Registration Provisions under the Ohio Blue Sky Law

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Prior to the enactment of the state laws regulating the sale of securities, commonly known as blue sky laws,1 innocent purchasers were subject to numerous frauds, perpetrated by unscrupulous corporate organizers and securities dealers. It was not uncommon for securities to be sold either in unsound condition, for example, watered stock, or in enterprises which were highly unlikely ever to become successful, for example, mining prospects or inventions.2 Often the actual sale was subject to exorbitant commissions or other dishonest practices by security distributors and salesmen. Compounding these practices was the fact that judicial remedies were available only "after the harm had been done, and because there were so many procedural difficulties in the way, the net result of what the courts" accomplished was inadequate.3

In hopes of finding some approach which would stop these practices before investors would be hurt, regulatory provisions were enacted. While these regulatory provisions have been subject to numerous attempts at classification,4 the simplest way to describe them is to call one group fraud-type provisions, and the second, regulatory-type provisions.5 The fraud-type initially gives the attorney general or other designated officials power to investigate practices in the advertisement and sale of securities. When fraud is discovered, the official has the power to bring criminal prosecutions and suits for injunctive relief.6 The second type of statute, the regulatory type, may require licensing of dealers and/or registration of securities.7 It is not uncommon for states to combine these various methods in attempting to achieve a workable law.8

1 "The name 'Blue Sky Law' indicates the evil at which it is especially aimed, that is, 'speculative schemes which have no more basis than so many feet of blue sky'. . . ." BALLANTINE, CORPORATIONS § 366, at 860 (rev. ed. 1946).
2 Id. § 365, at 859.
3 Jeffs v. Utah Power & Light Co., 136 Me. 454, 461, 12 A.2d 592, 595 (1940). See also BALLANTINE, op. cit. supra note 1, § 365, at 859.
5 Report of the Ohio Bar Association Committee on Corporate Law and Committee on Blue Sky Law in 1 OHIO BAR No. 42, at 1, 7-8 (Jan. 15, 1929).
6 See BALLANTINE, op. cit. supra note 1, § 367, at 862.
7 Ibid. See also Report of the Ohio Bar Association Committee, supra note 5, at 8.
REGISTRATION PROVISIONS

In an attempt to bring uniformity to the various state blue sky laws, and in some cases to improve them, the National Conference of Commissioners on Uniform State Laws, endorsed by the American Bar Association, accepted a Uniform Securities Act. Recognizing that states have different regulatory philosophies, the act was drafted so as to be acceptable in part or in whole depending on the needs of the state.

Most states, including Ohio, have enacted regulatory statutes, namely those which require the registration of securities and dealers. The intent of this article is to discuss in detail the different aspects of the Ohio provisions for securities registration.

I. HISTORY OF THE OHIO BLUE SKY LAWS

Ohio began regulating securities as early as 1913 when the Ohio Constitution was amended to allow the state to supervise and regulate the issuance and sale of stocks and securities. Ohio's first legislation, which became effective on August 8, 1913, was subjected to much criticism and debate. In answer to these objections, a new securities law was enacted in 1929, which, with minor amendment, continues today as the Blue Sky Law of Ohio.

The Ohio Securities Act delegates the administration of the law to the Division of Securities. This organization is provided with the power to make rules for the registration of securities, to regulate the business and sale of the stocks and securities of foreign corporations and joint stock companies in this state as may be prescribed by law. Laws may be passed regulating sale and conveyance of other personal property, whether owned by a corporation, joint stock company or individual. OHIO CONST. art. XIII, § 2.

10 Henn, op. cit. supra note 8, § 307, at 473.
11 Boesel, supra note 4, at 353. The Ohio act also includes some fraud provisions as well as registration provisions. See OHIO REV. CODE §§ 1707.36, .44, .99.
12 The entire section of the Ohio Constitution states:
Corporations may be formed under General laws; but all such laws may, from time to time, be altered or repealed. Corporations may be classified and there may be conferred upon proper boards, commissions or officers, such supervisory and regulatory powers over their organization, business and issue and sale of stocks and securities, and over the business and sale of the stocks and securities of foreign corporations and joint stock companies in this state as may be prescribed by law. Laws may be passed regulating sale and conveyance of other personal property, whether owned by a corporation, joint stock company or individual. OHIO CONST. art. XIII, § 2.
13 103 Ohio Laws 743 (1913).
14 See Boesel, supra note 4, at 352 n.4. This first act was declared constitutional in Hall v. Geiger-Jones Co., 242 U.S. 539 (1917). See also Note, 17 W. RES. L. REV. 1098 (1966).
15 113 Ohio Laws 216 (1929). See also Nida, The Ohio Division of Securities and the Ohio Securities Act, 13 OHIO ST. L.J. 427, 437 (1952).
16 See OHIO REV. CODE § 1707.01(A). See also Boesel, supra note 4, at 353 n.10.
17 OHIO REV. CODE §§ 1707.07, .09.
late the actual sale of securities, to regulate the licensing of dealers, to suspend and refuse registrations of licenses and securities, to make investigations, to make final orders, and to recommend criminal proceedings. The power of the Division of Securities which is most often encountered by the practitioner is its regulatory supervision over security registration.

The Ohio act regulates the securities that may be sold in the state of Ohio, the manner under which they can be offered, and the length of time such offering may exist. Section 1707.07 of the Ohio Revised Code provides that before a security can be sold or a transaction carried out there must be conformity with the registration procedures. It is these procedures that bear careful and full examination.

II. REGISTRATION OF SECURITIES

The Ohio Blue Sky Law sets out two methods of registering securities: the simple description method and the longer and more complicated system of qualification. In addition, certain transactions which are not exempted by law must also be registered in the same manner as securities which must be registered by description.

A. Registration by Description

Registration by description is permitted, regardless of the transaction, for certain securities which by their very nature are relatively free from the possibility of fraud and deceit. Most securi-

18 Ohio Rev. Code § 1707.07.
22 Ohio Rev. Code § 1707.36.
23 Ohio Rev. Code § 1707.22.
24 Ohio Rev. Code §§ 1707.23 (E), .44, .99.
26 For a definition of securities see Ohio Rev. Code § 1707.01.
28 See Ohio Rev. Code § 1707.08.
31 See Ohio Rev. Code §§ 1707.06-.08.
ties which fall into this category are those of a going business or concern which has over the years maintained a good earnings record. Businesses which are just beginning or which have maintained a growth pattern under which financial needs outstrip demonstrated past earnings usually cannot use this method of registration.33

(1) Those Securities Which May be Registered by Description.
—There are three types of securities which may fall into this category:
(a) securities issued by a going concern which has proven its stability;34 (b) securities backed by interests in land mortgages, land tracts, or steamships;35 and (c) securities issued where the company has collateral deposited in trust with a bank.36

(a) Securities Issued by Going Concerns.—Section 1707.05 (A) of the Ohio Revised Code requires that in order to comply with this section, securities must be “issued or guaranteed by a person owning a property or business which has been in continuous operation for not less than three years prior to the date of sale.”37 In addition, such person must show that during “a consecutive period of not less than two nor more than five years terminating not more than six months preceding the date of filing with the division of securities . . .”38 the “average annual net earnings” of issued securities were above a certain set amount.39 In order to

33 PRACTICE MANUAL, op. cit. supra note 30, at 53. See also Boesel, supra note 4, at 361.
34 ORIO REV. CODE § 1707.05 (A). This section is the most commonly used provision in § 1707.05. Letter to the author from the Division of Securities.
35 ORIO REV. CODE §§ 1707.05 (B)-(D).
36 ORIO REV. CODE § 1707.05 (B).
37 ORIO REV. CODE § 1707.05 (A).
38 Ibid. In computing the earnings of a security registered under § 1707.05 (A), the regulations state that if it is filed

on a date more than six months after the end of the fiscal year of the person whose securities are being registered, the required earnings may be computed as to any two or more consecutive fiscal years plus such fractional portion of a year as will terminate not more than six months preceding the date of filing with the Division. Average earnings shall be arrived at by dividing total earnings for the entire period chosen by the number of years and fractional part thereof in such period. If the inclusion of earnings for such fractional portion of a year would distort the estimate of average annual earnings by reason of the fact that earnings of the issuer are seasonal and largely occur during such fractional portion of the year, the Division may require that the figures on earnings for the first fiscal year of the period chosen be broken down to enable a calculation of average earnings on a straight annual basis. Regulations of the Division of Securities R-5B [hereinafter cited as Reg.], Ohio Security Regulations can be found in 2 CCH BLUE SKY L. REP. §§ 34001-851 and in OHIO SECURITIES ACT available from the Division of Securities.
39 ORIO REV. CODE § 1707.05 (A). The annual net earnings are to be determined by use of accepted accounting methods, “after deducting all charges and specified divi-
come under the statute as to interest-bearing securities, the earnings must have been at least one and one-half times the annual interest charges of those securities as well as any other similar obligations of equal rank.\(^40\) As to shares with a specified dividend, such earnings must have been at least one and one-half of the annual dividend requirements of issued securities and obligations of equal rank.\(^41\) If shares have no dividend rate specified, earnings must have exceeded "an amount of not less than five per cent of the maximum offering price of the shares of such class outstanding and any new shares being offered."\(^42\)

(b) Securities Backed by Land Mortgages, Land Trusts, or Commercial Marine Vessels.—Securities which are backed by land mortgages, land trusts, or commercial marine vessels may be registered by description provided they fulfill the statutory demands.

In order for securities backed by land mortgages to come under the registration statute, three requirements must be met:\(^43\) (i) that the notes, bonds, or other evidences of indebtedness "are not judicially declared invalid and no default exists according to the terms of the mortgage or deed of trust securing them";\(^44\) (ii) that they are "secured by a first mortgage lien on real estate, or leasehold estate . . .";\(^45\) and (iii) that they do not violate either of the following two eventualities. First, the "aggregate amount of such notes, bonds or other evidences of indebtedness . . . does not exceed two thirds of the fair value of the mortgaged property. . . ."\(^46\) Second,
the "mortgaged property consists of real estate or leasehold premises demised by bona fide lease for a term of years at an aggregate net rental sufficient, after deducting all charges payable by the lessor, to pay the interest on and principal of all bonds, notes, or other evidence of indebtedness secured by the mortgage." In addition, the term of such lease must extend beyond the maturity of such indebtedness, the rental under such lease must be irrevocably pledged under the mortgage, and the lessee must be a "person, body, government, agency, or bank, any of whose securities would be" either exempt under the statute or subject to the provision for registration of a going concern.

Section 1707.05 (C) of the Ohio Revised Code covers the requirements which must be fulfilled for a land trust to take advantage of registration by description. Such securities may be registered by banks, or other like organizations, as trustee representing some ownership of interests in improved land, or land to be improved. Such securities may be sold "where the aggregate sale price . . . to the public does not exceed either the fair market value of the land exclusive of improvements or two thirds of the fair market value of the land and the improvements erected or forthwith to be erected . . . and where substantially the entire property is leased for a period of not less than twenty-five years under a lease by which the lessee assumes the payment of taxes."

Section 1707.05 (D) allows bonds and notes as well as other evidences of indebtedness which are secured by lien on marine vessels operated in commercial use to be registered by description. However, such vessels must be shown "by policies of marine insurance to have a value, over and above all other indebtedness buildings to be built when sufficient funds are already or will be available whether through corporate planning or financing."

It is important to remember that when a registration is filed based on § 1707.05 (B) (1), the filer must along with his description, also file an appraisal signed by three persons who are both knowledgeable of value and disinterested as to the issuance. OHIO REV. CODE § 1707.08 (E).

47 OHIO REV. CODE § 1707.05 (B) (2).
48 OHIO REV. CODE § 1707.05 (B) (2) (a).
49 OHIO REV. CODE § 1707.05 (B) (2) (b).
50 OHIO REV. CODE § 1707.05 (B) (2) (c).

51 The exemption provisions which cover this are found in §§ 1707.02 (B) or (C).
52 See text accompanying notes 37-42 supra.
53 This provision includes title guaranty and trust companies and subsidiaries "wholly owned or controlled by a bank as trustee or cotrustee . . . . " OHIO REV. CODE § 1707.05 (C).
54 OHIO REV. CODE § 1707.05 (C).
secured by prior lien, of not less than one hundred fifty per cent of the principal amount of such . . . [security].’’

(c) Securities Issued Where the Company Has Collateral Deposited in Trust with a Bank.—Securities may also come under registration by description when secured by collateral securities deposited in trust with a bank provided such collateral fits the requirement detailed in the statute.

(2) Those Transactions Which May be Registered by Description.—In addition to those securities which are permitted to be registered by description, four types of transactions will also qualify for this simplified method, and at the same time not require the issuer to qualify as a dealer: (a) securities issued where a company has collateral deposited in trust with a bank; (b) securities sold to not more than fifteen shareholders; (c) securities sold in an unincorporated entity which does not have over ten members; and (d) securities sold to current holders in the same class. The rationale behind the inclusion of these transactions seems to be that all involve sales by small issuers or sales to existing shareholders, thereby decreasing any likelihood of fraudulent conduct. In order to more fully understand these provisions, it is important to examine the four classes of transactions in some detail.

(a) Securities Sold for Intangible Property With a Limited Commission.—Section 1707.06(A) (1) permits transactions to be registered by description if the following three factors are present: (i) the sale is of securities of an Ohio corporation; (ii) no part of the sale is issued for intangible property or property out of the state of Ohio; and (iii) the total commission does not exceed three per cent of the total sale price. While this statute is basically clear, certain problems have arisen as to what constitutes permissible tangible property for the sale and how the three per cent commission is to be calculated.

Tangible property as it is used in the Ohio Blue Sky Law means “all property other than intangible property and includes securities, accounts receivable, and contract rights, when such securities ac-

55 Ohio Rev. Code § 1707.05 (D).
56 See Ohio Rev. Code §§ 1707.05 (E) (1)-(3).
58 See Ohio Rev. Code § 1707.06 (B).
counts receivable, or contract rights have a readily determinable value." Thus it would seem that if the consideration fits into this provision the statute is satisfied. However, if the tangible property is not cash, the Division of Securities requires that with the registration form there be included either a sworn appraisal of the dollar value of the property, done by a disinterested and competent appraiser, or other proof of the value of such consideration.

Upon receipt of this proof of value, the Division of Securities conducts a study of the matter and, if they find that the sale was not on grossly unfair terms and not done to defraud or deceive purchasers or sellers, a certificate of acknowledgment is issued.

A question also arises as to what is included in computing the requirement that a commission cannot exceed three per cent of the total sale price. Suppose, that the total commission, remuneration, expense, or discount paid by a corporation does not come to more than the three per cent limit of the total sale price. However, certain officers of the corporation pay an additional consideration to the persons handling the distribution of the shares. The Division of Securities has ruled that in this situation the transaction has violated the statute and the intent of the legislature. "The total commission . . . is limited to 3% of the total sale price . . . irrespective of whether or not this amount is paid by an issuer or by some other person or persons. . . . The all-inclusive nature of this pro-

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60 OHIO REV. CODE § 1707.01(L) (2). Since the statute states that the sale should be made out of property not intangible property, it would be useful to define intangible property. OHIO REV. CODE § 1707.01(L) (1) defines intangible property as: "Intangible property" means patents, copyrights, secret processes, formulas, services, good will, promotion and organization fees and expenses, trademarks, trade brands, trade names, licenses, franchises, any other assets treated as intangible according to sound accounting practice, and securities, accounts receivable, or contract rights having no readily determinable value. Ibid.

61 Reg. R-6A.

62 Ibid. When protection of investors is involved the Division of Securities can permit an escrow of securities issued for consideration other than cash. Ibid.

Professor Cavitch, in his corporations text, notes that at times a problem arises where a corporation initially issued stock for intangible property which would qualify as an exemption under OHIO REV. CODE § 1707.03(O), and later issues additional stock which is to be paid for with cash. The question then arises whether these two issues should be integrated which perhaps would violate § 1707.06(A) (1). In such a situation he states that

The Division of Securities takes the point that a subsequent registration by description . . . will prompt the Division to consider whether, in view of the exempt initial issue for intangible property, the subsequent issue will be disposed of or purchased on grossly unfair terms as in such manner as to deceive or defraud or tend to deceive or defraud purchasers or sellers. CAVITCH, op. cit. supra note 57, at 559.
vision is obvious." This same result, namely a violation of the statute, occurs when certain interested purchasers pay additional compensation to representatives of an issuing company, if such compensation brings the total commissions to be received by the representatives to more than the statutory amount.

(b) Securities Sold to Not More than Fifteen Shareholders.—The second type of transaction which may be registered by description is the sale of securities to not more than fifteen shareholders. Section 1707.06(A)(2) permits a corporation to sell shares or subscriptions of shares provided the following conditions are satisfied: (i) the corporation is organized under Ohio laws or authorized to do business in Ohio; (ii) the sale is for a corporation's own shares; (iii) the total number of shareholders does not exceed fifteen; and (iv) the securities are issued and sold in good faith for the sole account of the issuer. If it can be shown that the sale was not done in good faith or that it was done to avoid the Blue Sky Law, the registration will not be permitted under this section.

The two especially difficult areas in this provision concern the fifteen-shareholder limit and the requirement that the securities be issued for the sole account of the issuer. The test of what is the number of shareholders is not the number of offerees, but instead the number of ultimate shareholders. In order to clarify this position, the Division of Securities has provided by regulation that if as a result of the sale the beneficial owners of the shares of such a corporation exceed fifteen, although the record owners do not exceed that number, there is presumed a prima facie case of bad faith and an intent to evade the provisions of the act. If, however, the number of record or beneficial owners exceeds fifteen by operation of law, the presumption will not exist.

The second question is whether the sale is for the sole account of the issuer when a company pays a commission to a salesman employed by them for selling the shares. The Division of Securities has said that the legislature intended that the securities be sold for the sole account of the issuer by the issuer, and that therefore the

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63 Ohio Division of Securities Administrative Ruling 8 [hereinafter cited as Ruling]. Administrative Rulings can be found in 2 CCH BLUE SKY L. REP. §§ 34001-851 and in OHIO SECURITIES ACT available from the Division of Securities.

64 1937 Ops. ATT’Y GEN. (Ohio) 1256.

65 OHIO REV. CODE § 1707.06(A)(2). See also CAVITCH, op. cit. supra note 57, at 559-60.

66 Reg. R-6C.

67 Ibid.
employment of a salesman on commission was apparently not intended.\textsuperscript{68} The statute suggests that "the corporation should receive the total gross proceeds of the sale of such securities undiminished by commission."\textsuperscript{69} It would seem, however, that if the salesman was not on commission the procedure would be permissible.

\textbf{(c) Securities Sold in an Unincorporated Entity Which Does Not Have Over Ten Members.}\—The third group of transactions which fall within the registration by description provision are those of an unincorporated entity in which the following conditions exist: (i) the total number of persons holding a beneficial interest in securities does not exceed ten after the sale is completed; (ii) no commission or other remuneration is paid; and (iii) the total expenses in connection with the sale do not exceed one per cent of the total sales price of the offered securities.\textsuperscript{70} Thus it would appear that sales of securities representing an interest in such entities as partnerships, trusts, and syndicates fall into this simplified registration method.

\textbf{(d) Securities Sold to Current Holders in the Same Class.}\—The last group of transactions which qualify for the description method of registration are securities sold to current holders of that class. Section 1707.06(A)(4) provides for the offering of securities to current shareholders provided the sale is made to the corporation's own security holder exclusively and that no commission or other remuneration is paid out due to the sale.\textsuperscript{71} The only exception to the rule preventing remuneration exists when some of the issue is not bought up by the shareholders and the residue is sold to a dealer at a discount or to a firm which might be underwriting the transaction.\textsuperscript{72}

The question arises whether a sale may be made to some members of a class and not to all members of such a class. Such an action may violate the pre-emptive rights provisions in section 1707.15 of the Ohio Revised Code if such is provided for in the articles of incorporation. In addition, the Division of Securities has ruled that section 1707.06(A)(4) is "not available for registration of an offering of securities of a corporation to less than a class of security

\textsuperscript{68} Ruling 9.
\textsuperscript{69} Ibid.
\textsuperscript{70} Ohio Rev. Code § 1707.06(A)(3).
\textsuperscript{71} See also CAVITCH, op. cit. supra note 57, at 561.
holders. The section, as drafted, contemplates a general offering to all of a class of security holders."

(3) The Procedure for Registering Securities and Transactions by Description.—Registration by description is a relatively simple procedure. The information which need be filed is spelled out in section 2707.08 of the Ohio Revised Code and also on the forms of the Division of Securities.

(a) Registration Requirements Under Ohio Revised Code Section 1707.08.—Section 1707.08 of the Ohio Revised Code requires that in order to register, a description must be filed setting forth the name of the issuer, a brief description of those securities offered, the amount of securities to be sold, the price at which it is offered, and a brief statement of facts sufficient to prove that it falls within the registration by description sections of the Code. This information is to be filed on the correct form prescribed by the Division of Securities along with a verification of the filing and the necessary fee.

(b) Division Procedure Upon Receipt of Registrations by Description.—The procedure to be followed once the description form and necessary fee are delivered to the Division is governed by the regulations of the Division of Securities. Upon receipt of an application the Division promptly examines it and if it appears to meet the statutory requirements a certificate of acknowledgment is issued. Upon receipt of such acknowledgment, transactions under section 1707.06 and sales of those securities specified in section 1707.05 may be carried out for the effective period of the registration.

At times, however, the certificate of acknowledgment will not issue. If the registration on its face or from a review of official rec-

78 Ruling 10.
74 Ohio Rev. Code § 1707.08 (A).
76 Ohio Rev. Code § 1707.08 (B).
76 Ohio Rev. Code § 1707.08 (C). If all of "the securities to be sold are not offered by the person filing the description, then the respective amounts to be offered by others, so far as such amounts are known, and the names and addresses of such other offerors..." must be filed. Ibid.
77 Ohio Rev. Code § 1707.08 (E).
78 The registration provisions are Ohio Rev. Code §§ 1707.05-.06.
79 Ohio Rev. Code § 1707.08 (D).
80 Ohio Rev. Code § 1707.08.
81 See p. 1137-38 infra.
82 See Reg. R-8A.
83 Reg. R-8A (a).
ords appears to have some "inconsistency, ambiguity, deficiency or other defect of substance" the party filing the registration will be so notified and permitted to amend the registration. If no amendment appears within thirty days, the Division will deem the original application to be ineligible and ineffective for failing to comply with the statutory provision.

When a description appears to comply, but needs further explanation or amplification, the Division will notify the party filing the registration to give the supplemental information within thirty days. Failure to do so will result in a suspension of registration for "failure to comply with a Division order."

(c) Effective Periods of Registration.—The periods vary under which the securities may be sold and transactions consummated. Those securities described in section 1707.05(A) may be sold for a period of thirteen months following the date of filing. The sales of other securities specified in section 1707.05(B)-(E) as well as those transactions specified in section 1707.06 are permitted to be consummated during such time as the registration remains in force. However, the Division of Securities does require semi-annual reports showing the "number and amount of securities sold during the preceding six months and ... [a] balance sheet and a profit and loss statement for a period ending not more than ninety days prior to the date of filing. . . ."

(d) Fees for Registration by Description.—The fees for filing

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84 Reg. R-8A(b).
85 OhiO Revised Code § 1707.08 states that amendments can be made by the person who filed the form when used to correct errors or omissions. The actual procedure for amending a registration by description is covered by Reg. R-8B. If the errors are numerous, the amendment should be perfected by filing a new form marked "Amended." Reg. R-8B(a) (1). If there are only isolated errors, the correction should be made by filing a supplemental description upon a form, but with only the corrected errors filled in. The form should be marked, "Amendment to _________." Reg. R-8B(2).
86 Reg. R-8A(b). Purported amendments which are not proper matters of amendment, e.g., change of sale plans, are inoperative. Reg. R-8B(b).
87 Reg. R-8A(c).
88 OhiO Rev. Code § 1707.05(A) refers to securities of a going concern. See text accompanying notes 37-42 supra.
89 OhiO Rev. Code §§ 1707.05(B)-(E) covers securities backed by land mortgages and trusts, commercial marine vessels, and collateral deposited in trust with a bank. See text accompanying notes 43-56 supra.
90 For the various types of transactions which may be registered by description, see text accompanying notes 57-73 supra.
91 Reg. Q-2. See Practice Manual, op. cit. supra note 72, at 55 for the forms to use for the semi-annual reports.
by description are regulated by statute. For those securities which fall within this registration method, as described in section 1707.05, the fee is one-twentieth of one per cent with a minimum set at twenty-five dollars and a maximum at 300 dollars. Transactions which can be registered by description under section 1707.06 require the payment of only twenty dollars.

(e) Forms for Registering Securities and Transactions by Description.—Section 1707.08 of the Ohio Revised Code states that registration by description "shall be on forms prescribed by the Division . . . ." Each form contains all the information that the filer needs to know, including pertinent instructions and regulations.

The following chart shows the forms which should be used to register by description.

<table>
<thead>
<tr>
<th>Statutory Provision Covered</th>
<th>Use of Form</th>
<th>Form Number</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ohio Revised Code sections 1707.05 (B)-(E)</td>
<td>No form is provided for these sections*</td>
<td></td>
</tr>
<tr>
<td>Ohio Revised Code section 1707.05 (A)</td>
<td>To effect registration by description</td>
<td>Form 5 (A)</td>
</tr>
<tr>
<td>Ohio Revised Code section 1707.05 (A)</td>
<td>Supplemental report to continue a registration by description</td>
<td>Form 5 (A) (5)</td>
</tr>
<tr>
<td>Ohio Revised Code sections 1707.06 (A) (2) and 1707.03 (O)*</td>
<td>To effect registration by description or to give notice of exemption</td>
<td>Form 6 (A)</td>
</tr>
<tr>
<td>Ohio Revised Code section 1707.06 (A) (3)</td>
<td>To effect registration by description</td>
<td>Form 6 (A) (3)</td>
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<td>Ohio Revised Code section 1707.06 (A), (B)</td>
<td>To register by description oil and gas interests</td>
<td>Form 6 (A) (3) - OG</td>
</tr>
<tr>
<td>Ohio Revised Code section 1707.06 (A) (4)</td>
<td>To effect registration by description</td>
<td>Form 6 (A) (4)</td>
</tr>
</tbody>
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* The Division of Securities in a letter to the author stated that no forms have been prescribed for these subsections due to the variety of presentations of operative facts and the probable uniqueness of such types of offerings. In these situations, a form of application is prepared by counsel delineating the responses to the basic requirements of the subsection. This is done with the cooperation of the Division. Further, these subsections are so seldom used that, for the sake of practicality, they might be said to be non-existent.

92 See PRACTICE MANUAL, op. cit. supra note 72, at 55.

93 OHIO REV. CODE § 1707.08. See PRACTICE MANUAL, op. cit. supra note 72, at 55.

94 Ibid.
B. Registration by Qualification

Registration by qualification is the procedure which must be followed if the security or transaction does not qualify for a shorter or simpler procedure. This method of registration, since it is devised to prevent fraudulent conduct in the issuance of securities, requires that the filer present a great deal of information. As such, this procedure is more detailed, expensive, and time consuming.

(1) Those Securities Which Must Register by Qualification.—Section 1707.09 of the Ohio Revised Code provides that all securities and transactions except those which are exempt or are permitted to file by description, must be qualified in order to be the subject matter of sale in the state of Ohio. This method of registration is really a “catch-all” for all securities which are not covered in other sections.

(2) How to Register Securities by Qualification.—Registration by qualification is usually done on the forms prescribed by the Division of Securities and must be accompanied by a sworn statement as to the accuracy and efficacy of the application. The ordinary application must contain certain information about the issuing corporation or entity and about the proposed securities. In order to properly understand this method of registration, it is necessary to examine the following: (a) the information required under the filing section; (b) the permissibility of provisional registration; (c) the procedures for handling registration of the Division of Securities; (d) the effective periods of registration by qualification; (e) the procedures to amend faulty registration; (f) the required forms for proper registration; (g) the procedures to register securities sold without prior registration; and (h) the proper forms for registration by qualification.

(a) Information Required Under Section 1707.09.—In general, section 1707.09 of the Ohio Revised Code requires such in-
formation as who runs and owns the corporation, where it is located, what is the nature of the business, what is the financial status of the issuer, and what are the provisions or articles under which the entity operates. As for information concerning the securities to be offered, the application usually requires that the issuer state the purpose of the sale, a description of the security, the consideration to be received along with a total itemization of expenses so that the net amount to be received can be determined, and a copy of any advertisements that are to be sent out.

In addition to the specific information enumerated in the statute, the Division can require any other information "as it deems necessary to enable it to ascertain whether such securities are entitled to qualification . . ." which may mean "an opinion of counsel as to the validity of securities which are the subject matter of the application. . . ." In lieu of the usual filing procedure, the Division is permitted to allow an applicant to file less information under certain enumerated situations.

(b) Permissibility of Provisional Registration.—At times it is important for a corporation to sell new issues quickly, namely, when favorable market conditions exist. Since the ordinary procedure of registration by qualification can at times be a lengthy process, provision is made for a provisional registration. Applicants who are residents of the state, and non-residents who consent to service, can sell securities pending full qualification "where the division of securities is satisfied that the issuer is solvent and of good

103 Ohio Rev. Code § 1707.09(B).
104 Ohio Rev. Code § 1707.09(C).
105 Ohio Rev. Code § 1707.09(E).
106 Ohio Rev. Code § 1707.09(I).
107 Ohio Rev. Code § 1707.09(F).
108 Ohio Rev. Code § 1707.09(D).
109 Ohio Rev. Code § 1707.09(G).
110 Ohio Rev. Code § 1707.09(H).
111 Ohio Rev. Code § 1707.09(H).
112 Ibid.
113 Ohio Rev. Code § 1707.09(K). The Division is empowered to waive the usual forms and to require that information that it desires in two cases. The first is where a registration is made under the Securities Act of 1933, 48 Stat. 74, as amended, 15 U.S.C. §§77a-aa (1964). The second is the case of securities "theretofore issued and outstanding which may not be made subject matter of transactions exempt under. . ." § 1707.03(M) because such securities were purchased within one year outside Ohio or were transported into Ohio within one year. Ibid.
114 Ohio Rev. Code § 1707.10.
115 Consent to service is provided for in Ohio Rev. Code § 1707.11.
business repute and that such preliminary offering will not deceive or tend to deceive the public. . . .”\textsuperscript{116} Permission to take advantage of this provision is granted in writing provided that the full application of registration is filed within thirty days in the office of securities.\textsuperscript{117}

In order to protect purchasers of securities sold under this provisional registration when the applications are denied, the statute provides that the full proceeds of the sale without deductions for expenses or commissions must be either segregated or “deposited in escrow in such manner . . . as the division directs.”\textsuperscript{118} A failure of the registration will cause the issuer or dealer to withdraw the security from sale and return the consideration paid.\textsuperscript{119}

(c) Actions and Powers of Division of Securities Upon Receipt of Applications for Registration by Qualification.—Upon receipt of an application by a prospective seller, the Division of Securities is empowered to make a complete examination of the issuing corporation and of the securities to be offered at the expense of the applicant.\textsuperscript{120} Upon completion of its study, if the Division of Securities decides to grant the application, notification is sent to the applicant, who upon payment of the registration fee, shall “register the qualification of such securities. . . .”\textsuperscript{121}

In determining whether or not to grant an application, the Division is required to exercise its judgment to decide that none of the following four factors exist. First, the Division must decide that the issuer is not conducting his business in a fraudulent manner.\textsuperscript{122} Second, it must be ascertained that the offering proposed is not on “grossly unfair terms.”\textsuperscript{123} Third, it is necessary that the plan of “issuance and sale” which is proposed “would not defraud or deceive, or tend to defraud or deceive, purchasers. . . .”\textsuperscript{124} The fourth prerequisite is that the issuer, after a payment of all commissions, will

\textsuperscript{116} OHIO REV. CODE § 1707.10.
\textsuperscript{117} The division is authorized to grant additional time at its discretion. See OHIO REV. CODE § 1707.10.
\textsuperscript{118} Ibid.
\textsuperscript{119} Ibid.
\textsuperscript{120} See OHIO REV. CODE § 1707.09.
\textsuperscript{121} Ibid.
\textsuperscript{122} Ibid. See also PRACTICE MANUAL FOR CONTINUING LEGAL EDUCATION PROGRAM: ADVISING SMALL BUSINESS CLIENTS 56 (1963) [hereinafter cited as PRACTICE MANUAL].
\textsuperscript{123} The term “grossly unfair terms” is a complex subject. For a brief discussion of some factors which fall into this area see PRACTICE MANUAL, op. cit. supra note 122, at 56-57. See also Rulings 16-20.
\textsuperscript{124} OHIO REV. CODE § 1707.09.
receive "not less than eighty-five per cent of the aggregate price at which all such securities are sold by or on behalf of the issuer. . . ." Under the last requirement the issuer can receive less than his eighty-five per cent share of the aggregate price if he has to bear reasonable expenses of the issuance, for example, legal fees.

(d) The Effective Periods of Registration by Description.—Once securities have been qualified and the fee paid, any dealer who is licensed "may thereafter sell such securities . . . so long as such qualification remains in force." However, the issuer is required to file semi-annual reports with the Division of Securities for as long as he is selling such securities. The reports must show "the number and amount of securities sold during the preceding six months and shall include a balance sheet and a profit and loss statement for a period ending not more than 90 days prior to the date of filing thereof." The applicant, in order to make the amendments effective may need to pay the additional fee that would have been required if the original application had contained the provisions added by amendment.

(f) Fees for Registration by Qualification.—Registration by qualification is more expensive than the aforementioned registration by description. The initial filing of an application requires that a twenty-five dollar fee accompany it. In the event that the registration is accepted, an additional fee of one-twentieth of one per

126 Ibid.
128 Reg. Q-2. The same requirement exists in the case of registration by description.
130 Ibid.
131 See text accompanying notes 92-94 supra.
cent of the aggregate price of the securities is also charged.\textsuperscript{133} In no event, however, should the fee be below twenty-five dollars and above 500 dollars.\textsuperscript{134} These fees, however, do not include costs of examinations as are permitted under section 2707.09(K).

\textbf{(g) Qualification of Securities Sold Without Compliance with the Ohio Blue Sky Laws.---}\textsuperscript{135} When securities have been sold in Ohio without compliance with the registration provisions now in effect, "any interested party may apply in writing to the division of securities for qualification of such securities..." If the Division finds that no one has been defrauded or damaged by the non-compliance or sale and that the qualification will not harm anyone, "the division may permit such registration to be qualified upon payment..." of prescribed fees.\textsuperscript{136} It is important to note, however, that such persons may still be subject to the criminal and civil liabilities arising out of their actions.\textsuperscript{137}

\textbf{(b) Forms to be Used for Registration by Qualification.---}\textsuperscript{138} As was previously mentioned with registration of securities and transactions by description, forms setting forth the required information together with the pertinent regulations are available from the Division of Securities.

The following chart specifies the forms to be used.\textsuperscript{139}

\begin{tabular}{|l|l|l|}
\hline
Statutory Provisions Covered & Use of Form & Form Number \\
\hline
Ohio Revised Code section 1707.09 To apply for registration by qualification & Form 9 \\
\hline
Ohio Revised Code section 1707.09 To apply for registration by qualification of oil and gas securities & Form 9-OG \\
\hline
Ohio Revised Code section 1707.09 To consent to service by non-resident for registration by qualification & Form 11 \\
\hline
Ohio Revised Code section 1707.39 To register by qualification securities having been sold without compliance with the statutes on registration & Form 39 \\
\hline
\end{tabular}

\textsuperscript{133} \textit{Ibid.}

\textsuperscript{134} \textit{Ibid.}

\textsuperscript{135} \textit{Ohio Rev. Code} § 1707.39.

\textsuperscript{136} \textit{Ibid.} The fee is $25 plus the amounts prescribed in \textit{Ohio Rev. Code} § 1707.09. See text accompanying notes 131-34 \textit{supra.}


\textsuperscript{138} See text accompanying notes 95-98 \textit{supra.}

\textsuperscript{139} \textit{Ibid.}
III. Power of Division of Securities to Suspend a Registration

A. Power to Suspend a Registration

The Division of Securities can suspend both the registration of securities and the right of issuers or of dealers to "deal in any particular security whether it is registered, qualified or exempt..." There seem to be three general grounds for this suspension: (1) that the issuer has violated the statutory provisions or regulations, or has conducted his business or sale of securities in a fraudulent and deceptive manner; (2) that the securities were disposed of or purchased on grossly unfair terms; and (3) that the issuer was insolvent when the securities were sold.

Notice of such suspension, specifying the particular securities which are suspended must be sent to all licensed dealers and to the issuer. The notice shall also "set a date, not more than ten days later than the date of the order of suspension, for a hearing on the continuation or revocation of such suspension." Since the statute states that the ten days runs from the date of suspension, a problem can arise as to what occurs if the notice is never received by the interested party. Provision is made for this contingency by allowing the Division to continue a hearing for requests based on good cause.

B. Hearing on a Suspension of Registration

Section 1707.13 of the Ohio Revised Code provides that the Division of Securities shall conduct a hearing using the authority and powers provided in section 1707.23. Such power includes compelling parties to give such additional information as it deems necessary, to require attendance of parties by subpoena and production of records by subpoena duces tecum, to initiate criminal proceed-
ings by presenting evidence to the county prosecutors, to require dealers to produce copies of advertisements, to require dealers to notify the Division of an intention to carry out a sale or transaction, and, if necessary, to suspend or revoke the license of a seller.

At the completion of the hearing, the Division is required to confirm or revoke the suspension placed on the parties. It is important to note, however, that no suspension can invalidate any sale of securities made before the suspension.

IV. Appeals From Orders Denying or Suspending Registration of a Security

The rules governing appeals from decisions of the Division of Securities are found in section 1707.22 of the Ohio Revised Code and in the Ohio Administrative Procedure Act. A. When Can a Party Appeal

Section 1707.22 of the Ohio Revised Code permits an aggrieved party to appeal to the court of common pleas from an unfavorable decision of the Division of Securities. Specifically, a party can appeal "whenever the division has refused to qualify securities or has suspended or revoked... registration... by description or by qualification, or the right to buy, sell, or deal in any particular security whether it is registered or qualified or exempt..." Appeals will also lie for denials of registrations of transactions.

B. Procedure for an Appeal and Temporary Suspension of an Agency Order

The parties adversely affected by a denial or suspension of a registration may appeal such order to the Court of Common Pleas is done in the same manner as in criminal cases. A party who refuses to obey the Division's subpoena is subject to two possible actions. Under § 1707.24 the division can apply to the court of common pleas to issue a subpoena with the failure to obey constituting contempt proceedings. The second remedy is for the director of commerce to apply to a court of common pleas to order an injunction against sale of securities and any other relief that the facts warrant. Ohio Rev. Code § 1707.25. 

OHIO REV. CODE § 1707.23 (E).

OHIO REV. CODE § 1707.23 (F).

OHIO REV. CODE § 1707.23 (G).

OHIO REV. CODE § 1707.23 (D).

OHIO REV. CODE § 1707.13.

Ibid.

OHIO REV. CODE §§ 119.01-13.

OHIO REV. CODE § 1707.22.

Ibid.
of Franklin County within fifteen days after the mailing of such notice. Notice of such appeal setting forth "the order appealed from and the grounds of . . . [the] appeal" must be filed with the Division of Securities and with the court.

After the notice of appeal is filed, the agency within twenty days must "prepare and certify to the court a complete record of the proceedings in the case." The cost of this record is taxed as part of the costs of the appeal.

While a notice of appeal will usually not automatically suspend an agency order, the court can so decide provided it is convinced that the party will suffer an unusual hardship. Such suspension of an agency order can continue to remain in force if a decision of the court of common pleas is appealed.

C. Hearing of an Appeal

The actual hearing on an appeal from a decision of the Division of Securities is conducted in accordance with the rules applicable to all civil actions. This means that the court can require the submission of briefs and oral argument.

Ordinarily, the appeal is confined only to the record which was certified by the agency. However, if additional newly discovered evidence appears, which could not "with reasonable diligence" have been presented to the agency, the court can permit its introduction. At the conclusion of the trial the court can either affirm the agency ruling if it finds "that the order is supported by reliable, probative, and substantial evidence and is in accordance with the law . . ." or reverse or modify the Division making what it considers to be the proper decision. After the court makes its decision, there is still procedure available after ten days for the plaintiff to file a new registration, or for the Division, after proper

157 Ibid.
158 Ibid. If the agency fails to comply and does not certify the record to the court, the court will allow a motion for a finding for the party adversely affected. However, the court may grant up to a ten day extension of time if the agency attempted but failed to comply. Ibid.
159 Ibid.
160 Ibid. The statute also provides that these hearings shall have a preference on the trial docket no matter what position they may be on the calendar. Ibid. This procedure is also an effective method to prevent hardship.
161 Ibid.
164 Ibid.
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notice and hearing, to again revoke or suspend a registration or right to buy and sell provided proper cause occurs or is discovered after the court decision.\textsuperscript{165}

D. \textit{Appeals From the Court of Common Pleas}

The judgment of the court of common pleas is final and binding unless changed on appeal.\textsuperscript{166} Such an appeal may be filed by either the aggrieved party or the agency. If the agency appeals, it must claim either that the common pleas court was incorrect in holding the agency’s decision was not supported by sufficient evidence, or that there are questions of law relating “to the constitutionality, construction, or interpretation of statutes and rules and regulations of the agency. . . .”\textsuperscript{167} The appellate court is required to certify its judgment to the agency or take whatever steps are necessary “to give its judgment effect.”\textsuperscript{168}

V. \textbf{Conclusion}

Since as early as 1913, Ohio has used its police power to regulate the sale of securities. Subscribing to the view that proper registration of securities before sale will prevent the possibility of many fraudulent practices, Ohio, most states, and the Uniform Securities Act provide for advance registration. In Ohio, a security or transaction which is not excused from registration must either register by description, a simple notification procedure, or by qualification, a drawn out procedure to inform the Division of Securities of all important aspects of the corporation’s business activities.

The actual procedure for filing under the Ohio Blue Sky Laws could be extremely complex, if it were not for the Division of Securities which is not only helpful in explaining the proper procedure, but also in designating forms which include the instructions and regulations pertinent to the particular problems involved. It is apparently because of the Division’s helpful and co-operative attitude that little use is made of the appellate procedure specified in the statutes.

\textbf{JAMES D. KENDIS}

\textsuperscript{165} See OHIO REV. CODE § 1707.22.
\textsuperscript{166} OHIO REV. CODE § 119.12. Appeals shall proceed as is provided in OHIO REV. CODE §§ 2505.01-45. \textit{Ibid.}
\textsuperscript{167} OHIO REV. CODE § 119.12.
\textsuperscript{168} \textit{Ibid.}