c)(7)(A-G) under the Exchange Act. The following features of the agreement must be present in order for it to qualify:

- (i) The subject matter of the loan must consist of cash or marketable securities;
- (ii) The agreement must be a written agreement between the dealer and the lender, which is binding and enforceable in accordance with its terms upon and against the lender, his creditors, heirs, executors, administrators, and assigns;
- (iii) The agreement must effectively subordinate any right of the lender to demand or receive payment or return of the cash or securities loaned to the claims of all present and future creditors of the dealer;
- (iv) The cash or securities must be loaned for a term of not less than 1 year;
- (v) The agreement shall not be subject to cancellation by either party and the loan shall not be repaid or the agreement be terminated, rescinded or modified by mutual consent or otherwise if the effect thereof would be to make the agreement inconsistent with the conditions of financial responsibility and net worth contained in Division regulations;

(vi) No default in the payment of interest or in the performance of any other covenant or condition by the dealer shall have the effect of accelerating the maturity of the indebtedness;

(vii) Any notes or other written instruments evidencing the indebtedness shall bear on their face an appropriate legend stating that such notes or instruments are issued subject to the provisions of a subordination agreement which shall be adequately referred to and incorporated by reference;

(viii) The cash or securities loaned to the dealer pursuant to this agreement may be used and dealt with by the dealer as part of his capital and shall be subject to the risks of the business. All such subordination agreements must be submitted to the Division within 10 days after execution. The agreement must be signed by each party thereto and each signature must be acknowledged before a notary public. In addition to the written agreement, the parties must submit an opinion of counsel covering the following:

- (i) In the case of a corporate lender, the existence of corporate authority to enter into the agreement and due execution thereof by corporate officers;
- (ii) The binding effect of the agreement upon the parties thereto;
- (iii) The good and unencumbered title of the lender to the cash or securities which are the subject of the loan;
- (iv) Satisfactory evidence that the dealer has reflected the existence of the subordinated obligation by appropriate identification on his books in a special account.

III. Books and Records.

Regulation DS-6 requires a dealer to maintain records that would enable the Division to determine its financial condition. In addition, a dealer must note fully such items as all customer transactions, complaints and free credit balances, and must keep records of all securities held (for safekeeping or otherwise) by the dealer.

The Division regards the adequacy of records as a significant factor in its evaluation of a dealer's fitness to continue to hold its license. The availability of records has become a problem, especially in the case of non-resident dealers such as developers of foreign real estate which carry on extensive marketing programs in this state. Under DS-6, if the non-resident dealer has a branch office in Ohio it must maintain adequate records at such branch office. The Division may waive this requirement where a non-resident dealer with its principal accounting office outside the state enters into an undertaking (1) to produce all pertinent records on request by the Division, or alternatively, (2) to provide upon request the funds necessary for the Division to perform an examination at the site where the books and records are maintained.

The dealer's records must also contain a current list of all licensed salesmen employed by the dealer. The term "salesman" is defined in Section 1707.01(F) to include "every person, other than a dealer, employed, authorized, or

appointed by a dealer to sell securities within this state". Subparagraph 2 of this Section exempts certain key individuals, such as general partners of a partnership and executive officers of a corporation, from the definition of salesman. However, where the Division determines that there is an element of public protection involved, it may require such person to qualify for a license. The Division has set up the following categories of persons to whom the licensing process applies:

1. Salesmen operating within this state must be licensed and must be working for the dealer specified on their initial application or application to transfer salesman's license. (Form 16.)
2. Principals, i.e., general partners of a partnership, executive officers of a corporation, or sales managers for a local branch office, who are active in sales must obtain a salesman's license.
3. At least one principal of the dealer must obtain a dealer's license on behalf of the dealer. The Division will not limit the number of principals eligible to obtain a dealer's license on behalf of the dealer. In other words, it is a discretionary matter with the dealer as to how many principals (except those active in sales) may obtain a dealer's license.

IV. Reporting.

Under the provisions of Regulation DS-9 (paragraph C), all licensed dealers are required to submit "from time to time upon order of the Division" a report of the financial condition of the dealer. If the dealer is presently reporting to the SEC or a national securities association, it may file a manually signed and verified duplicate of such report with the Division. [DS-9, paragraph (C)(3)].

Paragraph C(2) establishes the requirement that at least one financial report filed in every calendar year by every dealer reporting to the SEC or any national securities exchange of which it is a member must be "certified by a certified public accountant or a public accountant who shall be in fact independent". In addition, paragraph C(2)(I)(B)(i-iii) provides that where a dealer (1) extends credit in any form to customers, (2) holds securities owned by customers, or (3) carries credit balances of customers, an annual "certified" financial statement is required.

With respect to every other type of dealer (usually intrastate dealers which do not carry on any of the three above-listed activities), a "certified" report must be filed "during each calendar year". The Division has discretion to waive this requirement of "certification" of financial statements. However, this waiver is limited to each instance of reporting and the waiver can be granted only in response to a written application showing "good cause" for such waiver. It is beyond the Division's power to waive the "certification" requirement unless the dealer has submitted at least one "certified" report from an independent accountant in its operating history. Additional reports, which are prepared upon order by the Division, may be filed without an audit so long as they are prepared by an independent accountant. The accountant's qualifications [paragraph

C(5)] require such person to be registered and in good standing under the laws of his residence or principal place of business. The test for independence is not defined in the regulation. However, the Division would regard a business association in an active managerial or executive capacity or a close family relationship as potential grounds for determining that such accountant is not independent.

The Division has consistently received financial reports which are deficient on their face due to the absence of an independent accountant's unqualified opinion and there has been no attempt to secure a waiver of this requirement. Such a deficiency in the reporting process provides grounds for suspension and/or revocation of the dealer's license.

It is the policy of the Division to monitor the activities and financial condition of dealers through an active process of examination and request for compliance. Division Orders in the form of semi-annual "call letters" requesting financial statements to be filed under DS-9 [now designated COs-1-07(I)] are typically sent in March and October of each year.

In the Division's experience with DS-9, the major problems have arisen in the intrastate dealer area; there have been difficulties with both timely receipt and adequacy of such reports. The call letter requests a financial statement as of the end of the calendar year quarter just passed, (i.e., September 30 or March 31,) and must be submitted within 30 days of receipt by the dealer. Where no report is submitted within this period, the Division will seek compliance by notifying the dealer of the failure to submit a timely report. If a satisfactory result is not reached in this administrative fashion, the Division will seek a suspension of the dealer's license for refusal to comply with a lawful order or requirement, conduct in violation of a prescribed regulation, and failure to furnish the Division with requested information (Section 1707.19, Revised Code).

The Division may extend the due date of this report, but not to a time later than the "semi-annual period within which his financial condition is to be reported". [DS-9, paragraph C(4)]. For example, the spring call, due April 30 and current to March 31, could be extended to no later than June 30 of that year. The extension may be necessary to allow the dealer to fit this reporting obligation into its fiscal operating year.

IV. Conclusion.

The ultimate objective of the Broker/Dealer Section of the Division is to provide uniform interpretation and application of the regulations relevant to licenses. The foregoing analysis seeks to treat specific questions involved in establishing financial responsibility, record keeping and reporting obligations of dealers to advance the goal of uniformity. Unless an express exemption exists, the Section will require all licensees to comply with all applicable regulations. The Division will continue to refine and publish its interpretations of the regulations in order that dealers will know and understand their obligations.

Alan P. Baden

Ohio Foreign Real Estate Offering Circular

The Division has been engaged in preparing a form of Offering Circular to be used in connection with the offering of foreign real estate or interests therein to residents of the State of Ohio. The following proposed format of the Offering Circular is designed to be used in connection with offerings of foreign real estate or interests therein in the form of lots, parcels, or acreage, whether improved or unimproved, excepting offerings of houses, condominiums and other human dwelling units.

The purpose of this document is to provide the investor with all material and relevant facts which are prerequisite to the formulation of a prudent and intelligent investment decision, in an understandable and utilizable format.

Future issues of the **Bulletin** will contain additions to this Offering Circular to be used in connection with the offering of houses, condominiums and other residential property.

All Form 33 applications currently pending regarding such lots, parcels or acreage which will be modified by pre-effective amendment after August 1, 1974, will be required to use the Ohio Foreign Real Estate Offering Circular, as will new applications regarding such lots, parcels or acreage filed after August 1, 1974.

In addition, Form 33 registrants of such lots, parcels and acreage under pre-existing Division Orders will be required to use the Offering Circular upon request for amendments to original Division Orders, involving price increases and other matters which require a re-evaluation of the application.

Registrants of lots, parcels or acreage under pre-existing Division Orders submitting advertising pursuant to the terms thereof will be required to phase in the use of the Offering Circular over a sixty to ninety-day period.

The Division invites written comments by interested parties, regarding the following proposed format:

	Price to Public	Selling Commissions and Discounts	Proceeds to Registrant
Per Unit			
Total			
	Average Per Unit Price to Public	Total Price to Public	
Completed Improvements			
Promised Improvements			

General Instructions

A. Documents comprising submissions pursuant to Form 33.

The following documents must be included in the submission to the Division pursuant to this form:

1. Form 33
2. Ohio Foreign Real Estate Offering Circular
3. Exhibits
4. Undertakings, agreements, and such other documents as the Division may require as a condition of registration.

B. Use of Photographs, Charts and Illustrations.

1. The format contemplates the use of photographs, charts and illustrations which reasonably depict the property and its state of development accompanied by narrative text appearing on the respective opposite page in accordance with the prescriptions of the format.
2. All photographs should be taken at the site of the development. Photographs not taken on the site will only be permitted at the discretion of the Division for good cause shown.

Item No. 1 Content and Form of Cover Page

A. No more than 35% of the cover page of the Offering Circular may be comprised of photographs or artist's renderings.

B. The cover page shall clearly indicate the name of the applicant as specified in the governing documents, the address of the applicant and the telephone number of the applicant for customer service or complaints. If the applicant is not the owner of the subject property, the foregoing information shall also be stated for such owner.

C. The information required by the following table must appear on the cover page of the Offering Circular in substantially the form indicated:

Instructions:

1. In the event that all units of the property are not offered at the same price, the per-unit price of each category of units should be stated, together with the number of such units in each price category.
2. "Selling commissions and discounts" shall include all commissions, allowances, discounts, fees, expenses or other compensation or remuneration in any form which have been arranged, agreed or proposed to be paid or given, directly or indirectly, by the owner, developer, or any person interested in the property to or on behalf of any dealer, affiliate of a dealer, salesman or any finder in connection with the subject offering.

D. The name, address and telephone number of all dealers licensed by the State of Ohio, including the developer, if applicable, who are or will be engaged in connection with the subject offering shall appear at the bottom of the cover page to the Offering Circular.

E. The Division may require disclosure of any risk or special factors on the cover page of the Offering Circular.

Item No. 2 Summary Information.

A. The first page of the Offering Circular immediately following the reverse side of the cover page should contain a brief summary of the following items, referencing the reader to more detailed information in the text of the Offering Circular.

1. Name of applicant and developer
2. General location of real estate offered
3. Total number of units or parcels offered
4. Total amount of acreage
5. Existing improvements (if the property is not improved, clearly indicate)
6. Promised improvements and completion date
7. Salient risk factors
8. Unfair and deceptive practices
9. Suitability standards
10. Terms of sale
11. Annual estimated cost of ownership including principal and interest payments, dues, taxes, assessments, and other costs.
12. Financing information
13. Such other information as the Division may require.

Item No. 3 Table of Contents**Item No. 4 Risk Factors and Special Considerations.**

A. In a series of short, concise paragraphs, summarize the principal risks, uncertainties, and speculative factors inherent in the offering, development and ownership of the property.

By way of illustration and not limitation the following items should be summarized pursuant to this item:

1. Encumbrances, restrictions, covenants, conditions, easements, zoning and other factors affecting the use of the subject property by purchasers.
2. Topographical or geographical factors affecting the use of the property including the percentage of such property which is marsh, muck, swamp or subject to ponding.
3. Other factors affecting suitability of the property for intended or implied prospective uses.
4. Factors upon which the installation of promised improvements are contingent, including financial condition of the developer.
5. Pending legal or administrative actions and proceedings which may affect the developer's ability to complete the promised improvements, or fulfill other commitments relating to the property or which are otherwise material to an investment decision.
6. The absence of a resale market for the property interest offered.
7. Refund or rescission provisions, if any.
8. Unfair and deceptive sales practices common to the industry, or the developer.
9. Suitability standards.
10. Terms of sale.

Item No. 5 Description of Real Estate.**A. General Location**

1. Indicate the location of the subject property, specifically with reference to the nearest city and designate approximate population thereof and distance therefrom.
2. Indicate the type, quantity and quality of surrounding development.
3. Indicate in terms of both miles and minutes by car, the distance of the subject property from:
 - a. the nearest central business district;
 - b. employment centers;
 - c. existing schools.
4. Describe fully and completely the highway access of and to the subject property, whether any portion of the prop-

erty abuts a major thoroughfare, and the patterns of traffic flow with respect to:

- a. local streets and roads;
- b. highways and freeways.

5. State which of the services and facilities set forth below are available or accessible to the property. If these services and facilities are not available or accessible to all of the property, state the number of lots, parcels, or units of the property to which these services are available or accessible.

Describe fully such services and facilities which are now actually available or in existence, including, where appropriate, the cost and method of financing such service or facility. Such description should include, but not be limited to the following:

- a. fire protection;
- b. police protection;
- c. garbage and trash collection;
- d. shopping and commercial facilities;
- e. public schools;
 - 1. elementary
 - 2. junior high
 - 3. high school
- f. medical and dental facilities;
 - 1. hospital
 - 2. clinics
 - 3. physicians and dentists
- g. public transportation;
- h. U.S. Postal Service;
- i. recreational facilities.

6. Location Map

Provide a map, drawn to scale, indicating, in relation to the subject property, the location of the nearest city, all highways and other features discussed in the text of the Offering Circular pursuant to the requirements of this Item 5A. This map shall not be less than one full page of the Offering Circular.

B. Physical characteristics of the property:

1. Describe the topography of the property, whether the property is hilly, rolling and/or level, and the extent of such characteristics. Include relevant dates on the highest point, the lowest point and the average elevation and describe fully and completely the extent of any slope on or affecting the subject property.

2. Describe fully and completely any and all other relevant and material physical characteristics or features of the subject property, including specifically, but not limited to the following:

- a. The existence of lakes, ponds, swamps or marsh;
- b. Surface drainage;
- c. Flood plain;
- d. Steep ravines or gullies;
- e. Type of soil, including the results of any percolation tests;
- f. Rock outcropping;

- g. Soil stability, including the results of any soil borings;
- h. Tree growth, e.g., heavy, sparse, scrub, open — describe;
- i. Whether the subject site is adaptable to conventional construction without grading or cutting for building sites or streets and if not, the extent of grading and cutting necessary.

If the subject tracts must be cleared, drained, graded, filled, or otherwise physically modified to permit the use of conventional building techniques, a description of the extent and estimated cost thereof should be included.

C. Basic Improvements

1. Fully describe and explain all basic improvements to the property which are currently existing or promised, including location, stage of completion and availability for use. Include in the Offering Circular a table listing such basic improvements in the form set forth in Item 5F below.

For purposes of this Item 5, "basic improvements" shall be defined to include the following:

- a. graded streets;
- b. paved streets;
- c. electrical service;
- d. central water supply;
- e. sanitary sewer and/or septic tank (if sewer, state the number, average distance, size and invert of the nearest main or if sewers will not be installed, state whether the condition of the soil will permit septic tanks);
- f. drainage and storm sewers;
- g. curbs and gutters;
- h. sidewalks;
- i. street lighting;
- j. gas supply;
- k. telephone service;
- l. parking facilities.

D. Completed Recreational Improvements

1. Fully describe and explain all promised recreational improvements to or serving the property which are not presently completed and available for use including location, who retains ownership and responsibility for the maintenance of these improvements and the cost to the purchaser for the use of the same. For purposes of this Item 5, "recreational improvements" shall be defined to include, without limitation, the following:

- a. golf course;
- b. swimming pool;
- c. tennis courts;
- d. marina;
- e. canals, waterways;
- f. hiking trails;
- g. bridle trails;
- h. fishing areas;
- i. ski areas;
- j. open or wooded areas;
- k. cable television;
- l. community building or club house;
- m. pro shop, locker rooms;
- n. exercise facilities.

E. Promised Recreational Improvements

Fully describe and explain all promised recreational improvements to or serving the property which are not presently completed and available for use including location, stage of completion, estimated cost to complete, completion commitment date, fees or cost to the purchaser for use of the same and who retains ownership and responsibility for the maintenance of these improvements. Include in the Offering Circular a table listing such recreational improvements in the form set forth in Item 5F below to be completed, indicating location, estimated cost, completion commitment date.

F. Table of Basic and Recreational Improvements

The Table should include the following items: Description of Improvement, Location (Completed), Percent Complete/Proposed, Certified Cost, and Completion Commitment Date For All Improvements.

G. Development and Use Restrictions

Describe fully and completely all restrictions imposed upon or relating to development and use of the subject property including:

1. Zoning classification of the subject property and contiguous or nearby tracts, and whether the same have been complied with.
2. Compliance by the owner and developer with all laws, ordinances, rules and regulations of the federal, state and municipal governments and regulatory agencies relating to the use and development of the property.
3. Any restrictions or regulations imposed by federal, state or local laws, ordinances, rules, regulations or governmental agencies which may materially affect the purchaser's use and development of the subject property, including housing or building codes.
4. Encumbrances with respect to the subject property and contiguous or adjacent tracts or other parcels of land owned by developer which may affect the subject property.
5. Covenants, conditions, restrictions, easements, rights, etc., affecting the subject property.
6. The existence of any special districts with the power of taxation or levy.
7. If an Environmental Impact Statement is required to be filed under the National Environmental Policy Act, a description of the considerations, restrictions and recommendations made therein should be provided hereunder.

H. Acquisition and Financing

1. Describe briefly the transaction whereby the owner acquired the subject property, including the grantor thereof, price, and other financial considerations thereof, including the terms of any acquisition loans obtained by the owner.

2. If the owner or the developer of the property or any affiliate owns, or has options to purchase, land adjacent or nearby the property, describe the same.

3. Describe the terms of any loans or any commitments obtained by the owner for any construction or permanent financing of the subject property and improvements.

I. Public Health, Safety and Welfare

Describe any and all factors, considerations, or conditions that would directly or indirectly have a bearing upon the health, safety and welfare of residents of the subject property, including but not limited to the following:

- a. fire hazard;
- b. water supply;
- c. flood plain;
- d. industrial smoke;
- e. pollution;
- f. proximity to airport flight patterns;
- g. unsightly views;
- h. other possible adverse influences;
- i. pleasant scenery.

J. Disclosure Map

A detailed map of the property including but not limited to the following information must be included in the Offering Circular.

- a. location of respective lots, parcels or units;
- b. existing basic improvements;
- c. existing recreational improvements;
- d. existence of marsh, muck, swamp, excessive slope, ravines, gullies and other surface conditions affecting immediate use of or development of the property.

K. Aerial Photographs

The Offering Circular must contain an aerial photograph, taken within thirty (30) days of the date of the application which reasonably shows the existing state of the subject property and improvements.

In the event that the improvements described in Items 6C and E are not presently completed, such photograph shall be updated every ninety (90) days subsequent to the effectiveness of the application until all such improvements are completed. Such photograph shall also be updated to depict the existing state of such property and improvements in the event of a material change in the same.

Item No. 6 Information with Respect to the Developer, Subsidiaries, Affiliates and Controlling Persons

- A. State the year in which the developer was organized, its form of organization, (i.e. - corporation, etc.,) and the state or other jurisdiction of its organization.
- B. Briefly describe the business conducted and intended to

be conducted by the developer, its subsidiaries and affiliates.

A description of the business of the subsidiaries and affiliates of the developer should be included only to the extent relevant to material aspects of the offering.

C. List the names, addresses, and business history for the past ten (10) years of all officers, directors, and controlling persons of the developer.

If developer is a subsidiary or otherwise controlled by another legal entity, which has effective control of developer's business policies, the information required by Items 6A, B, and C must be given with respect to such entity.

D. Summarize any pending or threatened legal or administrative actions or proceedings with respect to the owner, developer, parent, subsidiaries, officers, directors, affiliates, and controlling persons which may affect directly or indirectly any material relevant aspect or feature of the offering, plan of development or which may be material to the formulation of an intelligent investment decision.

Additionally, if any of the entities or persons listed above have been involved in any administrative or legal proceedings within the last five years which relate to the offer for sale, or sale of securities, real estate or other consumer products, summarize the same.

E. Complaints

1. State the number and provide a general description of complaints by consumers or purchasers of real estate or products of developer within past five years.

2. Indicate the developer's established criteria, procedures, and policies with respect to complaints which may arise in connection with the sale or the interest offered.

F. Financial Information

The offering circular must include an audited balance sheet, income statement and source and use of funds statement prepared by an independent certified public accountant in accordance with generally accepted accounting principles and accompanied by an opinion thereon for the developer.

If the developer is controlled by another entity, the above financial information must be provided for such entity.

If the developer has any subsidiaries or affiliates who are materially involved in the plan of development, the above required financial information must be provided for such entities.

G. If the developer is not the person applying for the qualification of the offering with the State of Ohio, then the information required by this Item 6 shall also be stated in regard to the applicant.

Item No. 7 Marketing Program

A. Plan of Distribution

1. Fully describe the program whereby units of the subject property or interests therein will be offered to Ohio residents.

2. List the names, addresses, and telephone numbers of all dealers engaged in such Ohio offering.

3. Items A, C, and D of Item No. 6 hereof, should be included herein.

B. Information with respect to salesmen.

The following information with respect to each salesman must be included in the Offering Circular by way of an attachable insert prior to the delivery of such Circular to Ohio residents.

1. Full name, address and telephone number;

2. Personal history for past five years;

3. If the salesman has been involved in any administrative or legal proceedings within the last five years relating to the offering or sale of securities, or real estate or interests therein, describe the same;

4. A summary of all complaints filed against such salesman within the past two years relating to the offering or sale of securities, real estate or interests therein;

5. Whether or not such salesman has visited the property and if so, when;

6. The number appearing on his salesman license issued by the Ohio Division of Securities.

C. Information with respect to each broker engaged in the subject offering to Ohio residents.

1. The dealer's established criteria, procedures and methods for dealing with complaints and inquiries from purchasers of the property;

2. If the broker has been involved in any administrative or legal proceedings within the last five years relating to the offering or sale of securities, or real estate or interests therein, describe the same;

3. A summary of all complaints filed against the dealer within the past two years arising in connection with the offering of securities, or real estate or interests therein by such broker, employees or salesmen of such dealer.

Item No. 8 Use of Proceeds to Applicant

State the specific principal uses and purposes for which the net proceeds to the developer from the subject offering are intended to be used.

If any material amounts of other funds are to be used in conjunction with the proceeds, state the amount and source of such other funds.

The foregoing information must be presented in the form of a table with footnotes or following narrative if appropriate.

Item No. 9 Definitions

Technical terms and terms which are uncommon to normal usage should be clearly defined in the forepart of the Offering Circular.

Item No. 10 Secondary Market Information

A. Indicate whether the developer, its affiliates, or subsidiaries makes a secondary market in the subject property or interests therein being offered.

If the developer does provide a secondary market, fully describe the procedures and current listings and prices therefor.

B. List names and addresses of all persons who are principal secondary market makers in the property being offered or similar property.

A "principal secondary market maker" is one who currently has ten or more lots, units, parcels or interests listed and who has effected at least three transactions within the past six (6) months.

C. For each person listed above, a description of the listed property or a summary of the types of property, and the price therefor must be provided.

Item No. 11 Information with Respect to Locality

A. Population

Specify the population of the county in which the subject property is situated. Also specify the population of such county at five (5) year intervals for the past ten (10) years.

B. Employment Base

Briefly describe the county's principal employers, the current number of persons employed by each such employer, and whether such employers are proposing to increase or reduce the number of persons they employ in the immediate future.

C. Unemployment Rate

State the unemployment rate for the county in which the subject property is located.

D. Local Real Estate Market

Specify the average price at which property similar to that being offered is currently sold.

If the property being offered is presently unimproved, the price of comparable acreage should also be listed.

E. Describe any conditions or development occurring in the

county which may affect the value of the subject property.

Item No. 12 Terms of Sale

The format of the Ohio Offering Circular contemplates the use of the purchase agreement in accordance with Item 13 hereof. Accordingly, this Item 12 should include all terms, conditions of sale which would normally be found in a contract for the purchase and sale of real property.

Minimally, the following shall be stated:

A. A description of the property offered.

B. The interest in the property being offered (i.e., fee simple, leasehold).

C. Terms of Sale.

D. A description of the title insurance policy to be issued to the purchaser or, in the event that an abstract of title will be provided, a description of the opinion of counsel to be given upon an examination of such abstract. Such description shall include all liens, encumbrances, easements, covenants, conditions, restrictions on the property and all other exceptions to title which will appear in such title insurance policy or opinion.

E. Deposit provisions.

F. Provisions for possession of the property by the purchaser.

G. Provisions for proration of taxes, assessments, and rents and utilities, if any.

H. Payment of closing costs.

I. Provisions relating to damage or destruction of the property prior to the date of closing.

J. A copy of the form of the instrument of conveyance to be delivered to the purchaser.

K. A copy of the affidavit to be delivered to the purchaser made by or on behalf of the seller stating facts relating to title to the property and the validity of the execution of the instrument of conveyance delivered to the purchasers.

L. Truth-in-Lending information in accordance with Regulation Z.

M. The rescission rights included in the order qualifying the offering under the laws of the State of Ohio.

N. Covenant of the seller to complete the improvements noted in Item 5E of the Offering Circular and any improvements noted in Item 5C of the Offering Circular which are not yet completed and available for use on the respective completion commitment dates indicated therein as described, in a good and workmanlike manner, using high quality materials and obtaining all permits, approvals and acceptances required to be obtained from any governmental

authority having jurisdiction over such improvements.

O. Covenant of the seller that the improvements noted in Item 5D of the Offering Circular and the improvements noted in Item 5C of the Offering Circular which are completed and available for use have been constructed as described in a good and workmanlike manner using high quality materials and that all permits, approvals and acceptances required to be obtained from any governmental authority having jurisdiction over such improvements have been obtained.

P. A provision that all of the statements and representations set forth in the Offering Circular are made a part of the terms and conditions of the subject sale or other disposition of the property or interest therein being offered.

Q. A provision that the covenants and representations of the seller noted in this Item 12 shall survive the closing of the subject transaction.

Item No. 13 Purchase Agreement

The purchase agreement, which is required to appear in triplicate in the rear of the Offering Circular in substantially the form set forth below, shall be the sole and exclusive contract for the acquisition of the property or any interest therein pursuant to the subject offering.

_____ (hereinafter called the "Purchaser" whether one or more) hereby agrees to purchase and _____ (hereinafter called the "Seller" whether one or more) hereby agrees to sell, for the purchase price of _____ and upon the terms and conditions noted and set forth in Item 12 of the Offering Circular dated _____, which is incorporated herein and made part hereof, the following described real property together with all improvements and appurtenances thereto:

Purchaser and Seller hereby agree that this Purchase Agreement, together with Item 12 of the Offering Circular incorporated herein, shall constitute the entire agreement of the parties, and that no other written, oral or implied agreements or understandings shall vary the terms hereof.

The transaction which is the subject of this agreement shall be closed on _____ or within ten (10) days thereafter at such place as the Purchaser shall designate.

Purchaser and Seller further hereby agree that this agreement shall be construed and enforced according to the laws of the State of Ohio.

In witness whereof, the parties hereto have set their names or caused these presents to be executed this _____ day of _____, 19 _____.

Purchaser

Seller

Policies Applicable to the Regulation of Investment Companies in Ohio

1. Regulation Q-3 (COs-1-06) applies to all investment companies, including investment trusts and both open-end and closed-end management companies. All Sections of the Regulation apply to open-end companies, and all Sections with the exception of Sections A(20), (21), and (23) apply to closed-end companies. This regulation deals with conflicts of interest (Sections A(1)-(4)), custodial arrangements (Sections A(5)-(7)), investment restrictions (Sections A(8)-(17)), and management practices, including fees, commissions and reporting requirements (Sections A(18)-(25)).

2. The application of Section B of Regulation Q-3 is as follows:

A. All companies registered pursuant to the Investment Company Act of 1940 are automatically exempt from the Sections of Regulation Q-3 enumerated in Section B(1);

B. In addition, such companies may exempt themselves from the remaining Sections of Regulation Q-3 with the exception of Section A(22) by means of a majority vote of shareholders through the process described in Section B(2) (a);

C. Section B(2) (b) is not interpreted to allow, as an alternative, exemption from the remainder of such provisions merely by filing a recital of policy pursuant to the registration requirements of Section 8 of the Investment Company Act. This provision serves only as an alternative to the means outlined in Section A of the Regulation for the demonstrating compliance with the enumerated Sections.

3. Ohio also applies the National Association of Securities Administrators Regulations for Open-End Investment Companies (effective January 1, 1953). These regulations govern (1) income and capital gains distributions, (2) accounting practices, (3) redemptions, and (4) tips, give-ups, discounts, and reciprocal business arrangements, all of which are matters outside the scope of and therefore not inconsistent with the provisions of Regulation Q-3. Furthermore, Ohio applies the Central Securities Administrator's Council Statement of Policy on Open-End Investment Companies (effective August 31, 1971) to the extent that it is not inconsistent with the provisions of Regulation Q-3. This Statement of Policy deals with (1) investment restrictions (Section A), (2) disclosure of investment risks (Section B), (3) expense limitations (Section C), (4) minimum size (Section D), (5) redemptions (Section E), and (6) brokerage transactions (Section F). Specifically, Sections A(2) (a) and (c), A(3) (a), (b), and (c), A(4), B(2), (3), and (4), and D apply to supplement the requirements of Regulation Q-3. The remaining Sections of the Statement of Policy are inapplicable since the requirements of Sections A(1) (b), (9), (12), (15), (17), (21), and (22) of Regulation Q-3 apply.

4. In addition, Ohio applies the Central Securities Administrators Council Statement of Policy on Closed-End Investment Companies (effective August 14, 1973) to the extent that it is not inconsistent with the provisions of Regulation Q-3. This Statement of Policy deals with (1) investment restrictions (Section 2(a) and (b)), conflicts of interest (Section 2(c)), and disclosure of investment risks (Section 3). Specifically, Sections 2(a)(1), (2), and (3) and 3(a), (c), (d), and (e) apply to supplement the requirements of Regulation Q-3. The remaining Sections of the Statement of Policy are inapplicable since the requirements of Sections A(1)(b), (9), (10), (11), and (12) of Regulation Q-3 apply.

5. Regulation Q-3 does not bind the Division in the exercise of its discretion with respect to the approval or denial of registration applications. In appropriate circumstances, the Division may waive specific requirements of this Regulation. (Effective April 10, 1974, the Division is, upon request, waiving the requirements of Sections A(5) and (7) of Regulation Q-3 to the extent that such Section prohibits the lending of portfolio securities.) The Division also reserves the right to deny registration to companies which comply with all of the requirements of Regulation Q-3 where such action would be warranted on other grounds.

6. The Division is currently reviewing the policies represented by Regulation Q-3 with a view to completing a comprehensive revision of this Regulation before the end of the current year. The Sections of Regulation Q-3 which are currently the subject of the greatest amount of controversy are Sections A(9), (10), (12), (13), and (17) involving restrictions upon investment practices and Sections A(20), (21), and (22) involving limitations upon commissions, redemption fees, and charges for operating expenses, including management fees. Although, at this point the Division is inclined to view the Investment Company Act of 1940 as providing substantial protection for purchasers of investment company shares and intends generally to hold substantive restrictions beyond those provided for by the Investment Company Act to a minimum in the revised Regulation, it is likely that the Division will continue to implement some form of restriction upon industry practices in these two important areas. Nevertheless, a relaxation of certain restrictions (e.g., the limitation upon borrowing (Section A(9)) can be expected.

William L. Case, III

INTERPRETATIVE OPINION

Employee Stock Options and Stock Purchase Plans

The Division has been applying since April, 1974 a policy concerning employee stock option plans and employee stock purchase plans in accordance with the following opinion:

1. Employee Stock Option Plans

The Division will now acknowledge an exemption from dealer licensing for those option plans where the underlying securities are: (1) exempt; (2) the subject matter of an

exempt transaction; (3) registered by description; (4) registered by qualification; (5) the subject matter of a transaction which has been registered by description; or (6) not available pursuant to exercise until they are (a) exempt; (b) subject matter of an exempt transaction, (c) registered by description, (d) registered by qualification, or (e) the subject matter of a transaction which has been registered by description.

This result is obtained through the operation of Sections 1707.03(G)(2), 1707.03(G)(3), and 1707.03(I) and 1707.14(B)(1), Ohio Revised Code. Section 1707.03(G)(2) provides:

"The giving of any subscription right, warrant, or option to purchase a security or right to receive a security upon exchange, which security is exempt at the time such right, warrant, or option to purchase or right to receive is given, is the subject matter of an exempt transaction, is registered by description or by qualification, or is the subject matter of transaction which has been registered by description is exempt."

This Section is interpreted by the Division to mean that the granting of a stock option to an employee of a company is an exempt transaction under 1707.03(G)(2) where the exact provisions of that Section, as denoted above, are applicable.

The exercise of that option is exempt pursuant to Section 1707.03(I), which states:

"The delivery of securities by the issuer on the exercise of conversion rights, the sale of securities by the issuer on exercise of subscription rights or of warrants or options to purchase securities . . . is not an exempt transaction *unless* such rights, warrants, or options when granted were the subject matter of an exempt transaction under Division (G) of this Section or were registered by description or by qualification (emphasis added)."

The exemption from registration in Sections 1707.03(G)(2) and 1707.03(I) also follows from Section 1707.03(G)(3), which conditions the exemption for an option upon the restriction that the option is not exercisable until the requirements of Section 1707.03(G)(2) are met. (It should be noted that Section 1707.03(I) is not sufficient to constitute an exemption for underlying securities pursuant to Sections 1707.03(G)(2) and (3). These Sections clearly contemplate an "independent" exemption.)

While Section 1707.03 exempts certain transactions from the registration provisions of the Ohio Securities Act, Section 1707.14 is controlling concerning the dealer licensing requirements. Section 1707.14(B)(1) states:

"No person shall sell securities within this state or engage in the business of buying, selling, or dealing in securities otherwise than in transactions through or with a licensed dealer, unless such person is licensed as a dealer by the Division, except in the following cases:

(1) When the securities are the subject matter of one or more transactions enumerated in divisions (B) to (L), inclusive, and (O) to (Q), inclusive, of Section 1707.03 of the Revised Code."

Therefore, the employee stock option plan exempt under Section 1707.03 is also exempt from dealer licensing under Section 1707.14(B)(1).

Claims for this exempt status may be cleared through the Division of Securities, but no claim of exemption is required to be filed to obtain an exemption pursuant to these Sections.

II. Employee Stock Purchase Plans

The Division is aware of the fact that in the present market stock purchase plans come in many varieties. They often provide for the purchase of the employer's stock by the employee. As with stock option plans, purchase plans usually involve the granting of an "option" to the plan by the issuer. Therefore, 1707.03(G)(2) and 1707.03(G)(3) and 1707.03(I) can be used to create an exemption from registration and dealer licensing for the granting of the option to the plan. However, a problem arises if the "participatory interest" in the plan becomes a separate "security". If this is the case, no exemption from dealer licensing will be available for the offer of the "participatory interest" and the "participatory interest" must be registered.

The Division of Securities, in determining when a "participatory interest" becomes a separate security, has reviewed Securities Act Release Number 33-4790 (July 13, 1965), 1 CCH FED. SEC. L. REP. paragraphs 1131-33. At paragraph 1133, the Securities and Exchange Commission states that under normal circumstances a participatory interest would not constitute a separate security where "the plan involves minimal differences from the manner in which securities are acquired in ordinary brokerage transactions and the rights and obligations of the employee and the broker will be consistent with the ordinary broker-client relationship, which might include the leaving of securities in the custody of the broker or other person performing the same custodial function".

However, the Commission does recognize that separate securities can exist, and states:

"Where substantial variations exist, however, such as limitations on the right of the employee to withdraw from the plan or to withdraw securities held in custody, the granting of management discretion to someone other than the employee, the accumulation of sums for material periods of time before investment, the payment of special fees or charges such as a front-end load, or the diminution of his rights or privileges as a shareholder, a separate security may be created which will be required to be registered under the Securities Act of 1933 and the issuer which may be an investment company required to register under the Investment Company Act of 1940."

The Division believes that this Release provides a suitable guidepost for the interpretive standards which the Division

will apply in defining the term "Security" as it relates to the participatory interests in these employee stock purchase plans.

The Division has encountered several types of plans including thrift plans, bonus plans and employer contribution plans. The Division will consider each plan individually in determining whether or not there is a requirement for registration of the participatory interest and therefore no dealer licensing exemption.

The Division will consider determinative the fact that an issuer has chosen to register a participatory interest separately from the plan with the Securities and Exchange Commission pursuant to the Securities Act of 1933 and thus will require a licensed Ohio Securities Dealer to be involved in a transaction should this occur.

III. Policy and Procedure Concerning Stock Option and Stock Purchase Plans.

The Division feels that its policies and procedures for the qualification of stock options and stock purchase plans developed to date should be expressed at this time. Three basic questions will be addressed in this Section: the registration by description of stock purchase plans pursuant to Section 1707.08, general standards for the review of stock option and stock purchase plans pursuant to Section 1707.09, and finally, broker/dealer licensing requirements.

A. Registrations by Description

The availability of Section 1707.08 for stock purchase plans only becomes a problem where the participatory interests in the plan are deemed to be separate securities. The Division has developed no firm position on the issues or policies enumerated herein and welcomes commentary from the Bar and interested persons.

Registration by description of transactions described in Section 1707.06 carries the "benefit" of Section 1707.06(B), which excludes "issuers" engaging in these transactions from the definition of "dealer". Section 1707.14(B)(2) excepts an issuer who is "not a dealer under 1707.06" from the prohibition against selling securities without a license. Because of the understandable desire of corporations to avoid the burdens of dealer licensing, the analysis of the availability of Section 1707.06 is significant where employee stock purchase plans involving "separate securities" are sought to be registered; dealer licensing would be required with a registration pursuant to Section 1707.09.

Difficulties exist when the requirements of Section 1707.06(A)(1) are applied to such programs. Literally, an Ohio corporation can sell "its securities", (presumably of any class) "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..." Two problems immediately arise. First, are the "participatory interests" securities of the corporation or in other words "its securities"? Second, by the very nature of these plans, are the interests being issued in part for intangibles?

Before undertaking a review of these problems, reference should be made to the commentary of the draftsmen of the Ohio Securities Act. This commentary accompanied the original proposed bill as presented to the legislature by the Ohio State Bar Association's Committee on Blue Sky Law on January 15, 1929. The report and commentary on the Act was published in "The Ohio State Bar Association Report" Volume 1, Number 42 as a supplement.

The commentary states with respect to Section 6(1) [the predecessor of Section 1707.06(A)(1)]:

"This subsection is designed to enable the ordinary, usually small Ohio corporation to dispose of its own securities when such disposal is made without the aid of an expensive sales campaign... The provision against intangibles or property located outside of Ohio is to prevent fictitious valuations... (at p. 51)."

Therefore, while the draftsmen offer no solution to these questions, they display their intention to limit the scope of Section 6(1).

Addressing the first problem, the Division believes the phrase "its securities" in Section 1707.06(A)(1) refers to securities of which the corporation is the issuer. The question of who is the "issuer" of participatory interests, when deemed separate securities, pervades all of Section 1707.06. It is arguable that a corporation which organizes, promotes and operates a stock purchase plan "issues" any and all securities offered pursuant thereto. However, the Division believes that plans which have participatory interests that are separate securities are separate entities from the corporation. These participations are viewed as separate securities because the corporation is acting through a trustee or manager to perform duties other than by acting merely as "broker" or intermediary for the employee. The elements which destroy the mere broker/client relationship, such as limitation of withdrawal rights, managerial discretion as to purchase of investments, accumulation of funds, etc., also cause the plan itself to take on the characteristics of a separate entity from the corporation.

Therefore the Division concludes that the plan, and not the corporation, "issues" the participatory interests which are separate securities, and that the participatory interests are not the securities of the corporation or "its securities".

Second, the requirement of continued employment embodied in most, if not all, employee stock purchase plans is, in the Division's belief, an intangible. Therefore, although the employee contributes cash to the plan at least in part, the employee is contributing an intangible for the participatory interest *and* for any purchase of the corporation's "own" securities (whether equity or debt).

These problems would appear to preclude the use of Section 1707.06(A)(1) *alone* as a basis for a registration by description of both the participatory interest and the underlying securities to be purchased. Because of the complexity of many of these plans, the Division will entertain such a filing, but feels that this interpretation will preclude most plans from availing themselves of Section 1707.06(A)(1) by itself.

Section 1707.06(A)(2) refers to the sale of "shares or subscriptions for its shares". Although arguments could be made that participatory interests are "subscriptions," the Division believes that the restrictions of share ownership to less than fifteen shareholders will render this issue moot. However, assuming arguendo that such an interpretation is possible the Division would deem it at odds with the intent of the draftsmen, "This subsection is to enable the small, closely held company to dispose of its shares among interested parties, usually its organizers, without needless hindrance or obstruction". Share subscriptions certainly involve far less complexity than participatory interests in an employee stock purchase plan. Therefore the Division will not conscience the use of Section 1707.06(A)(2) for the basis of a registration by description.

Obviously, Section 1707.06(A)(3) cannot suffice to register the underlying shares of the corporation. However, a combination of Section 1707.06(A)(2) and Section 1707.06(A)(3) would appear, at a minimum, to cover the registerable transactions in a stock purchase plan where the participatory interests are separate securities, because Section 1707.06(A)(3) permits a corporation to register the offering of securities of an unincorporated association (the plan). If a corporation would have less than fifteen shareholders after the employees had purchased shares through the plan and if there were no more than ten participants in the plan itself, the plan could theoretically qualify the plan through a registration by description. Although no form is currently available for a "combination" filing, the Division is theoretically willing to acknowledge such a filing as being within the statutory framework and legislative intent of Section 1707.06.

B. Filings Pursuant to Section 1707.09

The second question is what general standards the Division will apply to registration of stock option and stock purchase plans pursuant to Section 1707.09. All plans will be subjected to a review for fairness in accordance with the Division's current guidelines for corporate offerings.

Where the plan is filed with the SEC, Form S-8 will suffice as a disclosure document. For all qualified plans (i.e., plans intended to qualify under Sections 421 and 423 of the Internal Revenue Code), the Division will require an opinion of counsel that the plan does so qualify.

Should a stock purchase plan involve the purchase of securities other than those of the employer corporation, the plan must specify the limitation and guidelines to be used in determining what securities are to be purchased.

C. Dealer Licensing

Finally, where an Ohio licensed broker/dealer is required to make all offers, the corporation may obtain a dealer's license. This should be obtained through the corporate officer directly responsible for the operation of the plan. The requirement that the corporation obtain the dealer's license does not resolve the question raised earlier of who is the "issuer".

For the licensing procedure, reference should be made to the procedure outlined for corporate reorganizations at pages 25-6 July, 1973 **Ohio Securities Bulletin**. Briefly

restated, the applicant should submit the usual application form to the Division and note clearly that the application is for the exclusive purpose of offering and administering an employee stock purchase plan. The corporate officer responsible for administering the plan will be required to take an examination with the aid of reference materials, but without assistance from any person. This examination will differ materially from examinations given to other dealer applicants. Minimum capital requirements with respect to the officer who will administer the plan need not be met, but other information which is required by statute, must be provided in the application. The applicant must publish the application by sending a proof of publication form to a daily newspaper of general circulation in the city where the applicant's principal place of business in this state is located, or to a newspaper of general circulation in Columbus, Ohio, if the applicant has no such place of business in this state. When the examination is returned by the officer along with an oath attesting that he alone took the test, and if proof of publication is returned to the Division indicating that one week has passed since the application appeared in an appropriate newspaper, the license will be issued and the officer responsible for administering the plan will be permitted to offer interests in this plan and purchase stock thereunder.

Alan P. Baden

THE SECTIONS

FOREIGN REAL ESTATE SECTION

This article will attempt to summarize the current status of the several regulatory projects now in progress and secondarily to provide interested parties with an indication of the Division's attitude with respect to the direction of the regulation of the foreign real estate industry in general terms.

Initially, the Division wishes to reaffirm its standing policy of inviting comments by interested parties as to suggested topics warranting discussion in the **Bulletin**, policy developments, and general comment, in the interest of bringing about an appropriate dialogue between the Division and interested parties.

Current Developments

A. Reporting Requirements

On July 8, 1974, the Division suspended twenty-five registrants for failure to file ninety-day periodic reports of progress concerning the subdivisions being sold in this state. This is the first phase of a continuing project which is anticipated to eventually affect approximately one hundred fifty (150) registrants who have not filed quarterly reports or whose reports are grossly inadequate as filed.

Registrants in the latter category will be notified by wire, no less than ten days prior to suspension, to allow time to correct deficiencies if it is apparent to the Division that a "good faith" attempt at compliance was made.

This suspension project reflects the priority the Division has attached to the reporting of current financial information

and the progress of development. Presently, any registrant not filing the required reports will be automatically suspended.

During the remaining days of the month of July, the Division will review reports submitted, in detail, to ascertain whether or not registrants have met developmental commitments, as represented to Ohio investors.

B. Proposed Format for Offering Circular

This issue of the **Bulletin** contains the proposed format for the Ohio Foreign Real Estate Offering Circular. The Division is of the opinion that this format will help insure full and fair disclosure at the point of sale and will further serve to abate fraudulent and deceptive practices in connection with the sale of foreign real estate by providing purchasers with all pertinent information prior to the consummation of sale.

The proposed format of the offering circular is designed to be used in connection with offerings of foreign real estate or interests therein in the form of lots, parcels, or acreage, whether improved or unimproved, excepting offerings of houses, condominiums and other human dwelling units.

All Form 33 applications for the registration of such lots, parcels, or acreage, which will be modified by pre-effective amendment after August 1, 1974, will be required to use the Ohio Foreign Real Estate Offering Circular, as will such new applications filed after August 1, 1974.

In addition, Form 33 registrants under pre-existing Division Orders will be required to use the Offering Circular upon request for amendments to original Division Orders involving price increases and other matters which require a re-evaluation of the application.

Registrants under pre-existing Division Orders submitting advertising pursuant to the terms thereof will be required to phase in the use of the Offering Circular over a sixty to ninety-day period.

The Offering Circular is the only sales document which will be permitted to be used in the State of Ohio. This requirement is in accord with the Division's findings that historically many purchasers have not been provided with the character of information which is requisite to an intelligent investment decision. Rather, offerees have been materially misled and deceived by advertisements, artists' renderings, and oral representations by salesmen which contain untrue statements and omissions of material facts.

The Offering Circular is essentially modeled after the Securities and Exchange Commission's Form S-11 although in recognition of the "real estate" aspect of these offerings, the format has been substantially liberalized to require the use of photographs, maps, and other graphic representations in order to provide a fair presentation of the real estate, existing improvements and other amenities which have been completed.

It is not the intention of the Division to make the Offering Circular a dry academic dissertation of obscure boiler plate

legalisms, but rather to provide an attractive, readable single "advertising package" in which narrative explanation and photographic representation work together to provide full disclosure.

The proposed format also eliminates the use of the "sales contract" and in lieu thereof contemplates the use of the purchase agreement which incorporates, by reference, the representations contained in the offering circular.

In order to assure proper use of the Offering Circular, and with a view toward eliminating many of the deceptive sales techniques which have come to the Division's attention through complaints of purchasers from existing registrants, the following conditions of registration will be included in the Division Order effecting qualification of the application.

1. The Offering Circular shall be delivered by mail to every Ohio offeree no less than three days prior to the date of any personal solicitation or offer for sale other than pursuant to permitted advertising employed solely for the purpose of soliciting indications of interest in receiving the Offering Circular.
2. The use of any sales, advertising or promotional material other than the most recently approved Ohio Offering Circular, ~~and property~~ report required by Federal law and advertising approved by the Division (see "Advertising" below) is prohibited.
3. The salesman and purchaser shall each initial the spaces provided immediately adjacent to each Risk Factor and Special Consideration contained in the Ohio Offering Circular, prior to execution of the purchase agreement.
4. No dealer, salesman, or agent or employee of the owner or developer shall make any statement or imply or represent any state of facts not contained in or represented in the Ohio Offering Circular.
5. Any sale of any part of the property or any interest therein shall be rescindable as follows:

A. Breach of any of the conditions set forth above will give rise to a right of rescission.

B. Every Ohio purchaser shall have an unconditional right of rescission, exercisable within thirty (30) days after the date of sale.

C. Every Ohio purchaser shall have the unconditional right to physically inspect, by agent or otherwise, the property he has purchased within twelve months of the date of sale and thereafter to rescind the entire transaction within thirty days and receive all monies previously paid within thirty days after the date the purchaser has notified the owner or developer, in writing, of his election to rescind.

6. An administrative or judicial adjudication that the Offering Circular contained an untrue statement of a material fact, or omitted to state a material fact necessary, in light of the circumstances under which the statements therein are made, to make such statements not misleading, shall give rise to a right of rescission.

C. Advertising

As a result of the Division's findings that many advertisements and artists' renderings may mislead purchasers and hamper an intelligent investment decision, the only form of advertising other than the Offering Circular which may be used in connection with new registrations will be that approved by the Division in the format set forth below.

In addition to the Offering Circular, the Division will permit advertisements in newspapers, magazines and other publications, cards, pamphlets, letters and other literature employed and intended solely for the purpose of eliciting indications of interest from Ohio residents who desire to obtain a copy of the most recently approved Ohio Offering Circular, provided however, that such advertisements, cards, pamphlets, letters, or other literature contain no more than the following:

1. The name of the owner and the developer of the property.
2. A brief description of the property limited to the name of the project or development, the location of the property, its proposed use and the number of parcels, lots or units offered.
3. The interest (i.e. fee simple, leasehold) in the property being offered.
4. Per-unit offering price or, in the event that all units of the property are not offered at the same price, the per-unit offering price of each category of units together with the number of such units in each price category.
5. A photograph or photographs which are not greater in total surface area than ninety-three and one-half square inches and which accurately represent the state of development and/or characteristics of the property, and which, when taken in the context of all material facts pertaining to the property would not tend to deceive purchasers.

All such advertisements, cards, pamphlets, letters and other literature shall contain the following:

1. The following statement in type equal in size to that used in the remainder of the text of the advertisement:

"A copy of the Offering Circular filed with the Division of Securities of the State of Ohio must be delivered to you by mail no less than three days prior to any personal solicitation whatsoever. This Offering Circular contains information which is relevant and important to your decision to purchase the property. You should read this Offering Circular carefully to make up your mind on the suitability to you of this investment."

2. Name and address of the licensed Ohio dealer from whom a copy of the Offering Circular may be obtained.

In order to allow sufficient time for review by the Division, submissions in the above format shall be tendered not less than thirty days prior to the intended date of publication or dissemination.

D. Use of Unauthorized Advertising

Many Ohio residents have filed complaints with the Division regarding the use of unauthorized advertising by foreign real estate developers. The Division is currently investigating the registrants against whom consumer complaints have been filed. These matters are being handled on an *ad hoc* basis with a view toward enforcement or administrative action for violations of the Ohio Securities Act to be commenced during the next thirty days depending on the extent of violations such investigation reveals.

E. Requests for Price Increases

In the interests of fairness to applicants and for purposes of insuring the consistency of our regulatory approach to requests for price increases under pre-existing registrations, the Division proposes to utilize certain discretionary guidelines in order to ascertain whether a price increase is on grossly unfair terms.

In this connection, all price increases currently pending and those which are submitted after this date will be handled on the following basis:

1. Inasmuch as a price increase substantially alters the most fundamental aspect of the offering upon which the Division originally made a fairness determination, such proposals will require an amendment to the existing registration and Division Order, thereby giving rise to a full re-evaluation and review by the Division in accordance with the substantive fairness provisions of Section 1707.33, O.R.C.
2. The Division will request every applicant to provide an independent appraisal of the market value of the subject property by a disinterested independent professional appraiser, approved by the Division, at the applicant's cost.
3. Full and complete certification of the applicant's development costs by an independent registered engineer must be submitted.
4. The applicant must provide certification that all previous developmental commitments have been timely achieved.
5. Information with respect to the applicant's profits, rate of return on invested capital, and other pertinent financial data with respect to the total development program will be required.

The Division invites written comments by interested parties regarding the foregoing procedures.

Mike Jones

BROKER/DEALER SECTION Mergers and Acquisitions

A large number of the recent applications for broker/dealer licenses have been submitted for the limited purpose of consummating a merger, consolidation or other corporate reorganization which requires a broker/dealer license even in transactions where the securities themselves may be

exempt from registration.

In addition to previous articles in the July, September, and November **Bulletins** a further delineation of procedure is offered.

The Form 15, to be submitted to the Broker/Dealer Section at the same time the registration material is submitted to the Registration Section, should include, in response to Question No. 13, the names and addresses of five persons of whom the Division *may* inquire as to the character, reputation, and financial responsibility of the applicant as required under 1707.15(E) of the Ohio Securities Act. The Form 15-B should be sent to a newspaper as detailed in 1707.15. Although the financial data requirements will be waived, it is important to complete all signatures, verifications, notarizations, and naming of the person upon whom process may be served to avoid delay in issuance of the license.

The testing requirement which must be done by an elected officer of the company will be mailed upon receipt of Form 15 with fees attached. This officer will be held responsible for all compliance procedures; all other persons actively selling must take an appropriate examination and become licensed by filing Form 16. The test, an open-book examination, can only be waived if the applicant dealer is a licensed dealer in another state or is registered with the Securities and Exchange Commission as a *dealer*, is a member of a national securities association, or is a member of a national securities exchange, *and has passed a qualification examination administered by such organization.*

James C. Warneka

CONSUMER FINANCE SECTION Basic Annual Report - Small Loans and Mortgage Loans

Section 1321.09, O.R.C. states in part: "every licensee shall on or before the fifteenth day of April of each year file a report with the Division giving such relevant information as the Division reasonably requires, . . ."

The Division acknowledges that to keep current records in conformance with the Division's reporting format is a burdensome on-going task and that the final composite results are of mild interest to many operations.

From the Division's standpoint, this is a statutory requirement and the consolidation of the reports of some 2700 licensees into the final report is a difficult, time consuming task. As of the statutory deadline, April 15, 1974, the Division had numerous requests for extensions to as far as June 30th and had not received reports or replies from some 28 respondents. Other financial regulatory agencies are presently assessing fines for each day of non-compliance and the Division does not want to believe that its Ohio licensees need a system of fines to insure compliance with the statutory deadline.

A present study is underway for a national revision of the format for the Basic Annual Reports in an attempt to up-date the information and provide uniform information and format for all states.

The most generally quoted compliance problem of all state administrators at the recent convention was that of the lack of statutory operational knowledge by branch personnel. It was agreed that a large portion of the problem emanated from inter-state, middle management transfers. In Ohio this ranks second to "on-line" conversions. It is the hope of the Division that its budget will allow it to provide an examiner-specialist, trained in "on-line" to work in cooperation with the programmers when conversions are made or discrepancies found.

R. P. Fickell

CREDIT UNION SECTIONS

Ohio Credit Union Shareowner's Guaranty Association

The implementation of a program for share deposit insurance for state chartered credit unions in the State of Ohio is imminent. This much sought after guaranty program has culminated in the efforts of Mr. Paul Deaton of the NCR Employees Credit Union of Dayton, Ohio and takes its form in the creation of "The Ohio Credit Union Shareowner's Guaranty Association" (OCUSGA).

The Articles, Constitution and By-Laws of this corporation are currently under review by the Director of Commerce. Principals of this corporation have been given the go-ahead to solicit charter subscribers in order to meet the minimum statutory requirement of twenty-five member credit unions.

As defined by statute, the purpose of the OCUSGA is to create and maintain a fund for the guarantee or insurance of shares and deposits of members of those credit unions which become members of the association. As proposed, there is no limit to the amount of guarantee extended.

The Division contemplates the formation of this organization to be a vital step in the overall qualification and preservation of sound credit unions in Ohio. Requirements for participation in this association parallel the requirements of this Division in the ordinary conduct of credit union business. The additional requirement of participation in the guaranty association, which the Division feels will be insisted upon by individual credit union memberships, will tend to reinforce the tougher regulatory posture adopted by the Division in the past fifteen months.

The onus of regulation of the Ohio Credit Union Shareowner's Guaranty Association falls upon this Division. The initial question was just how far our regulatory presence was to be extended. Suffice to say at this writing that the decision to involve ourselves in the regulatory process of this OCUSGA will be minimal. Every cooperation, however, will be extended as required by the statute. A primary responsibility will be the furnishing of examination reports and other field data obtained from our staff review. The Division anticipates a close bond between the Division and

OCUSGA, necessary for the ultimate goal of more sound credit unions in this state.

Participation by credit unions in this association will be voluntary and will be effected by application to the OCUSGA's review committee. Standards for participation have not yet been published; however, it is anticipated that at the outset restrictions for membership will be minimal. Each credit union participating must deposit with the association one percent of its total share deposits as of the previous year-end as an entrance requirement. Such deposit must remain with the association for as long as the credit union elects to continue its relationship with the association. Earnings of the corporation will be distributed according to limits of participation. Additionally, an annual fee amounting to one-twelfth of one percent of the credit union's share balances outstanding at year-end will be assessed and will be payable on a monthly basis.

Actuarial strength of the association will not be limited to the one-percent capital funding. A bill has been introduced in the Wisconsin legislature to create the National Reinsurance Corporation, which corporation is intended to re-insure regional and state-oriented share insurance corporations. Additionally, this corporation will be able to lay off risk to major line insurance companies who have already expressed interest in participation.

State-chartered credit unions have been permitted to subscribe to the share deposit insurance program of the National Credit Union Administration. To date, 176 credit unions out of a total of 687 have subscribed for and are presently covered under its plan. These credit unions represent about half of the total assets of all credit unions in this state. It is anticipated that many of those presently insured under the federal program will elect to participate in the state-oriented plan. The primary reason for leaving the federal program to opt for the independent plan is that under federal participation there exists a conflict in regulatory authority and supervision. Most credit unions reject the idea of a duality of supervision and will look favorably upon the availability of an alternate plan of share insurance.

John Gouch

REGISTRATION SECTION

I. Reorganization of Section Staff

Recent reorganization changes within the Registration Section have apparently caused some difficulty among certain members of the Ohio Bar trying to direct their inquiries to the members of the Registration Section.

In an attempt to clear the confusion, the current Registration Section staff and their particular area of expertise are listed below:

Bernard G. Boiston	Supervisor
George A. Ward	Chief Examiner - Oil and Gas Programs and Working Interests
Ronald Lembright	Attorney-Examiner - Interstate Corporate Offerings
Warren Williams	Attorney-Examiner - Form 39 Registrations
(Enforcement Section)	
Jeffrey Ginther	Attorney-Examiner - Interstate Corporate Offerings
Dan Rosenfield	Examiner - Real Estate Syndications
Robert Bibler	Examiner - Interstate Corporate Offerings
Robert Almond	Examiner - Forms 3-0, 6
Tom Simon	Examiner - Intrastate Corporate Offerings, Form 6 in excess of \$50,000
Gordon Stott	Examiner - Mutual Funds

II. New Procedures

A. Appointments and Conferences with Registration Section Staff

To increase the efficiency of the Registration Section staff, at this time, it seems appropriate to remind certain members of the Bar that they must schedule an appointment to confer with anyone from the Registration staff. The Division does not object to pre-filing conferences, etc., however, the Division does object to individuals who "drop-in". To accommodate them, the examiner must interrupt his work to the detriment of other registrants.

B. Notification of Effectiveness of Division Orders

In the past, the Division has had several instances where Division Orders were issued at a time when the entity selling the securities was not licensed by the Broker/Dealer Section. To remedy this problem, the Registration and the Broker/Dealer Section have coordinated a new procedure whereby all requests for Division Orders will be processed through the Broker/Dealer Section to insure that the entity which proposes to sell securities is, in fact, duly licensed as a dealer to sell the securities to be described in the Division Order and in good standing with the Broker/Dealer Section. Since this particular procedural step occurs subsequent to the examination performed by the Registration Section, the only written representation that can be made by the Registration Section examiner is the fact that the Form 9 registration is effective in Ohio subject to compliance with dealer licensing requirements. Even in those situations where the offering is to be sold through a dealer already licensed in Ohio, the "subject to . . ." language is still applicable since it is conceivable that the Broker/Dealer Section might be in the process of or is eminently going to refer the dealer to the Enforcement Section for appropriate action (if that were the case, the Broker/Dealer Section will

immediately notify the Registration Section examiner, who will in turn contact the attorney for the issuer who can then consider an alternative course of action). On the other hand, if the dealer is not licensed in Ohio, counsel for the issuer and/or dealer should communicate with the Supervisor of the Broker/Dealer Section to inquire about the status of the application for a dealer license keeping in mind that the request for the Division Order will not be totally effective and issued without caveat until such time as the Broker/Dealer Section is ready to issue a license. In cases where the entity that proposes to sell the securities is not licensed as a dealer, the Registration Section will continue its policy of issuing a Division Order concurrent with the issuance of the dealer's license. In those situations where the dealer is already licensed, again, the request for Division Orders will have to clear through the Broker/Dealer Section before it can be issued.

C. Open-End Mutual Fund Division Orders

Until a few years ago Division Orders issued in conjunction with mutual funds filings did not have an expiration date. Therefore, in an attempt to control them, the examiner then in charge of mutual funds imposed a \$250,000 limit on the amount that could be registered, the rationale being that since on the average it would take the fund two years to sell this amount, the fund would have to come back in at which time we would have an opportunity to "look it over". Approximately three years ago, the Division changed its policy and Division Orders issued in conjunction with open-end mutual funds were limited to two years. Since the need for imposing a maximum on the amount to be registered has been superseded by the time limitation on Division Orders, henceforth, open-end mutual funds will not be limited to a maximum of \$250,000 but instead can register whatever amount they reasonably anticipate they will be able to sell during the two year period.

D. Delivery of Prospectus

It has come to the attention of the Registration Section that certain intrastate dealers and salesmen working for them do not provide prospective purchasers with a copy of the prospectus in connection with public offerings of securities. The Registration Section is of the opinion that the failure to provide a prospectus to a prospective investor does injustice to the spirit of the Ohio Securities Act in addition to potentially perpetrating a fraud on the public by not providing them the necessary information to make an informed investment decision. It will therefore be deemed to be grossly unfair and in violation of 1707.09, O.R.C., if the following are not complied with:

1. *Language to be inserted in Underwriting Agreements, Selected Dealers Agreements Whereby Dealers Contract to Sell Securities of Issuer, etc.* Said document must contain language to the effect that the dealer represents to the issuer that all prospective purchasers will be provided with a selling document (prospectus, offering circular, etc.) prior to the time of the signing of the subscription form or contract to purchase the securities.

2. Language to be inserted on Subscription Form, Purchase Contract, etc. The following language should be prominently displayed on the subscription form, purchase agreement or similar document. Said language should be capitalized and located immediately above the space provided for the investor's signature, and should read, "I acknowledge receipt of a copy of an Offering Circular describing the company (1) and the securities therein. I have read the offering circular in general and the Risk Factors Section in particular (2).

(1) The Second sentence of the above language should be required only if it is applicable (i.e., only if the prospectus does in fact contain a *Risk Factor* section). (2) The language should be altered to correctly identify the type of issuer, (i.e., a corporation, partnership, etc.)

Bernard G. Boiston

OTHER DEVELOPMENTS

1. Move to the Borden Building: Effective Monday, August 12, 1974, the Division of Securities will be operating at its new location, the thirteenth floor of the Borden Building at 180 East Broad Street in Columbus. Although budget limitations will allow only a few private offices and no free parking will be available, the new site does offer the advantages of a greater proximity to the center of human activity and to other government offices and the ease of communications resulting from all Sections of the Division being located on one floor. It is expected that all Division telephone numbers will, following the move, remain the same as those currently in use.

2. Personnel Changes: On Monday, July 8, Ann Casto, formerly associated with the law firm of Vorys, Sater, Seymour & Pease of Columbus, joined the Division to serve in the position of Chief Counsel. Mrs. Casto is a graduate of Stanford University (B.A. 1968) and Stanford University Law School (J.D. 1971). Originally from Denver, Colorado, she practiced law in San Francisco before establishing residence in Ohio.

On Monday, July 22, Alan B. Smith, III, formerly a special agent with the Organized Crime Section of the Federal Bureau of Investigation in New York City, joined the Enforcement Section of the Division. Mr. Smith is a graduate of Ohio Wesleyan University (B.A. 1966) and the Ohio State University College of Law (J.D. 1969). He returns to Ohio following five years service with the U.S. Department of Justice.

On Monday, April 22, Daniel L. Rosenfield joined the Registration Section of the Division and is now in charge of the Non-Corporate team, dealing with real estate limited partnerships and other offerings of a similar character. He is a graduate of the Ohio State University (B.A. Finance, 1973) and will receive his Masters Degree in Finance during August of this year.

Three recent law school graduates joined the Division in June to serve as staff and enforcement attorneys. William C. Phillippi is a graduate of Case Western Reserve University (B.S. 1969) and Case Western Reserve Law School (J.D. 1974). As Staff Attorney for Administration, he will be assisting the Deputy Commissioner in crisis management activities. Kathleen H. Ransier is a graduate of Western College for Women (B.A. 1969) and Ohio State University College of Law (J.D. 1974). She brings with her to the Enforcement Section eighteen months experience with the Consumer Frauds and Crimes Section of the Office of the Attorney General. Karl E. May is a graduate of Ohio Northern University (B.A. 1971) and the Ohio State University College of Law (J.D. 1974) where he served on the Board of Editors of the Ohio State Law Journal.

On Friday, June 21, Nelson E. Genshaft left the Division to join the Office of the Attorney General. As Counsel for Policy Development, he made significant contributions in all areas of the Division's policy development program and rendered special assistance in connection with Broker/Dealer Section enforcement activities. Fortunately, we can look forward to a continued association with Nelson since he has been assigned to representation of the Division of Securities and other divisions of the Department of Commerce.

On Friday, July 5, Veronica M. Dever left the Division to join the Division of Administration as Hearing Officer for the Department of Commerce. As Attorney-Inspector of the Division during the past twelve months, Veronica initiated the current revitalization of the Enforcement Section and skillfully supervised the progress of several major enforcement cases which arose during that period. Her service as Hearing Officer for the Department will benefit our enforcement program by increasing the efficiency of the administrative process.

On Wednesday, May 22, Michael H. Sewell left the Division to accept a management position with the North American-Rockwell Corporation in Columbus. As a real estate limited partnership examiner with the Registration Section during the past eighteen months, Mike gained a reputation for proficiency among members of the Bar dealing with the Division in this area.

On Friday, May 10, J. Richard Burdick left the Division to accept a management position in the consumer finance industry. As Assistant-Supervisor of the Consumer Finance Section of the Division and as a field examiner in the Cincinnati area, Dick was a valuable asset to the Division who will not easily be replaced.

Although we regret to see good people leave the Division, it is unavoidable in light of current civil service pay scales which we hope will be revised upwards by the legislature next year. On the other hand, it is gratifying to note that for many former employees service with the Division has played an important role in career development and has led to attractive opportunities in industry. We are very fortunate that we have been able to continue to attract to the Division the kind of high quality individuals represented by those who have recently joined our staff. This mobility can

only be considered a healthy phenomenon not only for the individuals involved but for the Division as well.

William L. Case, III

ADMINISTRATIVE ACTIONS

Summary of Credit Union Section Administrative Actions for April, May, and June, 1974

Suspension of Normal Operations

Calvary Baptist Credit Union, Inc.	4- 1-74
Fairfield Employees Credit Union, Inc.	4-18-74
C.G.B. Employees (McConnellsville)	5- 2-74
Cleveland YMCA	5-31-74
Anchor Fasteners	6-14-74
PERCWA	6-27-74

Vacations of Suspension Orders

Title Workers Credit Union, Inc.	4- 8-74
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Mergers Approved

Carpenters Local 1438 merged with Ohio Central	5-17-74
Lyman Employees merged with Ohio Central	6- 3-74
UA-UCC merged with Western	6- 4-74
Sun Employees merged with Ohio Federal	6-17-74
Ken-Sil Ridge merged with Cincinnati Central	6-21-74

Other Actions

New Charter Granted:	
Burndy Corporation Employees, Toledo, Ohio	4-25-74
Twin Rivers Marietta Credit Union, Inc.	6-21-74

Ordered into Liquidation:

Fairfield Employees Credit Union	5-31-74
Varsity House	6- 3-74

Summary of Enforcement Activity for April, May, and June, 1974

Broker/Dealer Suspensions

Key Properties, Inc.	4-74
Allied Investment Corporation	4-74
First Cincinnati Securities, Inc.	4-74
Equitable Development Corp.	4-74
Florida Investment Corp.	4-74
Padre Island Investment Corp.	4-74
Multi-State Unit, Inc.	4-74
American Securities, Inc.	4-74
Western Exploration, Inc.	5-74
Vernon C. Barnhill DBA Vernon Barnhill Realty & Investment Fund	5-74
Wilson-Salem Realty, Inc.	6-74

Broker/Dealer License Revocations

Provident Securities, Inc.	4-74
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Broker/Dealer License Denial

E. J. Plott	4-74
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Salesman Suspension

Philip Lombardo	4-74
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Salesman License Denials

Robert Lengyel	4-74
James Weixel	4-74
Mary Helen Nicholas	4-74
Edwin Wilde	6-74
Cecil Berry	6-74
Emerson Berry	6-74
James Harry Adams	6-74
Timothy A. Buckley	6-74

Registration Suspensions

Padre Island Investment Corporation	4-74
Americus Budget, Ltd.	6-74

Hearings

Multi-State	5-74
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STATISTICS

		Applications Received	Orders
<u>April, 1974</u>			
Registration	Certificates		
2-B	18	Form 39 18	3
3-0	480	Note: 1 Request for Cursory Review 7 Withdrawals	
5-A	2		
6-A-1	127	<u>May, 1974</u>	
6-A-1 with Offering Circular	1	Interstate Corporate	27 6
6-A-2	64	Stock Option & Purchase Plan	6 0
6-A-3	22	Intrastate Corporate	4 3
6-A-3 OG	0	Investment Companies	35 21
6-A-4	9	R.E.I.T.	1 3
<u>May, 1974</u>		Real Estate Ltd. Partnerships	14 13
2-B	35	Oil & Gas Offerings	14 17
3-0	523	Cattle Funds	1 1
5-A	3	Other Non-Corporate	4 10
6-A-1	128	Form 39	13 0
6-A-1 with Offering Circular	6	Note: 1 Request for Cursory Review 16 Withdrawals	
6-A-2	71		
6-A-3	16	<u>June, 1974</u>	
6-A-3 OG	11	Interstate Corporate	11 18
6-A-4	4	Stock Option & Purchase Plan	7 11
<u>June, 1974</u>		Intrastate Corporate	2 2
2-B	21	Investment Companies	24 42
3-0	341	R.E.I.T.	0 0
5-A	2	Real Estate Ltd. Partnerships	12 10
6-A-1	121	Oil & Gas Offerings	12 17
6-A-1 with Offering Circular	1	Cattle Funds	0 2
6-A-2	56	Other Non-Corporate	10 3
6-A-3	22	Form 39	12 0
6-A-3 OG	0	Note: 1 Request for Cursory Review 7 Withdrawals	
6-A-4	8		
<u>April, 1974</u>			
	Applications Received	Orders	
Interstate Corporate	18	24	
Stock Option & Purchase Plan	6	1	
Intrastate Corporate	5	4	
Investment Companies	42	38	
R.E.I.T.	0	1	
Real Estate Ltd. Partnerships	12	17	
Oil & Gas Offerings	13	29	
Cattle Funds	0	1	
Other Non-Corporate	2	5	

Securities Broker/Dealer (Form 15) Received in April, May, and June, 1974

Oxford Laboratories	4- 1-74
Arthur Wiesenberger & Co., Inc.	4- 3-74
Up-Right, Inc.	4- 8-74
North American Corporation	4-10-74
The Lenox Fund	4-15-74
Wrather Corporation	4-15-74
Honeywell Information Systems, Inc.	4-18-74
Eaton Corporation	4-22-74
Herb Berns dba Investors Realty Funding	4-23-74
Fastener House, Inc.	4-24-74
Warren Vens	4-24-74
Society Corporation	4-29-74
Jeffrey I. Friedman	4-29-74
Realty Investments Associates, Inc.	4-29-74
Allied Chemical Corporation	4-29-74
American Equitel Corporation	5- 1-74
First Illinois Bancshares Corporation	5- 2-74
Kenneth I. Gillespie dba KGR Securities & Investments	5- 6-74
Issued	6-24-74
F. L. Putnam & Company, Inc.	5- 8-74
Diversified Retailing Company, Inc.	5- 8-74
Ostendorf-Morris Company	5- 9-74
Issued	5- 9-74
Madison Financial Corporation	5-10-74
(Withdrawn 6-6-74)	
First Railroad & Banking Co. of Georgia	5-10-74
Gulf Investment Bankers, Inc.	5-13-74
Issued	7- 8-74
First Maryland Bancorp.	5-13-74
Issued	6- 7-74
Data 100 Corporation	5-13-74
Issued	6- 3-74
Fabri-Tek Incorporated	5-13-74
The First Columbus Securities Corp.	5-15-74
Issued	6- 1-74
First Banc Group of Ohio, Inc.	5-16-74
Issued	7- 8-74
CFS Continental, Inc.	5-20-74
The University of Akron Development Foundation	5-21-74
Hyster Company	5-21-74
Issued	6-20-74
Olinkraft, Inc.	5-22-74
Issued	6- 5-74
Fourteen Seventy-One Andrews Associates	5-23-74
Consolidated Oil & Gas, Inc.	5-24-74
Issued	6-26-74
The Jupiter Corporation	5-28-74
OGR Service Corporation	5-28-74
Weiss, Peck & Greer	6- 3-74
J. P. Cabot-Short Term Fund, Inc.	6- 5-74
Arthur G. McKee & Company	6- 7-74
Delta Securities, Inc.	6-10-74
Vanderbilt Management Corp.	6-10-74
Carter Hawley Hale Stores, Inc.	6-10-74
Issued	7- 7-74

Management Assistance Inc.	6-11-74
Halliburton Company	6-12-74
Valhalla Racquet Club	6-14-74
Issued	7- 3-74
Zoom Ltd.	6-14-74
Conwood Corporation	6-17-74
Paul J. Bruck & Associates, Inc.	6-21-74
Becton, Dickinson & Co.	6-24-74
Witt Industries, Inc.	6-26-74
Tanbark Realty Company	6-27-74

Foreign Real Estate Broker/Dealer Applications (Form 331-A) Received in April and June, 1974

Heritage (Realtors)	4- 2-74
Paul B. Wilson	4-10-74
Glen R. Ketteler dba Florida Properties	6-11-74
Denham Realty Investments, Inc.	6-13-74
Clifford John Steinbarger	6-17-74
Jack Hochheiser	6-19-74

Salesman Applications Received in April, May and June, 1974

Form 16 - Securities	210
Form 331 - B - Foreign Real Estate	76
Total Salesmen for April	286
Form 16 - Securities	240
Form 331 - B - Foreign Real Estate	68
Total Salesmen for May	308
Form 16 - Securities	197
Form 331 - B - Foreign Real Estate	53
Total Salesmen for June	250

Summary of Consumer Finance Activity for April, May, and June, 1974April, 1974

	Issued	Cancelled	Suspended
Small Loan Licenses	1	6	0
Second Mortgage Licenses	3	7	0
Premium Finance Licenses	0	0	0
Pawnbroker Licenses	0	0	0

Compliance Examinations Made: 925
Financial Examinations Made: 2

May, 1974

Small Loan Licenses	1	1	0
Second Mortgage Licenses	1	6	0
Premium Finance Licenses	0	0	0
Pawnbroker Licenses	0	0	0

Compliance Examinations Made: 249
Financial Examinations Made: 3

June, 1974

Small Loan Licenses	2	2	8
Second Mortgage Licenses	1	1	9
Premium Finance Licenses	0	0	0
Pawnbroker Licenses	0	0	0

Compliance Examinations Made: 244
Financial Examinations Made: 1

Hearings Held Pursuant to Section 1321.04April

Sterling Finance Company of Dayton
20524 Southgate Park Boulevard
Maple Heights, Ohio

Household Consumer Discount Company
Monroe Avenue, Monroe Mall
New Philadelphia, Ohio

May

Household Consumer Discount Company
Monroe Avenue, Monroe Mall
New Philadelphia, Ohio
74-2943

June

Household Consumer Discount Company
Montgomery Road
Surrey Square Mall
Norwood, Ohio
74-2945

Foreign Real Estate**New Applications for April, 1974****Forms 33**

Prescott Valley	#33164
Diamonhead Corporation	#33165
Punta Gorda Developers	#33154
The Deltona Corporation	#33188

Status of Division Personnel July, 1974

Commissioner - William L. Case, III
Deputy Commissioner - Robert J. DeLambo
Chief Counsel - Ann Casto
Special Counsel - Alan P. Baden
Attorney-Inspector - Jack D. Jester

Supervisors

Registration Section - Bernard G. Boiston
Broker-Dealer Section - James C. Warneka
Foreign Real Estate Section - R. Michael Jones
Credit Union Section - John Gouch
Consumer Finance Section - Robert P. Fickell
Enforcement Section - Jack D. Jester
Administration Section - Nicholas J. Caraccilo