Ohio Securities Bulletin

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Commissioner's Letter

In the beginning, there were advisory committees. Their function was to provide a meaningful interchange of ideas between the Division of Securities and members of the securities community. Although the use of these committees lost their vitality over the years, I would like to see if there is interest in resurrecting them. It is essential to the Division to have an interested group with which to consult when changes in our policies are contemplated.

We are currently updating our committee lists and will be sending inquiries to those prior members for an indication of interest. Anyone not a prior member interested in participating should express their interest to Debra Chafin at the Division (614-462-7371).

Broker-dealers

For some time, the issue of whether the Division should continue broker-dealer testing has been discussed with no apparent resolution. The examination we currently administer does not seem to adequately discriminate between the truly knowledgeable applicant and those merely able to achieve a passing score.

We currently test approximately 300 applicants per year, which results in about 200 new licenses. Compare this to the 15,000 annual NASD-tested licensees. Almost two-thirds of all the states now use NASD testing procedures exclusively for their licensing. If we discontinued our in-house testing, these same applicants could take the NASD Series 63 examination at Control Data Centers located throughout the United States.

To effectuate this change we need merely delete subsection (2) of 1301:6-3-15(C) and subsection (2) of 1301:6-3-16(B). Please send in any comments you might have on this proposal.

Excusable Neglect

Pursuant to the command of Revised Code section 1707.391, the Division of Securities promulgated administrative rule 1301:6-3-391, defining excusable neglect. This rule creates a presumption that excusable neglect will be found when the conditions of the rule are met.

The rule creates a narrow set of preconditions for Division acceptance of a Form 391 (*see* discussion at page 3 *infra*). Although the language of the rule does not eliminate the possibility of the Commissioner exercising discretion when finding excusable neglect, the present policy of the Division is to use extremely limited discretion in this regard.

Should an issuer seek post-sale qualification of a transaction that does not fit within rule 1301:6-3-391, that issuer should apply pursuant to section 1707.39 in lieu of seeking discretionary relief pursuant to section 1707.391.

Personnel

There have been several recent additions to the staff of the Division during the last year.

D. Michael Quinn joined the Division in May, 1985. He graduated from Capital University Law School in 1978. His previous experience includes corporate work in Chicago (1978-1981) and acting as counsel to the Ohio Division of Banks (1981-1985). He is an attorney examiner in the registration section with responsibility in the area of real estate limited partnerships.

Daniel A. Malkoff joined the Division in April, 1986. He is a graduate of the University of Toledo College of Law. He was admitted to the Bar in November 1985. He is a staff attorney in the enforcement section.

Deborah L. Dye Joyce joined the Division in May, 1986. A graduate of Ohio Northern University Law School, she was admitted to the Bar in November 1985. She is an attorney examiner in the registration section with primary responsibility in the investment company area.

Norman A. Essey joined the Division in May, 1986, a few days after graduating from Capital University Law School. By the time you read this, he will probably have completed the Bar Exam. Norman is a staff attorney in the enforcement section.

Corey V. Crognale joined the Division in June, 1986. He is a graduate of Capital University Law School, admitted to the Bar in November 1980. He has worked in the area of utility law as an assistant attorney general in the State Department of the Ohio Attorney General's Office. He is a staff attorney in the enforcement section.

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Enforcement

William E. Meister, Jr., et al.

From June 1984 to February 1985, William E. Meister, Jr. issued promissory notes (primarily to Hamilton County residents) representing a face amount of approximately three million dollars in order to fund a "ticket-scalping" enterprise. Investors were promised double or triple their investment in short periods of time. The ticket business supported the enterprise for only a short time. Through the issuance of promissory notes, Meister began running a "Ponzi Scheme" whereby funds received from new investors were used to repay the notes of current noteholders. Meister was aided in the scheme by Thaddeus Muething (acting as Meister's attorney), Robert and Jean Howard (commissioned salespersons), Lawrence Newberry (loan coordinator), and Daniel Ancona (commissioned salesperson).

The issuance and sale of the promissory notes was determined by the Division to be sales of unregistered securities by unlicensed persons sold in a scheme which operated as a fraud upon the investors in violation of Ohio Revised Code sections 1707.44(C), (A), and (G), respectively. The fraud allegation is based largely upon material omissions.

In May, 1985, the above allegations were made and indictments returned in Hamilton County against Meister and the above-named individuals. Thaddeus Muething's trial began on July 7, 1986. The co-defendants are expected to either enter pleas or go on trial thereafter, however, no formal pleas have been entered to date.

This case was investigated and referred for criminal action by former Acting Commissioner Phillip Lehmkuhl and Staff Attorney Tina K. Manning.

Walter Evans

In the summer of 1982, Attorney Walter Evans engaged in the sale of unregistered securities to a Montgomery County resident. While assisting a young widow in the investment of her late husband's life insurance proceeds, Evans invested her funds in a company incorporated and controlled by him. The investment contract constituted a sale of an unregistered security.

Evans was indicted on counts of selling unregistered securities in violation of Ohio Revised Code Section 1707.44(C), securities fraud in violation of 1707.44(G), and grand theft.

The trial date has been set for July 21, 1986. This case was investigated and referred by Tina K. Manning, Staff Attorney.

Capricorn I

On July 31, 1985, and October 8, 1985, Lyle Shull and J. Robert Larson, respectively, pled guilty in Cuyahoga County Common Pleas Court to securities charges in connection with the sale to a Cuyahoga County resident of a limited partnership interest in Capricorn I (a limited partnership which was never formed). Capricorn I was supposed to have been formed as a licensee of a commodities software program designed to assist the partnership in investing in commodities. The licensor appeared to have been nonexistent and the investor's funds were misappropriated. The limited partnership interest sold was not registered.

Larson pled guilty to one count of securities fraud, Revised Code section 1707.44(G), and one count of grand theft, Revised Code section 2913.02. Shull pled guilty to one count of selling unregistered securities, Revised Code section 1707.44(C). Staff Attorney Tina K. Manning investigated and referred the case for criminal prosecution.

Gem City Life Holding Company

In the summer months of 1985, Charles M. Walden and James Kevin Brown formed Gem City Life Holding Company in order to fund a Dayton-based life insurance company. Shares of stock were sold by Walden and Brown to approximately 300 Montgomery County residents. The proceeds from the sale of the securities were to be held in escrow until such time as the insurance company was to be formed.

The securities of Gem City Life Holding Company were not registered, neither Walden nor Brown were licensed to sell securities in Ohio, and the investors' funds were misappropriated. Pursuant to Revised Code sections 1707.26 and 1707.27, the Division moved for, and was granted, a permanent injunction and a receivership by the Court of Common Pleas of Montgomery County. The receivership was terminated upon the filing of bankruptcy on behalf of the company.

The matter was investigated by former Acting Commissioner Phil Lehmkuhl and Staff Attorney Tina K. Manning.

Raymond S. Ficere/R.S.F. and Associates

In June of 1983, Raymond S. Ficere, an investment adviser in Akron, sold shares of a Columbus-based maid service company to an Ohio resident and promised great returns on the investment. Ficere neglected to disclose material facts relating to the investment. The shares were not registered, nor was Ficere licensed to sell securities.

On June 20, 1986, Ficere was indicted in Summit County on charges of selling unregistered securities in violation of Revised Code section 1707.44(C), selling securities without a license in violation of Revised Code section 1707.44(A), and securities fraud in violation of Revised Code section 1707.44(G). This case was investigated and referred for prosecution by Staff Attorney Tina K. Manning.

Hollis B. Reed/Reed Energy, Inc.

On April 30, 1985, the Division issued a final Cease and Desist Order against Reed Energy, Inc. and Hollis B. Reed of Dublin, Ohio. The Division found that Hollis B. Reed and Reed Energy, Inc. sold unregistered working interests to Ohio investors in three different oil and gas offerings. In addition, the Division found that neither Hollis nor Reed Energy were licensed to sell securities in Ohio.

On March 27, 1986, the Chicago Regional Office of the Securities and Exchange Commission filed a complaint in the U.S. District Court for the Southern District of Ohio seeking a permanent injunction against Hollis B. Reed. The complaint charged that from about January 1982 through July 1983, Hollis B. Reed raised $3.3 million from approximately 178 investors through the sale of unregistered securities in the form of fractional undivided interests in nine oil and gas wells. The complaint also alleged that the defendant made material misrepresentations and omissions concerning the return on the investment, the risks associated with the investment, expenses associated with drilling the wells, compensation received by Hollis B. Reed, and the use of the proceeds.

Franklin J. Cristiano

On July 18, 1985, Franklin J. Cristiano was indicted on securities violations in Geauga County. Mr. Cristiano was charged with securities fraud and selling securities while unlicensed as a securities salesman. The indictment alleged that he sold an interest in foreign real estate and subsequently the investor received nothing for his investment. By consent, since 1981, Mr. Cristiano has been subject to a permanent injunction against the illegal sale of securities in Ohio.

A warrant for Mr. Cristiano's arrest has been issued by Geauga County.

D.L.F.I., Inc./Dale L. Furtwengler

On February 28, 1985, Dale L. Furtwengler was indicted on twenty-four counts of securities violations and theft in Hamilton County. The indictment included five counts of securities fraud, five counts of unregistered sales, nine counts of theft, and five counts of selling securities while unlicensed. The charges allege that Mr. Furtwengler falsely represented himself as a securities broker from November 1, 1979, to August 27, 1982. Mr. Furtwengler advertised his financial planning type services in magazines and also promoted investment deals for his now defunct company, D.L.F.I., Inc., formerly located in Montgomery, Ohio.

Mr. Furtwengler told clients that he was putting their money in a complicated web of certificates of deposit, secondary mortgage funds, and real estate. He placed approximately $500,000 in his own account for his personal use.

This case is still pending and a court date is scheduled for late July in Hamilton County.

This case was investigated and referred for prosecution by former Staff Attorney James Lummanick and Staff Attorney Melanie Braithwaite.

Registration

Correction: Insider Loans Policy

The registration policy on insider loans found on page 5, Issue 1, May 1986, contained a typographical error. Divisions a, b, and c were incorrectly connected in sequence with the word "or." The word "and" should be substituted for "or," and the requirements a, b, and c are cumulative.

Retroactive Qualification

Effective April 11, 1985, Senate Bill 310 created an abbreviated system for post-sale perfection of a securities filing. Where a securities filing was improperly made because of "excusable neglect," Revised Code section 1707.391 provides the issuer a simple alternative to the procedures of section 1707.39.

The Division has promulgated rule 1301:6-3-391 setting forth the standards for excusable neglect (*see* Commissioner's letter *supra*).

The Division is pleased to announce that since the implementation of section 1707.391 on April 11, 1985, and administrative rule 1301:6-3-391, the number of forms found defective when filed has been reduced by fifty percent.

The most common deficiencies retroactively qualified or exempted pursuant to the provisions of section 1707.391 are as follows:

Not filed in a timely manner	35%
Filing fee incorrect	10%
Basic information incomplete	20%
Type of security not entered	5%
Date of sale omitted	10%
Number of units sold not entered	5%
Price per unit sold not entered	5%
Number of purchasers omitted	5%
Other	5%

Questions relative to the above should be directed to Cyril L. Sedlacko (614-462-7383) or Gordon Stott (614-462-7385) at the Division of Securities.

Consent to Service; Section 1707.02(B)

Effective March 6, 1986, Revised Code section 1707.11 has been amended to eliminate the requirement that an applicant for a claim of exemption pursuant to section 1707.02(B) attach a consent to service to the application.

Real Estate

The Division has adopted the North American Securities Administrators Association's (NASAA) Statement of Policy regarding Real Estate Investment Trusts effective January 1, 1986, as its guideline in determining whether such offerings are being made on grossly unfair terms.

Equipment Leasing

The Division has adopted NASAA's Statement of Policy regarding Equipment programs effective April 23, 1983, as its guideline in determining whether those offerings are being made on grossly unfair terms.

Future Transactions with Affiliates

A proposed public offering of securities will be considered to be made on grossly unfair terms unless the final offering circular or prospectus prominently discloses that any future transactions between the issuer and any affiliate will be entered into on terms at least as favorable as could be obtained from unaffiliated independent third parties.

Debt Service

A proposed public offering of securities of either preferred stock or debt securities will be considered to be made on grossly unfair terms unless the issuer prominently discloses a ratio of earnings to fixed charges or a ratio of earnings to combined fixed charges and preferred stock dividends (calculated in accordance with Regulation S-K, Item 503, under the Securities Act of 1933) of at least 1.00 for the three most recent fiscal years and the latest interim period preceding the date of effectiveness of such public offering.

Takeovers

Fleet Aerospace bid for Aeronca, Inc.

On May 21, 1986, Fleet Aerospace (Fleet), a Canadian corporation, made a tender offer of $5.00 per share for 50% to 100% of the shares of Aeronca, Inc., an Ohio corporation with its principal place of business in Ohio and with executive offices in North Carolina. Both Fleet and Aeronca are primarily engaged in the production of specialty aerospace equipment.

Simultaneously, Fleet applied to the District Court of the Southern District of Ohio for a preliminary injunction against the invocation, application, or enforcement of Revised Code sections 1707.041, .042 (Securities Act/takeovers), .23, .26 (Securities Act/general powers), and 1701.831 (Corporation Act/control share acquisitions), on the basis of conflict with the commerce and supremacy clauses of the United States Constitution. Pending the decision upon the injunction, with the consent of the Division, the court issued a temporary restraining order against any invocation of the above laws with the exception that administrative proceedings pursuant to section 1707.041 could continue.

On May 21, 1986, Fleet also filed a form 041 in compliance with Revised Code section 1707.041.

On May 30, 1986, Aereonca advised the Commissioner that it would make no request for a hearing pursuant to section 1707.041(B)(1)(b). Pursuant to section 1707.041(B)(1)(a) the Division was unable to find cause for such a hearing.

Because no further proceedings were contemplated under section 1707.041, the issue of its constitutionality was dropped from the litigation in federal court.

On June 11, 1986, District Court Judge Holshuh awarded Fleet a preliminary injunction against the invocation or enforcement of the Ohio Control Share Acquisition Act (OCSAA), Revised Code section 1701.831. The court found a likelihood that the Act was both a direct and indirect violation of the commerce clause of the United States Constitution. The court also found a likelihood that the OCSAA conflicted with the purpose and intent of the Williams Act and was thereby preempted by the supremacy clause of the Constitution. Pending appeal to the Sixth Circuit Court of Appeals, the District Court enjoined Fleet from voting shares of Aeronca.

The Division appealed the decision of the District Court to the Sixth Circuit Court of Appeals. Prior to oral argument, the Aeronca board of directors approved a "sweetened" offer of $6.00 per share by Fleet coupled with a proposed merger agreement and certain guarantees to Aeronca's chief executive. The State of Ohio thus became the sole appellant arguing on behalf of the constitutionality of the statute.

On June 18, 1986, Judge Wellford, writing also for Judges Peck and Kennedy, approved the district court's preliminary injunction with the qualification that:

> We have reservations, however, about the district court's conclusionary statement that MITE Corp. "sounded the death knell for state control of federally regulated tender offers," if the court meant by this statement that all state regulation regarding tender offers is foreclosed. See the concurring opinions of Justice Powell and Justice Stevens, 457 U.S. at 646, 647, 655.[1]

Although requests to Justices O'Connor and Powell for an interim stay of the transaction were denied, the Division is presently pursuing an appeal of the decision to the Supreme Court of the United States.

[1]Fleet Aerospace Corp v Holderman, No. 86-3533 slip op. at 9 n.5 (6th Cir 6/25/86).