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NOTE

STATE EXEMPTIONS FROM SECURITIES REGULATION COEXTENSIVE WITH S.E.C. RULE 146

The Federal Securities Act of 1933¹ (the 1933 Act) and state blue sky laws² have various registration and antifraud provisions designed to protect investors in an offering of securities made by an issuer. To provide this protection, the federal and state acts require the issuer to disclose all material information necessary to enable a purchaser to make a knowledgeable investment decision. Most state blue sky laws also provide for a merit standard under which the state commissioner of securities³ has the power to deny issuance if the securities offered or the terms of the offering are not "fair, just and equitable."

An issuer of securities will often attempt to avoid the expense of registration by utilizing one of the exemptions from registration found in the 1933 Act and state laws. One of these is the private offering exemption. Recently promulgated Securities and Exchange Commission Rule 146,⁴ implementing section 4(2)⁵ of the 1933 Act, clarifies what offerings are private under the federal law; similar state provisions set out the blue sky law private offering exemptions. Often prerequisites for the federal and state private offering exemptions are quite different, making coordination difficult, if not impossible.

Shortly after the Securities and Exchange Commission (S.E.C.) promulgated Rule 146, two states—Maryland and Delaware—adopted rules that would automatically exempt from state registration any offering that is exempt from federal registration under Rule 146; in other words, they established state exemptions coex-

¹ 15 U.S.C. §§ 77a-77aa (1970).

² "The name that is given to the law indicates the evil at which it is aimed, that is . . . 'speculative schemes which have no more basis than so many feet of "blue sky."'" Hall v. Geiger-Jones Co., 242 U.S. 539, 550 (1917).

³ In some states, the secretary of state or some other administrator makes this determination. For a listing of the name and address of the responsible official in each state, see 1 BLUE SKY L. REP. 811 (1975).

⁴ SEC Rule 146, 39 Fed. Reg. 15,261-68 (1974) [hereinafter cited as Rule 146]; SEC Securities Act Release No. 5487 (April 23, 1974), 1 CCH FED. SEC. L. REP. ¶ 2710 (1974).

⁵ 15 U.S.C. § 77d(2) (1970).

tensive with Rule 146.⁶ However, most states have not followed this course, and two more—California and Wisconsin—have explicitly refused to do so. This Note will examine these recent state responses to the adoption of Rule 146.

I

SECURITIES REGULATION

A. Federal Registration

The 1933 Act requires that all offerings of securities made by an issuer through use of the mails or other facilities of interstate commerce must be registered with the Securities and Exchange Commission.⁷ To register, the issuer must file a registration statement disclosing all material information about the issuer and offering; most of this information is in the form of a prospectus which could be distributed to investors. The minimum expense for an S-1 registration⁸ is \$100,000.⁹ This is, of course, burdensome to a company making a small offering,¹⁰ and may force it to forego "going public" altogether.¹¹

Congress, however, has provided for several exemptions from the registration requirements of the 1933 Act.¹² The House of Representatives Report on the Act explains that it "carefully exempts from its application certain types of securities and se-

⁶ On May 22, 1975, Hawaii, following Maryland and Delaware, adopted a similar state exemption coextensive with Rule 146. See note 78 *infra*.

⁷ 15 U.S.C. § 77e (1970) (§ 5 of the 1933 Act).

⁸ Form S-1 is the standard registration statement and is used in all offerings for which no other form is specifically prescribed. It contains 21 items of information required in the prospectus distributed to investors, and an additional ten items of information which are not required in the prospectus. The information required by Form S-1 falls into four general categories—(1) the method of offering, (2) a description of the security, (3) a description of the issuer and its business, and (4) an explanation of the management and control structure of the issuer. SEC Form S-1, 17 C.F.R. § 239.11 (1968). See D. RATNER, *SECURITIES REGULATION* 84-85 (1975).

⁹ Alberg & Lybecker, *New S.E.C. Rules 146 and 147: The Nonpublic and Intrastate Offering Exemptions from Registration for the Sale of Securities*, 74 COLUM. L. REV. 622 n.2 (1974). It has been estimated that the expense for a public offering of an \$8 million bond issue would run about \$170,000, whereas a private placement would cost about \$55,000. H. HENN, *LAW OF CORPORATIONS* 576 n.10 (2d ed. 1970).

¹⁰ In an offering of \$1,000,000, with a typical 10% underwriting discount, the cost of registration would leave the company with only \$800,000. Alberg & Lybecker, *supra* note 9.

¹¹ For a case history of the process of a security registration and an illustration of other problems that may cause an issuer to forego going public, see Mofsky, *State Securities Regulation and New Promotions: A Case History*, 15 WAYNE L. REV. 1401 (1969).

¹² A security exempt from registration is still subject to the federal antifraud provisions found in § 12 and § 17 of the 1933 Act, 15 U.S.C. §§ 77l, 77q (1970), and § 10(b) of the 1934 Act, 15 U.S.C. § 78j(b) (1970).

curities transactions where there is no practical need for its application or where the public benefits are too remote."¹³

Section 4(2) of the 1933 Act exempts "transactions by an issuer not involving any public offering."¹⁴ Thus, as an alternative to the costly registration process for a public offering, an issuer may make a "non-public" or private offering. However, the judicial and S.E.C. interpretations of section 4(2) have made the requirements of the exemption unclear and reliance on it uncertain.¹⁵ Although the private offering exemption speaks in terms of "transactions," every offer or sale involved in an offering must meet its requirements. Offer or sale of even one security that does not comply with the terms of the section destroys the exemption for the entire offering. Section 12(1)¹⁶ of the 1933 Act, which imposes civil liability for the sale of any security that is not registered and not exempt, makes reliance on section 4(2) risky.¹⁷

In order to make the standards of a private offering more objective and to provide a degree of certainty to issuers relying on the exemption, the S.E.C. on April 23, 1974, adopted Rule 146. The Rule provides that an offering is deemed to be private under section 4(2) if the following requirements are met:¹⁸

1. *Limitations on Manner of Offering*—No general advertising

¹³ H.R. REP. No. 85, 73d Cong., 1st Sess. 5 (1933). Section three of the 1933 Act provides exemptions for the type of security offered, such as government bonds, certain notes, securities issued by a non-profit organization, etc. It also exempts any security which is part of an issue offered only within a single state. 15 U.S.C. § 77c (1970). Section four exempts certain transactions, such as private offerings, private sales by a person not an issuer, underwriter, or dealer, broker transactions, and certain dealer sales. 15 U.S.C. § 77d (1970).

¹⁴ 15 U.S.C. § 77d(2) (1970).

¹⁵ Uncertainties arose over requirements as to the degree of sophistication of offerees, the access they must have to material information, limitations on resale, the number of offerees, their relationship to each other and to the issuer, the number of shares offered, the amount of the offering, and the manner of offering. Some of these factors will be dealt with later in this Note. See also Alberg & Lybecker, *supra* note 9; Hill York Corp. v. American Int'l Franchises, Inc., 448 F.2d 680 (5th Cir. 1971).

¹⁶ 15 U.S.C. § 77l(1) (1970).

¹⁷ For example, if one security of the offering is sold to an individual who is not sufficiently sophisticated (see notes 20, 88-92 and accompanying text *infra*), the exemption is lost for the entire offering. Those who have sold any of the securities of the offering have therefore sold them without registration or exemption, a violation of § 12(1). They are thus liable to any person who bought the security from them for any loss in value the security has suffered. See Henderson v. Hayden, Stone Inc., 461 F.2d 1069 (5th Cir. 1972). In that case, plaintiff, who had bought \$180,000 worth of stock in an offering totaling \$300,000, sought to rescind his purchase under § 12(1) because the offering had not been registered. The court allowed rescission even though the plaintiff was clearly a sophisticated investor, because the defendant failed to prove the availability of the private offering exemption as to other investors who had bought the security.

¹⁸ Rule 146(b).

may be used to sell the securities, except under very limited circumstances.¹⁹

2. *Nature of Offerees*—Each person to whom the security is offered and sold must either meet certain sophistication requirements,²⁰ or be able to bear the economic risk of the investment and hire an “Offeree Representative” who meets the sophistication requirements.²¹

3. *Access to or Furnishing of Information*—Each offeree must have access to or be furnished with the kind of information that would be included in a registration statement, and have the opportunity to ask questions of the issuer and obtain any additional information necessary.²²

4. *Number of Purchasers*—The issuer shall have reasonable grounds to believe, and after making reasonable inquiry shall believe, that there are no more than thirty-five purchasers of the securities in any offering pursuant to the Rule.²³

5. *Limitations on Disposition*—The issuer must exercise reasonable care to assure that the purchasers of the securities are buying for investment purposes, rather than for resale.²⁴

B. State Regulation

Even if an offering is exempt from federal registration under section 4(2) or Rule 146, it may be subject to registration and other requirements under the blue sky laws of the states in which it is to be offered. The *Uniform Securities Act*, adopted by thirty-one jurisdictions,²⁵ requires much the same information in a registration

¹⁹ Rule 146(c).

²⁰ The offeree must have “such knowledge and experience in financial and business matters that he is capable of evaluating the merits and risks of the prospective investment.” Rule 146(d).

²¹ Rule 146(d). For a more complete discussion of the sophistication requirement, see text accompanying notes 88-92 *infra*.

²² Rule 146(e). For a more complete discussion of the access requirement, see text accompanying notes 93-96 *infra*.

²³ Rule 146(g).

²⁴ Rule 146(h). A private offering is possible without compliance with the requirements of Rule 146. The Preliminary Notes to the Rule state:

Transactions by an issuer which do not satisfy all of the conditions of this rule shall not raise any presumption that the exemption provided by Section 4(2) of the Act is not available for such transactions. Issuers wanting to rely on that exemption may do so by complying with administrative and judicial interpretations in effect at the time of the transactions. Attempted compliance with this rule does not act as an election; the issuer can also claim the availability of Section 4(2) outside the rule.

²⁵ Twenty-nine states plus Puerto Rico and the District of Columbia have adopted the *Uniform Securities Act*. NATIONAL CONFERENCE OF COMMISSIONERS ON UNIFORM STATE LAWS, HANDBOOK Table 1, at 951c (1974); UNIFORM SECURITIES ACT, Table of Jurisdictions 152 (Supp. 1975).

statement as is required in Form S-1 of the 1933 Act.²⁶ Certification of financial statements, one of the most expensive parts of registration, may be required under the *Uniform Securities Act*.²⁷ At least twenty-eight jurisdictions, some of which have adopted the *Uniform Securities Act*, specifically require independent certification of financial statements.²⁸ In most of these states, the only difference between a registration statement under the 1933 Act and under the local blue sky law is the requirement of fewer exhibits in the state registration statement (such as the articles of incorporation and bylaws), hardly a significant part of the expense of a registration statement. An issuer seeking to avoid the expense of registration with the S.E.C. under Rule 146 may find that he has saved very little by the time he has complied with state registration requirements.

²⁶ UNIFORM SECURITIES ACT § 304(b). See note 8 *supra*.

²⁷ The *Uniform Securities Act* authorizes, but does not compel, the state commissioner to adopt rules requiring certified financial statements. *Id.* § 412(c).

²⁸ States requiring audited or certified financial statements by statute are: ARIZ. REV. STAT. ANN. § 44-1894(9) (1967), 1 BLUE SKY L. REP. (Ariz.) ¶ 6184 (1956); GA. CODE ANN. § 97-105(b)(1)(XV) (Supp. 1974), 1 BLUE SKY L. REP. (Ga.) ¶ 14,125 (1975); HAWAII REV. STAT. § 485-10(b)(3)(O) (1968), 1 BLUE SKY L. REP. (Hawaii) ¶ 14,708 (1973); ILL. ANN. STAT. ch. 121½, § 137.5(C)(1)(j) (1975), 1 BLUE SKY L. REP. (Ill.) ¶ 16,205 (1975); IND. ANN. STAT. CODE § 23-2-1-5(b)(6) (Burns 1972), 1 BLUE SKY L. REP. (Ind.) ¶ 17,106 (1975); KY. REV. STAT. ANN. § 292.370(2)(p) (Baldwin Supp. 1974), 2 BLUE SKY L. REP. (Ky.) ¶ 20,107 (1972); NEV. REV. STAT. § 90.150(2)(c) (1973), 2 BLUE SKY L. REP. (Nev.) ¶ 31,119 (1975); N.M. STAT. ANN. § 48-18-19.5(B)(15) (1966), 2 BLUE SKY L. REP. (N.M.) ¶ 34,109 (1973); S.D. COMPILED LAWS ANN. § 47-31-19.1(8) (Supp. 1975), 3 BLUE SKY L. REP. (S.D.) ¶ 44,119 (1975); TENN. CODE ANN. §§ 48-1608(j), (k) (1964), 3 BLUE SKY L. REP. (Tenn.) ¶ 45,108 (1973); TEX. REV. CIV. STAT. art. 581-7(D) (1964), 3 BLUE SKY L. REP. (Tex.) ¶ 46,107 (1967); WASH. REV. CODE ANN. § 21.20.210(14)(d) (Supp. 1974), 3 BLUE SKY L. REP. (Wash.) ¶ 50,122 (1975).

States requiring audited or certified financial statements by commission rule are: Arkansas State Bank Dept., Securities Rule 5(A), 1 BLUE SKY L. REP. (Ark.) ¶ 7605 (1974); California Reg. 260.613, 1 BLUE SKY L. REP. (Cal.) ¶ 8638, at 4607-3 to 4608 (1975) (See also CAL. CORP. CODE § 25,613 (West Supp. 1975), 1 BLUE SKY L. REP. (Cal.) ¶ 8334 (1974)); Colorado Rule 5.01, 1 BLUE SKY L. REP. (Colo.) ¶ 9706 (1975); Florida Securities Division, Rule 3B-2.02, 1 BLUE SKY L. REP. (Fla.) ¶ 13,632 (1972); Idaho Reg. § 30-1430(2), 1 BLUE SKY L. REP. (Idaho) ¶ 15,620 (1975); Kansas Reg. 81-7-1(A), 2 BLUE SKY L. REP. (Kan.) ¶ 19,707 (1973); Maryland Rule S-5(1), 2 BLUE SKY L. REP. (Md.) ¶ 23,613 (1975); Mississippi Reg., 2 BLUE SKY L. REP. (Miss.) ¶ 27,632 (1964); North Dakota Reg., N.D. Securities Bulletin, Feb. 1967, 2 BLUE SKY L. REP. (N.D.) ¶ 37,626 (1974); Oklahoma Rule R-410 (2), (3), 2 BLUE SKY L. REP. (Okla.) ¶ 39,612 (1970); Oregon Administrative Rules, ch. 815, Rule 11-0025, 3 BLUE SKY L. REP. (Ore.) ¶ 40,631 (1972) (requires audited financial statements only for offerings over a certain amount); Pennsylvania, Regulations of the Securities Commission, 64 Pa. Code ch. VI, §§ 6.9.3.1(5), (6), 3 BLUE SKY L. REP. (Pa.) ¶ 41,306 (1975) (See also PA. STAT. ANN. tit. 70, § 1-609(c) (1975), 3 BLUE SKY L. REP. (Pa.) ¶ 41,169 (1972)); Puerto Rico Rules and Regulations, tit. 10, ch. 37, § 892-154, 3 BLUE SKY L. REP. (P.R.) ¶ 41,826 (1971); South Carolina Rule IIC, 3 BLUE SKY L. REP. (S.C.) ¶ 43,657 (1972) (See also S.C. CODE ANN. § 62-7 (1962), 3 BLUE SKY L. REP. (S.C.) ¶ 43,207 (1968)); Utah, Rules and Regulations for Issuers, 3 BLUE SKY L. REP. (Utah) ¶ 47,601 (1973); Wyoming Rules and Regulations, ch. IV, § 1(a), 3 BLUE SKY L. REP. (Wyo.) ¶ 53,612 (1968).

Like the 1933 Act, most state blue sky laws, including the *Uniform Securities Act*, have a private offering exemption. In certain respects, however, these state exemptions are usually more restrictive than Rule 146. *Uniform Securities Act* section 402(b)(9), for example, requires that the *offer* not be made to more than ten persons²⁹ within a twelve month period.³⁰ Other laws have private offering exemptions based on the ultimate number of shareholders (usually limited to ten) after the offering has taken place.³¹ In contrast, Rule 146 allows up to thirty-five *purchasers* of the security, with no limit on the number of offerees or ultimate number of shareholders.³² *Uniform Securities Act* section 402(b)(9) further requires that no commission or other remuneration be paid for soliciting any prospective buyer and thus prohibits use of dealers or underwriters.³³ Rule 146, on the other hand, allows the use of dealers or underwriters in an offering pursuant to the exemption.

C. *The Merit Standard and Disclosure Philosophy*

In addition to registration requirements, most state blue sky laws also impose a merit standard. In these jurisdictions the responsible state official is empowered to deny a license for the sale of securities if, in his opinion, the securities do not meet certain standards of fairness. This approach to securities regulation had its

²⁹ Many states that have adopted the *Uniform Securities Act* have increased this number to 15 or 25. See Appendix.

³⁰ See Appendix for the text of UNIFORM SECURITIES ACT § 402(b)(9).

³¹ The Maine statute, typical of these, provides an exemption for [a]ny sale of securities of a corporation organized under the laws of this State if the number of holders of such securities does not at the time of such sale, and will not in consequence of such sale exceed 10 in number [exclusive of institutional investors].

ME. REV. STAT. ANN. tit. 32, § 874(9) (Supp. 1973), 2 BLUE SKY L. REP. ¶ 22,124 (1974). States with similar statutes are Mississippi, Missouri, New Mexico, Ohio, Texas, Vermont, Virginia and Wisconsin. See Appendix. Besides being very restrictive as to the number of purchasers, the exemption in Maine, Mississippi, New Mexico, and Vermont is only available to a domestic corporation. The Wisconsin exemption applies only to a corporation having its principal office in the state; the Ohio exemption applies only to a corporation incorporated in or qualified to do business in Ohio.

³² Rule 146(g). Fourteen state statutes, like Rule 146, base the private offering exemption on the number of purchasers rather than on the number of offerees. These are Arkansas, which allows up to 35 purchasers, Florida (20), Georgia (15), Indiana (35), Iowa (35), Minnesota (25), Missouri (15 transactions), Oklahoma (25), Oregon (10), Pennsylvania (25), South Dakota (25), Tennessee (15), Texas (15), and Washington (10). See Appendix.

³³ Five states that have adopted § 402(b)(9) omit this provision, and thus allow the use of dealers and underwriters. They are Delaware, Maryland, Nebraska, Nevada, and North Carolina. Massachusetts and Montana allow commissions under limited conditions. Colorado and the District of Columbia have adopted the *Uniform Securities Act*, but not § 402(b)(9). Both allow private offerings in which commissions are paid. See Appendix.

start in Kansas in 1911, in the first securities regulation statute to be passed in this country.³⁴ The law was the result of a sweeping Populist victory in 1910; its paternalistic approach was influenced by Populist sentiments that the "Moneyed East" was bleeding the "Agrarian West."³⁵ The law prohibited the sale of any security in Kansas, unless exempted, until a permit had been obtained from the state commissioner. The commissioner could deny the permit if he found that the plans for the issuer's business

contain any provision that is unfair, unjust, inequitable or oppressive to any class of contributors, or if he decides from his examination of its affairs that said [issuer] is not solvent and does not intend to do a fair and honest business, and in his judgment does not promise a fair return on the stocks, bonds, or other securities by it offered for sale³⁶

Other Populist areas quickly followed the lead of Kansas,³⁷ but the Eastern states generally did not pass merit standard statutes until after World War I, and these laws were generally not as harsh as those enacted earlier.³⁸

The statutes adopted by most states granted the commissioner power to deny issuance unless the securities and the terms of the offering met the "fair, just and equitable" standard. Administrators were allowed wide discretion in evaluating the economic risk involved in investments in order to determine whether the security was sound enough to be offered within the jurisdiction.³⁹ Several states today still retain this kind of securities statute.⁴⁰

The newer state laws, patterned after *Uniform Securities Act* section 306,⁴¹ have abandoned the "fair, just and equitable" language for specific criteria which the commissioner should consider

³⁴ J. MOFSKY, *BLUE SKY RESTRICTIONS ON NEW BUSINESS PROMOTIONS* 10 (1971).

³⁵ Bateman, *State Securities Registration: An Unresolved Dilemma and a Suggestion for the Federal Securities Code*, 27 Sw. L.J. 759, 765 (1973).

³⁶ Kan. Laws 212, ch. 133, § 5 (1911) (repealed 1915), *quoted in* Bateman, *supra* note 35, at 765.

³⁷ Within two years, 23 states had adopted securities regulation statutes, most of which were modeled on the Kansas act. Bateman, *supra* note 35, at 766.

³⁸ J. MOFSKY, *supra* note 34, at 12.

³⁹ Such factors as assets of the issuer and expected earnings were considered by the Administrator in passing on the merits of the security. *Id.* at 15.

⁴⁰ For example, the Florida law provides:

If upon examination of any application the department shall find . . . that the terms of sale of such securities would be fair, just and equitable, and that the enterprise or business of the issuer is not based upon unsound business principles, it shall record the registration

FLA. STAT. § 517.09(7) (1972), 1 BLUE SKY L. REP. ¶ 13,109 (1973).

⁴¹ The *Uniform Securities Act* was first adopted by Hawaii, Kansas, and Virginia in 1957.

when passing on the merits of a security. These criteria include amounts of underwriters' and sellers' discounts or commissions, and amounts or kinds of options. These jurisdictions still retain general antifraud provisions.⁴²

Many states that have adopted the *Uniform Securities Act* have promulgated rules and regulations under section 306 that set specific percentage limits on underwriters' compensation,⁴³ promoters' profits,⁴⁴ and options and warrants.⁴⁵ Further requirements are often imposed by commission rule. For example, some states require that the promoters put up a certain percentage of the amount that is to be raised in the offering,⁴⁶ that stock received by promoters for less than the offering price be held in escrow to prevent sale until the company is making a profit,⁴⁷ and that the proceeds from the sale of the securities be impounded until, and refunded unless, a specified amount has been raised.⁴⁸ These rules considerably reduce administrative discretion and give promoters a clear idea of the requirements which their offering must meet to satisfy the merit standard of a particular jurisdiction. Uniform regulations adopted in many states facilitate multi-state offerings. The Midwest Securities Commissioners Association, for example, with twenty-two members, has adopted model rules.⁴⁹

In contrast to the merit standard, federal securities regulation is based on a disclosure philosophy. An issuer making an offering

⁴² UNIFORM SECURITIES ACT § 306.

⁴³ Underwriters' compensation is generally limited to a certain percentage of the total offering price. Hueni, *Application of Merit Requirements in State Securities Regulation*, 15 WAYNE L. REV. 1417, 1423-34 (1969).

⁴⁴ Limits are placed on the percentage of cheap stock that can be held as promotional shares and on the resulting dilution of publicly held stock. *Id.* at 1423-28.

⁴⁵ The amount of options and warrants outstanding is limited to a certain percentage of outstanding securities; the duration cannot exceed a fixed number of years; and the exercise price must at least equal the public offering price plus a step-up of a certain amount per year. *Id.* at 1428-34.

⁴⁶ *Id.* at 1421-23.

⁴⁷ *Id.* at 1434-40.

⁴⁸ *Id.* at 1440-44.

⁴⁹ However, Mofsky contends that these guidelines give only a "misleading sense of specificity and objectivity" because the determination of the set percentages in the rules is dependent on variables that are in turn dependent on administrative discretion. For example, the maximum amount of promotional stock permitted to the organizers of a new company is based on the percentage of stock outstanding after completion of the public offering. But valuation of the shares is dependent on a large number of variables, some of which are subject to administrative discretion. "[U]nless such explicit rules cover every possible dimension of evaluation of securities, true discretion will be left with the administrators in some regard." J. MOFSKY, *supra* note 34, at 16. It seems clear, however, that these rules significantly reduce administrative discretion.

of securities to the public must disclose all material information⁵⁰ regarding the security. Failure to do so subjects the issuer, its directors, officers, and others, to civil liability.⁵¹ The S.E.C. passes on the sufficiency of disclosure in a prospectus that must be filed with the Commission and distributed to investors. The S.E.C. can delay a public offering until the prospectus is adequate, but has no authority to deny an issuer the right to make a public offering on the basis of the merits of the security, so long as there is full disclosure.

The earliest drafts of the 1933 Act introduced in Congress were patterned on state merit systems, rather than on the disclosure philosophy.⁵² But ultimately the disclosure philosophy prevailed, because many believed that a federal merit standard would be unworkable, that the existence of such a standard would imply approval of the security by the federal government, and that disclosure would best protect the interests of investors and promoters alike.⁵³

The disclosure philosophy is based on the idea that an investor can make his own decision as to the merits of a security as long as all material information is revealed to him. However, as many scholars point out, a prospectus probably is understandable by few of the even fewer investors who bother to read it.⁵⁴ Others believe that disclosure works through a "filtration" process—the experts read the prospectus and advise investors on whether or not to buy the security.⁵⁵

Section 4(2) of the 1933 Act and Rule 146 operate in the context of the disclosure philosophy. They exempt from the registration requirements of the 1933 Act transactions in which disclosure through a prospectus is not necessary to protect the investors involved. As the Supreme Court stated in *S.E.C. v. Ralston Purina Co.*,⁵⁶ interpreting what is now section 4(2) before the adoption of Rule 146:

⁵⁰ "Material information" has been defined as "matters which . . . an investor needs to know before he can make an intelligent, informed decision whether or not to buy the security." *Escott v. Barchris Construction Corp.*, 283 F. Supp. 643, 681 (S.D.N.Y. 1968). It has been further described as "a fact which if it had been correctly stated or disclosed would have deterred or tended to deter the average prudent investor from purchasing the securities in question." *Matter of Charles A. Howard*, 1 S.E.C. 6, 8 (1934), quoted in *Barchris, supra*, at 681.

⁵¹ Section 11 of the 1933 Act, 15 U.S.C. § 77k (1970).

⁵² Bateman, *supra* note 35, at 767-68.

⁵³ *Id.*

⁵⁴ See D. RATNER, *supra* note 8, at 106-19.

⁵⁵ *Id.*

⁵⁶ 346 U.S. 119 (1953) (holding that an offering by a corporation to its employees may be a public offering).

The design of the [1933 Act] is to protect investors by promoting full disclosure of information thought necessary to informed investment decisions. The natural way to interpret the private offering exemption is in light of the statutory purpose. Since exempt transactions are those as to which "there is no practical need for . . . [the 1933] Act's application," the applicability of [§ 4(2)] should turn on whether the particular class of persons affected need the protection of the Act. An offering to those who are shown to be able to fend for themselves is a transaction "not involving any public offering."⁵⁷

II

THE MAJORITY RULE

Forty-three states have not adopted an exemption coextensive with Rule 146, and do not have a provision in their blue sky laws exempting all offerings exempt under section 4(2). At one time, Pennsylvania had coextensive exemption with section four of the Federal Act.⁵⁸ In 1973, however, that state adopted a new section on exempt transactions,⁵⁹ deleting the provision providing for coextensive exemption.⁶⁰ The new private offering exemption limits sales to twenty-five persons,⁶¹ making coordination with Rule 146 possible by restricting the number of purchasers to twenty-five or by selling to at least ten persons in another state (rather than limiting the number of offerees). However, the Pennsylvania exemption, unlike Rule 146, prohibits the use of underwriters or dealers, as does the *Uniform Securities Act*.⁶²

The Securities Commissioners of California and Wisconsin have even gone so far as to issue releases stating that exemption under Rule 146 does not automatically exempt transactions under their blue sky laws. They have also refused to adopt an exemption coextensive with Rule 146.⁶³ The reason given by the California Commissioner

⁵⁷ *Id.* at 124-25 (footnote omitted).

⁵⁸ PA. STAT. ANN. tit. 70, § 43(c)(e) (1965) (repealed 1973).

⁵⁹ PA. STAT. ANN. tit. 70, § 1-203 (Supp. 1975-76), 3 BLUE SKY L. REP. ¶ 41,113 (1972).

⁶⁰ However, securities exempt under § 4(2) of the 1933 Act are exempt from the subsequent reporting requirements of the Pennsylvania Securities Commission. Reg. §§ 2.7.11(a), (b), 3 BLUE SKY L. REP. ¶ 41,302 (1975). The rationale for an exemption from subsequent reporting, but not from registration, is not clear.

⁶¹ PA. STAT. ANN. tit. 70, § 1-203(d) (Supp. 1975-76), 3 BLUE SKY L. REP. ¶ 41,113 (1972).

⁶² *Id.*

⁶³ Corporate Securities Newsletter, Nov. 1974, California Department of Corporations, 1 BLUE SKY L. REP. ¶ 8708 (1974); Monthly Bulletin, Nov. 1974, Wisconsin Office of Commissioner of Securities, 3 BLUE SKY L. REP. ¶ 52,764 (1974).

for not adopting a coextensive exemption is the "fundamental differences between a disclosure standard [in the federal securities laws] and a fair, just and equitable standard [in the California securities laws]."⁶⁴ Furthermore, under the California standard, "review is not limited to determining the impact of the transaction solely upon prospective purchasers of the securities but in many instances upon other investors of the issuer."⁶⁵ The Wisconsin Commissioner also based his objection to an exemption coextensive with Rule 146 on the difference between a disclosure and a merit standard.⁶⁶

III

THE MINORITY RULE

In contrast, several states, even before the S.E.C. adopted Rule 146, exempted all securities or transactions that are exempt under the 1933 Act other than by the intrastate offering exemption.⁶⁷ New Jersey, for example, makes it unlawful to offer or sell any security not registered under its blue sky law unless "the security or transaction . . . is exempted from . . . the registration requirements of the Securities Act of 1933 and the rules and regulations thereunder"⁶⁸ New York and Nevada require registration of intrastate offerings only.⁶⁹ Both states exempt transactions of an intrastate offering that would be exempt under the 1933 Act other than by the intrastate exemption.⁷⁰ The new North Carolina blue

⁶⁴ 1 BLUE SKY L. REP. ¶ 8708, at 4656.

⁶⁵ *Id.*

⁶⁶ Wisconsin Monthly Bulletin, *supra* note 63.

⁶⁷ The intrastate offering exemption, § 3(a)(11) of the 1933 Act, provides that "[a]ny security which is a part of an issue offered and sold only to persons resident within a single State or Territory, where the issuer of such security is a person resident and doing business within or, if a corporation, incorporated by and doing business within, such State or Territory" is exempt from registration. 15 U.S.C. § 77c(a)(11) (1970). Its purpose is to place upon the state the responsibility of regulating offerings taking place completely within its borders.

⁶⁸ N.J. STAT. ANN. § 49:3-60(b) (1970), 2 BLUE SKY L. REP. ¶ 33,114 (1974).

⁶⁹ The New York blue sky law defines an intrastate offering as "an issue offered and sold only to persons resident within this state." The statute is one of the few state laws which requires disclosure only. N.Y. GEN. BUS. LAW § 359-ff(1) (McKinney Supp. 1968), 2 BLUE SKY L. REP. ¶ 35,116-1 (1968). The Nevada securities law defines an intrastate offering as "every attempt or offer to dispose of, or solicitation of an offer to buy, a security . . . made solely within this state to 35 persons or more." NEV. REV. STAT. § 90.075 (1973), 2 BLUE SKY L. REP. ¶ 31,110 (1975). The Nevada law has a merit standard. NEV. REV. STAT. § 90.155 (1973), 2 BLUE SKY L. REP. ¶ 31,121 (1975).

⁷⁰ N.Y. GEN. BUS. LAW. § 359-ff(5) (McKinney Supp. 1968), 2 BLUE SKY L. REP. ¶ 35,116-1 (1968); NEV. REV. STAT. § 90.075 (1973), 2 BLUE SKY L. REP. ¶ 31,110 (1975).

sky law, effective April 1, 1975, grants the Administrator rulemaking power to exempt any transaction that is exempt from federal registration under section 4(2).⁷¹

Maryland and Delaware, in response to adoption of Rule 146, have already created exemptions coextensive with the federal rule. Any offering in these two states that meets the requirements of Rule 146 is automatically exempt from registration under the state blue sky laws.⁷² The new regulation provides:

Any offering that complies with the conditions required to be met under SEC Rule 146 . . . will be deemed to be in compliance with this rule, upon receipt by the [Maryland Division of Securities or the Delaware Department of Justice] of the issuer's representation . . . that the issuer has complied with the conditions of SEC Rule 146.⁷³

Prior to the adoption of this new regulation, both states only had private offering exemptions based on *Uniform Securities Act* section 402(b)(9).⁷⁴ The exemption was limited to twenty-five *offerees*,⁷⁵ but did not prohibit sales through underwriters and dealers, as does the *Uniform Securities Act*.⁷⁶ Under the new Maryland-Delaware rule, an issuer may *sell* to thirty-five persons within the state, and can rely with more certainty on the exemption.⁷⁷ As the Commissioners stated:

Adoption of the New Rule will result in uniform private offering requirements under federal law and the law of two neighboring states, Maryland and Delaware. The Commissioners hope that their mutual adoption of the New Rule will serve to encourage other states to consider the importance of uniformity in the private offering area.⁷⁸

⁷¹ N.C. GEN. STAT. § 78A-17(9) (1975), 2 BLUE SKY L. REP. ¶ 36,172 (1975). However, the Administrator has not yet adopted such a rule.

⁷² Maryland and Delaware jointly announced this change. Delaware Securities Release, issued Oct. 24, 1974, 1 BLUE SKY L. REP. ¶ 11,653 (1975).

⁷³ 1 BLUE SKY L. REP. ¶ 11,622, at 7511-2 to 7511-3 (1974).

⁷⁴ DEL. CODE ANN. tit. 6, § 7309(b)(9) (1975), 1 BLUE SKY L. REP. ¶ 11,109 (1973); MD. ANN. CODE art. 32A, § 26(b)(9) (1957), 2 BLUE SKY L. REP. ¶ 23,314 (1968), now in Md. Securities Act § 11-602(9), 2 BLUE SKY L. REP. ¶ 23,372 (1975).

⁷⁵ However, both states adopted rules that somewhat modified the offeree test into a more workable purchaser standard. Delaware Securities Release, *supra* note 72.

⁷⁶ UNIFORM SECURITIES ACT § 402(b)(9)(B). See note 33 *supra*.

⁷⁷ The Commissioners, in adopting the new rule, recognized "that Rule 146 is an improvement, in a number of respects, over their states' current rules." One of the most important improvements is increased certainty. Delaware Securities Release, *supra* note 72, at 7524.

⁷⁸ *Id.* at 7526. Hawaii recently amended its blue sky law to provide an exemption for "[a]ny offer or sale not involving a public offering within the meaning of Rule 146 . . . or any successor rule." HAWAII REV. STAT. § 485-6(15), 1 BLUE SKY L. REP. ¶ 14,705 (1975). This

In addition to the section on "Exemption by Coordination," the Maryland-Delaware rule creates a private offering exemption based on some, but not all, of Rule 146.⁷⁹ For example, both the Maryland-Delaware and federal rules limit the number of purchasers of the security to thirty-five.⁸⁰ However, the Maryland-Delaware rule excludes from the computation of this number "any related person of the issuer,"⁸¹ defined as "the officers and directors, or general and managing partners, of the issuer, their spouses, parents, brothers, sisters and children."⁸² Rule 146, on the other hand, has no comparable exclusion. Thus, the Maryland-Delaware rule is more liberal in this respect: an offering could be

provision is simply added to the section on exempt transactions, which still includes the previous private offering exemption based on UNIFORM SECURITIES ACT § 402(b)(9). HAWAII REV. STAT. § 485-6(9) (1968), 1 BLUE SKY L. REP. ¶ 14,705 (1975). This old private offering exemption, in contrast to the new coextensive rule, is limited to 25 *offerees* and prohibits payment of commissions.

Arkansas has provided some degree of coextensive exemption with Rule 146 by adopting a private offering exemption similar to the federal rule. ARK. STAT. § 67-1248(b)(14), 1 BLUE SKY L. REP. ¶ 7114 (1975). It does not, however, expressly exempt any offering that meets the requirements of Rule 146, as do the Maryland, Delaware, and Hawaii provisions. As under Rule 146, the Arkansas law provides that 35 persons may purchase the security, all buyers must purchase for investment, and all offerees and purchasers must meet certain sophistication requirements. There is no access requirement as in Rule 146, so an offering could be exempt from Arkansas registration, but not from federal requirements. Furthermore, commissions may be allowed by rule of the Commissioner.

However, variations from the sophistication requirements of Rule 146 may create some difficulties in coordinating the Arkansas statute and the federal rule. The Arkansas exemption provides that the issuer shall have reasonable grounds to believe and shall believe that each person to whom the offer is made is a "sophisticated investor." In contrast, Rule 146 allows an offer to be made to persons who either have knowledge or experience in financial matters *or* are able to bear the economic risk of the investment. *See* text accompanying note 88 *infra*. Unless an investor able to bear the economic risk is considered "sophisticated" for purposes of the Arkansas statute, the Arkansas exemption is somewhat more restrictive. It is also unclear whether there is any difference between a "sophisticated investor" and one with knowledge and experience in financial matters.

Under the Arkansas statute, the issuer prior to sale must reasonably believe both that the offeree has knowledge and experience in financial matters and that he is able to bear the economic risk of investment, or that the offeree and offeree representative together have this knowledge and the offeree is able to bear the economic risk. Under Rule 146, it is sufficient upon sale that the purchaser alone have knowledge and experience, without any requirement that he be capable of bearing the economic risk. *See* text accompanying notes 89-90 *infra*. The reason for these variations in the Arkansas statute is not apparent. These minor differences needlessly make coordination with Rule 146 more difficult.

⁷⁹ The Maryland-Delaware rule omits certain requirements of Rule 146 but does not in any way conflict with the federal rule. Rules of the Delaware Securities Commissioner, Rule 9(b)(9)(I), 1 BLUE SKY L. REP. ¶ 11,622 (1975).

⁸⁰ *Id.* Rule 9(b)(9)(I) § (e)(1). Rule 146(g)(1).

⁸¹ Rule 9(b)(9)(I), *supra* note 79, at § (e)(2)(i)(e).

⁸² *Id.* Rule 9(b)(9)(I) § (a)(5).

exempt in Maryland and Delaware but not exempt under Rule 146.⁸³

As noted above, all offerees in an offering under Rule 146 must either have access to or be furnished with the same kind of information that is required in a registration statement.⁸⁴ The most significant difference between the new Maryland-Delaware rule and Rule 146 is that the state rule does not have this access requirement. If an offering is dependent on Rule 146 for its exemption from federal registration, this difference would, of course, be meaningless—the offering would have to meet the access requirement for federal exemption. If, however, the offering is exempt from federal registration because it is an intrastate offering under section 3(a)(11)⁸⁵ of the 1933 Act, the difference is important. The resulting “intrastate private offering” exemption—exempt from federal registration under the intrastate exemption and from state registration under the Maryland-Delaware rule—has no access requirement.⁸⁶

IV

THE CASE FOR COEXTENSIVE EXEMPTION

As previously stated, the California and Wisconsin Commissioners have refused to adopt an exemption coextensive with Rule 146 because of the “fundamental differences” between a merit standard and the disclosure philosophy.⁸⁷ However, the access and sophistication requirements of Rule 146 make it clear that the persons to whom sales will be made under the Rule are not in need of state blue sky law registration or merit standard protection.

The sophistication requirement provides that the issuer shall have reasonable grounds to believe and shall believe that each person to whom he *offers* the security either (1) has “such knowledge and experience in financial and business matters that he is

⁸³ This could also occur in a multi-state offering in which there are more than 35 purchasers throughout the country, but 35 or fewer in Maryland or Delaware.

⁸⁴ See text accompanying note 22 *supra* and text accompanying notes 93-96 *infra*.

⁸⁵ See note 67 *supra*. See also SEC Rule 147, SEC Securities Act Release No. 5450 (Jan. 7, 1974), 1 CCH FED. SEC. L. REP. ¶ 2340 (1974).

⁸⁶ In place of the access requirement, the Maryland-Delaware rule substitutes “an undertaking to provide (upon request) such information concerning the issuer as would be required to be provided in accordance with . . . the anti-fraud provisions of the [Maryland and Delaware] Acts.” Delaware Securities Release, *supra* note 72, at 7525. The antifraud provisions are Delaware Securities Act § 7303, 1 BLUE SKY L. REP. ¶ 11,103 (1973), and Maryland Securities Act § 11-301, 2 BLUE SKY L. REP. ¶ 23,321 (1975).

⁸⁷ See notes 63-66 and accompanying text *supra*.

capable of evaluating the merits and risks of the prospective investment" or (2) is a person "who is able to bear the economic risk of the investment."⁸⁸ Further, the issuer shall have reasonable grounds to believe and shall believe that each person to whom he sells the security either (1) has the requisite knowledge and experience, or (2) is able to bear the economic risk of the investment and, together with his "Offeree Representative,"⁸⁹ has the requisite knowledge and experience.⁹⁰

The different standards for offer and sale allow the issuer to offer to an individual who may be financially unsophisticated but who is rich enough to bear the risk of the investment. However, the offeree must be represented by someone with knowledge and experience before any sale is made. The issuer may both offer and sell to an investor without an offeree representative so long as the investor has knowledge and experience in financial and business matters.

The sophistication required of purchasers is not just the general sophistication of, for example, a doctor or a lawyer. Rule 146 requires "sophistication in financial and business matters" to the extent of being "capable of evaluating the merits and risks of the prospective investment." Existing case law prior to Rule 146 makes clear that the burden of proving sophistication is on the person seeking the exemption,⁹¹ and indicates that this requirement will not be easily satisfied.⁹²

⁸⁸ Rule 146(d)(1). This section of Rule 146 reintroduces some uncertainty into a private offering under the Rule. The requisite knowledge and experience will have to be defined in case law. See note 92 and accompanying text *infra*.

⁸⁹ The definition of Offeree Representative is found in Rule 146(a)(1). This person must have "such knowledge and experience in financial and business matters that he, either alone, or together with other offeree representatives or the offeree, is capable of evaluating the merits and risks of the prospective investment." Rule 146(a)(1)(ii). An offeree representative could be the investor's own stockbroker, or an individual or firm hired by the issuer to advise prospective investors as to the security. In the latter case, any compensation received by the offeree representative from the issuer and any material relationship between the representative and issuer must be revealed. Rule 146(a)(1)(iv).

⁹⁰ Rule 146(d)(2).

⁹¹ *SEC v. Ralston Purina Co.*, 346 U.S. 119 (1953); *Andrews v. Blue*, 489 F.2d 367 (10th Cir. 1973); *SEC v. Continental Tobacco Co. of South Carolina*, 463 F.2d 137 (5th Cir. 1972); *Lively v. Hirschfield*, 440 F.2d 631 (10th Cir. 1971). SEC Securities Act Release No. 5487 (April 23, 1974), 1 CCH FED. SEC. L. REP. ¶ 2710, at 2907-11, makes clear that Rule 146 "does not shift [the] burden [of proof]. In addition, it should be pointed out that the burden of proof applies with respect to each offeree and not just to the purchasers . . ."

⁹² See *Lively v. Hirschfield*, 440 F.2d 631 (10th Cir. 1971), in which an airline pilot "who had considerable business experience and who had purchased stocks from time to time" was not considered to be sophisticated. The standard that the court applied was whether the offerees were "persons of unusual business experience and skill." 440 F.2d at 632-33.

Rule 146 also mandates that each offeree either (1) have access⁹³ to the same kind of information that would be contained in a registration statement⁹⁴ or (2) be furnished with this information.⁹⁵ Further, each offeree or his representative must have the opportunity to ask questions of and to obtain additional information from the issuer to the extent it can be provided without unreasonable expense.⁹⁶ The sophisticated offeree or the offeree and his representative will therefore be entitled to more information than would be disclosed either by federal or state registration.⁹⁷

Perhaps the California and Wisconsin Commissioners are concerned about secondary trading, *i.e.*, investors will be able to purchase the security, without the protection of the sophistication and access requirements, from persons who bought in the original offering. Rule 146 prevents this. The issuer, under the federal rule, must determine before each sale that the purchaser is buying for investment rather than for resale, and must take steps⁹⁸ to make resale by the original buyer virtually impossible (unless the security is registered or transferred under an exemption).⁹⁹

The California Commissioner's second ground for denying coextensive exemption is that California uses its securities laws to protect existing shareholders of a corporation, as well as those to

In *Andrews v. Blue*, 489 F.2d 367 (10th Cir. 1973), the court found that the plaintiff, "although . . . a sophisticated real estate investor . . . was a babe in the woods when it came to stocks." 489 F.2d at 373 n.3. See also Annot., 6 A.L.R. Fed. 536 (1971) (discussion of what constitutes a public offering within the meaning of § 4(2)).

⁹³ "Access," in contrast to being "furnished with information," is the ability of the offeree to get information because of his position with respect to the issuer. The offeree could be in a position affording access because of employment with the issuer, a family relationship, or the economic bargaining power of a large-scale investor. See Rule 146(e) nt.

⁹⁴ Rule 146(e)(1)(i).

⁹⁵ Rule 146(e)(1)(ii).

⁹⁶ Rule 146(e)(2). It would, however, be extremely risky for an issuer to rely on unreasonable expense as a defense for not providing information. See *Alberg & Lybecker*, *supra* note 9, at 641.

⁹⁷ Although the language for the degree of sophistication required of an offeree representative and of the investor is identical, it seems reasonable that more expertise will be required of an offeree representative. See *Alberg & Lybecker*, *supra* note 9, at 637. In order to minimize the risk that an investor will be found to be insufficiently sophisticated, a prudent issuer should require all investors, no matter what their degree of sophistication, to retain an offeree representative. (An offeree representative could represent more than one or even all offerees, thus reducing expenses.) Investor protection greater than this would be hard to imagine.

⁹⁸ These steps include placing a legend indicating restrictions on transferability on the share certificates, issuing stop transfer instructions to the transfer agent, and obtaining a signed agreement by the purchaser that he will not sell the securities without registration under the 1933 Act or exemption therefrom.

⁹⁹ Rule 146(h).

whom the security is offered.¹⁰⁰ Other states use the general corporation laws dealing with fiduciary duties to protect minority shareholders from unfair securities transactions.¹⁰¹ This is usually an adequate remedy, assuming the minority shareholders are aware of a breach of fiduciary duty involved in an offering. The California procedure simply adds an administrative agency that keeps watch for minority shareholders. When an offering must be federally registered because it is public, this added protection is beneficial. But when an offering is exempt from federal registration under section 4(2) or Rule 146, this added protection to minority shareholders is not worth the extra cost of registration, which must be borne by *all* the shareholders. And there is certainly no reason for this rule when a corporation is being formed—there are then no existing stockholders to protect. In any case, other states which do not use their securities laws to protect present stockholders should not follow California's lead.

Because of the added expense involved in requiring both federal and state registration, and the belief that state merit standards are unnecessary, there has been an ongoing debate for many years over whether federal securities registration should preempt state regulation.¹⁰² Without getting into the merits of this argument, which have been adequately developed elsewhere,¹⁰³ it seems clear that states could alleviate a small part of the problem that has brought forth the calls for federal preemption by adopting coextensive exemption with the federal statute when there is no need to provide additional protection for investors.

CONCLUSION

The argument for coextensive exemption is different from the debate over whether the merit standard or disclosure philosophy is

¹⁰⁰ See note 65 and accompanying text *supra*.

¹⁰¹ There has also been a tremendous growth in recent years in the number of suits brought by existing shareholders under federal antifraud provisions, especially Rule 10b-5 of the Securities Exchange Act of 1934, 17 C.F.R. § 240.10b-5 (1974). This trend can be expected to continue as the purchaser-seller requirement of Rule 10b-5 is further liberalized, thus providing for greater protection of existing shareholders when state laws are inadequate.

¹⁰² Section 18 of the 1933 Act expressly provides that the Act does not preempt state securities regulation. 15 U.S.C. § 77r (1970).

¹⁰³ See J. MOFSKY, *supra* note 34, at 84-86; Bateman, *supra* note 35; Bloomenthal, *Blue Sky Regulation and The Theory of Overkill*, 15 WAYNE L. REV. 1447 (1969); Hueni, *supra* note 43; Millonzi, *Concurrent Regulation of Interstate Securities Issues: The Need for Congressional Reappraisal*, 49 VA. L. REV. 1483 (1963); Mofsky, *State Securities Regulation and New Promotions: A Case History*, 15 WAYNE L. REV. 1401 (1969).

preferable. That controversy is not relevant to the question of coextensive exemption because Rule 146 protects investors by requiring *sophistication*, as well as access. Because every purchaser under Rule 146 must be sophisticated, such an offering does not have to be substantively regulated by a state.

The objections of the California and Wisconsin Commissioners therefore appear to be totally unfounded.¹⁰⁴ Purchasers in an offering under Rule 146 are more than adequately protected. They do not need the protection afforded by state disclosure requirements because they either have access to or are furnished with more information than they would receive in a state registration statement. They do not need the protection of state merit standards because either they or their representatives are capable of passing on the merits of a security.¹⁰⁵ Requiring state registration of an offering that is exempt under Rule 146 involves needless expense to the issuer, which is, of course, paid for by those who purchase the security, the very people supposedly protected. Determination by the commissioner's office that the security is not sound will deprive investors, equally capable of making their own determination, of any chance to invest in it.

The Maryland-Delaware rule is preferable to the California-Wisconsin approach since it provides full protection to investors at lower cost. States should, therefore, adopt exemptions coextensive with Rule 146 to simplify the needlessly burdensome procedures for a private offering.¹⁰⁶

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¹⁰⁴ The refusal of the Wisconsin Commissioner to adopt coextensive exemption is especially groundless. Wisconsin has a private offering exemption based on UNIFORM SECURITIES ACT § 402(b)(9). See notes 29-33 and accompanying text *supra* and Appendix. The Wisconsin exemption, as compared to Rule 146, merely allows less offers and sales and prohibits use of dealers or underwriters. This does not afford nearly as much protection as the sophistication and access requirements of Rule 146.

¹⁰⁵ Although the degree of sophistication required of an offeree is not completely clear (see note 92 and accompanying text *supra*), it is reasonable to assume that the offeree will have to be at least smart enough to perform the same simple numerical calculations that the state commissioner's office often makes in passing on the merits of the security. See notes 43-49 and accompanying text *supra*. The investor can then make his own evaluation of the security, taking these, as well as many other factors, into consideration.

¹⁰⁶ At least two states are currently moving in this direction. A provision granting the Colorado Securities Commissioner authority to adopt an exemption for offerings exempt under Rule 146 was recently passed by the Colorado legislature. COLO. REV. STAT. ANN. § 11-51-114(2)(i), 1 BLUE SKY L. REP. ¶ 9114 (1975). The Colorado Division of Securities is now circulating proposed Rule 8.16, intended to implement the new legislation. Letter from Stanley R. Hays, Securities Commissioner, State of Colo., to author, Aug. 28, 1975. However, rather than merely providing for coextensive exemption with Rule 146, the proposed rule imposes additional conditions on the issuer. Among these are a minimum

initial cash investment requirement and a requirement that each offeree have a certain income or net worth. These additional conditions, however, are not burdensome.

The California Senate is presently considering Senate Bill No. 377 that would adopt, for purposes of California's securities act, the definition of a private offering found in Rule 146. BNA SEC. REG. L. REP., No. 290, Feb. 19, 1975, at Y-1. The proposal as it now stands, however, would merely adopt this definition for purposes of CAL. CORP. CODE § 25102(a) (West Supp. 1975), 1 BLUE SKY L. REP. ¶ 8133 (1974). That section only exempts offers (not sales) not involving any public offering. Securities offered under § 25102(a) must be qualified before sale takes place. Therefore, even if the amendment passes, an offering that meets the requirements of Rule 146 could be offered without registration, but would still have to be qualified before sale.

APPENDIX

SUMMARY OF STATE PRIVATE OFFERING EXEMPTIONS

This Appendix summarizes the provisions in each state dealing with private offering exemptions. It is complete through the July 23, 1975 CCH BLUE SKY L. REP. [hereinafter cited as CCH]. An asterisk (*) preceding the name of the state indicates that the jurisdiction has adopted the *Uniform Securities Act* as promulgated or in slightly modified form. See note 25 and accompanying text *supra*.

UNIFORM SECURITIES ACT § 402(b)(9) [hereinafter cited as USA § 402(b)(9)] has been adopted by many states, with and without modification. It provides as follows:

(b) The following transactions are exempted from sections 301 and 403 [which require registration and filing]:

(9) any transaction pursuant to an offer directed by the offeror to not more than ten persons (other than those designated in paragraph (8) [institutional investors]) in this state during any period of twelve consecutive months, whether or not the offeror or any of the offerees is then present in this state, if (A) the seller reasonably believes that all the buyers in this state (other than those designated in paragraph (8)) are purchasing for investment, and (B) no commission or other remuneration is paid or given directly or indirectly for soliciting any prospective buyer in this state (other than those designated in paragraph (8)); but the (Administrator) may by rule or order as to any security or transaction or any type of security or transaction, withdraw or further condition this exemption, or increase or decrease the number of offerees permitted, or waive the conditions in Clauses (A) and (B) with or without the substitution of a limitation on remuneration.

* ALABAMA. Alabama has adopted USA § 402(b)(9) with the following changes: (1) the seller must reasonably believe that institutional investors (excluded in computing the ten offerees) are purchasing for investment; and (2) commissions may not be paid for soliciting institutional investors. ALA. CODE tit. 53, § 38(i) (Supp. 1973), 1 CCH ¶ 5211 (1974).

* ALASKA. Alaska has adopted USA § 402(b)(9) with the following changes: (1) the offer may be made to not more than 20 persons; (2) the seller must reasonably believe that institutional investors (excluded in computing the 20 offerees) are purchasing for investment; (3) commissions may not be paid for soliciting institutional investors; and (4) the last clause of § 402(b)(9), which grants the Administrator wide discretion to modify the requirements of private offerings by rule or order, is omitted. This clause was deleted by a 1972 amendment. ALASKA STAT. § 45.55.140(b)(5) (1962), 1 CCH ¶ 6014 (1972). See also Alas. Administrative Code Regs., tit. 3, § 08.310, 1 CCH ¶ 6047 (1972) (contains notice requirements of a private offering under § 45.55.140(b)(5)).

ARIZONA. Arizona exempts "[t]ransactions by an issuer not involving any public offering." ARIZ. REV. STAT. ANN. § 44-1844(1) (Supp. 1974-75), 1 CCH ¶ 6134 (1974). Any offering within the state to not more than ten persons is exempt under § 44-1844(1) by Order No. S-2 of the Corporation Commissioner, 1 CCH ¶ 6652 (1972). Arizona also exempts sales to institutional investors. ARIZ. REV. STAT. ANN. §§ 44-1844(8) (Supp. 1974-75), 1 CCH ¶ 6134 (1974). Certification of financial statements is required. See note 28 and accompanying text *supra*.

* ARKANSAS. Arkansas has adopted USA § 402(b)(9) with the following changes: (1) the offer may be made to not more than 25 persons; (2) the seller must reasonably believe that institutional investors (excluded in computing the 25 offerees) are purchasing for investment; and (3) commissions may not be paid for soliciting institutional investors. ARK. STAT. ANN. § 67-1248(b)(9) (1947), 1 CCH ¶ 7114 (1975). See also Ark. Securities Rules, Rule 8(K), 1 CCH ¶ 7608 (1974) (sets forth proof of exemption requirements under the private offering exemp-

tion and interpretations of various provisions of the exemption; prohibits large disparities between consideration paid by insiders and that paid by offerees). Furthermore, Arkansas has adopted an additional private offering exemption similar to Rule 146. ARK. STAT. ANN. § 67-1248(b)(14), 1 CCH ¶ 7114 (1975). There are, however, some differences that may make coordination difficult. See note 78 *supra*. This new private offering may not be utilized if an exemption has been claimed or filed pursuant to the other private offering exemption, § 67-1248(b)(9), within 12 months. Only a registered agent may offer or sell the securities. See also note 32 and accompanying text *supra*. Certification of financial statements is required. See note 28 *supra*.

CALIFORNIA. California does not have a generally applicable private offering exemption. It does, however, exempt offers or sales of voting common stock by a corporation incorporated in any state if, immediately after the proposed sale, there will be only one class of stock of the issuer outstanding which is owned beneficially by no more than ten persons. CAL. CORP. CODE § 25102(h) (West Supp. 1975), 1 CCH ¶ 8133 (1974). However, the exemption may only be used: (1) in the takeover of an existing business by a newly formed corporation; (2) upon initial organization of the issuer; (3) in sales solely to existing shareholders; or (4) where there will be only one shareholder. Payment of commissions is prohibited. See also notes 63-66, 106 and accompanying text *supra*; Calif. Regs., subch. 2, art. 1, § 260.102.4, 1 CCH ¶ 8614 (1974) (definition of "one class of stock"); § 260.102.5, 1 CCH ¶ 8614 (1974) (definition of "beneficial ownership"); § 260.102.6, 1 CCH ¶ 8614 (1974) (share transfer restrictions); § 260.102.7, 1 CCH ¶ 8614 (1974) (definition of "selling expenses"); and § 260.102.8-9, 1 CCH ¶ 8614 (1974) (notice requirements). Sales to institutional investors are exempt. CAL. CORP. CODE § 25102(i) (West Supp. 1975), 1 CCH ¶ 8133 (1974); Calif. Regs., subch. 2, art. 1, § 260.102.10, 1 CCH ¶ 8614 (1974). See also CAL. CORP. CODE §§ 25102(a), (e), (g) (West Supp. 1974). Certification of financial statements is required. See note 28 *supra*.

* **COLORADO.** Colorado has adopted the *Uniform Securities Act*; however, the private offering exemption is substantially different from USA § 402(b)(9). It exempts "[a]ny transaction in this state not involving any public offering." These are defined as offerings in which (1) the seller reasonably believes that the securities are purchased for investment; and (2) each offeree, by reason of his knowledge about the affairs of the issuer or otherwise, does not require the information which would be set forth in a registration statement. COLO. REV. STAT. ANN. § 11-51-114(2)(i) (1973), 1 CCH ¶ 9114 (1975). There is no absolute limit on the number of offerees or purchasers (however, see Colo. Regs., Rule 8.15, 1 CCH ¶ 9709 (1975), which makes this a factor in determining the availability of the exemption); but in contrast to § 402(b)(9) each offeree must have the requisite knowledge. See also Colo. Regs., Rule 8.15, 1 CCH ¶ 9709 (1975) (listing the factors to be considered in determining whether the private offering exemption is available); Rule 4.62, 1 CCH ¶ 9705 (1975) (guidelines for what constitutes sufficient knowledge of the business of the issuer on the part of the offeree). Colo. Regs., Administrative Order of Colo. Division of Securities, Dec. 13, 1974, 1 CCH ¶ 9724 (1975), makes clear that exemption under Rule 146 does not automatically make the Colorado private offering exemption available. This release also sets forth specific criteria to be considered in determining whether the exemption is available. BNA SEC. REG. L. REP. ADVANCE SHEET, 5-7-75, No. 301, A-21 (1975), reports that a bill giving the commissioner authority to adopt an exemption coextensive with Rule 146 was introduced into the legislature. The provision was passed as part of Senate Bill 284, effective July 1, 1975. See note 106 *supra*. Sales to institutional investors are exempt. COLO. REV. STAT. ANN. § 11-51-114(2)(h), 1 CCH ¶ 9114 (1975). Certification of financial statements is required. See note 28 *supra*.

CONNECTICUT. Under Connecticut law, securities do not have to be registered. However, unless the security or transaction is exempt, only a registered broker, dealer, or salesman may sell the securities. Therefore, securities may be sold either through a registered broker, dealer, or salesman (with no further registration requirements) or directly by the issuer in a private offering "within the meaning of § 4(2) of the [1933 Act]." CONN. GEN. STAT. ANN. § 36-322(a)(E) (1958), 1 CCH ¶ 10,103 (1973). Presumably, compliance with Rule 146 would qualify as a private offering.

DELAWARE. Delaware has adopted USA § 402(b)(9), with the following changes: (1) the

offer may be made to not more than 25 persons; and (2) payment of commissions is not prohibited. DEL. CODE ANN. tit. 6, § 7309(b)(9) (1974), 1 CCH ¶ 11,109 (1973). See note 33 and accompanying text *supra*. Furthermore, Delaware has adopted a private offering exemption coextensive with Rule 146. Rules of the Del. Securities Commissioner, 1 CCH ¶ 11,653 (1974), ¶ 11,622 (1975). See notes 72-86 and accompanying text *supra*. Compliance with either the *Uniform Securities Act* provision or Rule 146 exempts the offering.

* DISTRICT OF COLUMBIA. The District of Columbia does not require registration of offerings, but does require the licensing of brokers and agents who make offerings for an issuer. The law exempts from the definition of "agent" any person effecting exempt transactions. D.C. CODE ANN. § 2-2401(a)(2) (1973), 1 CCH ¶ 12,101 (1972). Section 2-2401(f)(5) exempts any transaction pursuant to an offering to not more than 25 persons in the District. (The seller must reasonably believe that all buyers are purchasing for investment. Payment of commissions is allowed. See note 33 and accompanying text *supra*.) This means that a corporation may itself sell the securities if the offering qualifies as private. If it does not qualify, the corporation must hire a licensed broker to make the offering, but no further registration is required.

FLORIDA. In Florida, sales by a corporation to not more than 20 persons during any period of 12 consecutive months are exempt. FLA. STAT. ANN. § 517.06(11) (Supp. 1975-76), 1 CCH ¶ 13,106 (1973). See note 32 and accompanying text *supra*. Sales to institutional investors, exempted by § 517.06(5), are not included in computing the 20 persons. Each purchaser, prior to consummation of the sale, must be furnished with "adequate information" concerning (1) the true financial condition of the issuer; (2) its business operations; and (3) the use of the proceeds from the sale. No public solicitation or advertisement may be used; commissions may be paid only to registered dealers and salesmen; buyers must purchase for investment only. Certification of financial statements is required. See note 28 *supra*.

GEORGIA. In Georgia, sales by an issuer to not more than 15 persons during a 12 month period are exempt. GA. CODE ANN. § 97-109(m) (Supp. 1974), 1 CCH ¶ 14,129 (1975). See note 32 and accompanying text *supra*. The 15 persons does not include purchasers (1) acquiring securities in transactions exempt from registration (sales to institutions are exempt under § 97-109(g)); (2) acquiring exempt securities; and (3) acquiring securities registered under the Georgia act. No public advertising may be used. Each purchaser must execute a statement that he is purchasing the securities for investment and the share certificates must indicate restrictions on transferability. Certification of financial statements is required. See note 28 *supra*.

* HAWAII. Hawaii has adopted USA § 402(b)(9) with the following changes: (1) the offer may be made to not more than 25 persons; (2) the seller must reasonably believe that institutional investors (excluded in computing the 25 offerees) are purchasing for investment; (3) commissions may not be paid for soliciting institutional investors; and (4) the last clause of § 402(b)(9), which grants the Administrator wide discretion to modify the requirements of private offerings by rule or order, is omitted. HAWAII REV. STAT. § 485-6(9) (1968), 1 CCH ¶ 14,705 (1975). Furthermore, Hawaii has adopted a private offering exemption coextensive with Rule 146. HAWAII REV. STAT. § 485-6(15), 1 CCH ¶ 14,705 (1975). See note 78 *supra*. Compliance with either the *Uniform Securities Act* provision or Rule 146 exempts the offering. Certification of financial statements is required. See note 28 *supra*.

* IDAHO. Idaho has adopted UNIFORM SECURITIES ACT § 402(b)(9), with the following changes: (1) the seller must reasonably believe that institutional investors (excluded in computing the ten offerees) are purchasing for investment; (2) commissions may not be paid for soliciting institutional investors; and (3) the last clause of § 402(b)(9), which grants the Administrator wide discretion to modify the requirements of private offerings by rule or order, is omitted. IDAHO CODE § 30-1435(8) (1967), 1 CCH ¶ 15,135 (1975). See also Idaho Regs. § 30-1435(8), 1 CCH ¶ 15,623 (1975) (restricts use of the exemption to issuers only). Certification of financial statements is required. See note 28 *supra*.

ILLINOIS. In Illinois sales by an issuer (or controlling person) to not more than 25 persons during a 12 month period are exempt so long as offers are not made to more than 50 persons during the 12 month period. ILL. ANN. STAT. ch. 121½, § 137.4(G) (Smith-Hurd Supp. 1975-76), 1 CCH ¶ 16,204 (1975). The 25 or 50 persons does not include: (1) purchasers or offerees of exempt securities; (2) purchasers or offerees of securities in transactions exempt

under this section (sales to institutions are exempt under subsection 4(C)); and (3) purchasers or offerees of registered securities. Commissions are limited to 15% of the initial offering price. Certification of financial statements is required. See note 28 *supra*.

* INDIANA. In Indiana, sales by an issuer to not more than 35 persons are exempt. IND. ANN. STAT. § 23-2-1-2(b)(10), 1 CCH ¶ 17,102 (1975). See note 32 and accompanying text *supra*. Excluded from this number are persons buying securities in other exempt transactions under this same section (sales to institutional investors are exempt under § 23-2-1-2(b)(8)) or purchasers of registered securities. No general advertising may be used, and each purchaser must make written representation that he is acquiring the securities for investment. If any commissions are paid, each offeree must be furnished with an offering statement setting forth all material facts, and the commissioner may disallow the exemption within five business days. Certification of financial statements is required. See note 28 *supra*.

IOWA. In Iowa, sales by an issuer to not more than 35 persons during a 12 month period are exempt. IOWA CODE § 502.5(15) (1971), 2 CCH ¶ 18,105 (1974). See note 32 and accompanying text *supra*. Sales to institutional investors, exempt under § 502.5(5), are not included in computing the 35 persons. No commissions are allowed, except as permitted by order of the commissioner.

* KANSAS. Kansas exempts any offer or sale by a Kansas corporation to not more than 15 persons within a 12 month period. KAN. STAT. ANN. § 17-1262(n), 2 CCH ¶ 19,111 (1975). The offeror must believe that all the purchasers are buying for investment, and no commissions may be paid. The commissioner is granted the power to withdraw or impose conditions on the use of the exemption. There is no private offering exemption applicable to foreign corporations. Certification of financial statements is required. See note 28 *supra*.

* KENTUCKY. Kentucky has adopted USA § 402(b)(9) with the following change: the seller must reasonably believe that institutional investors (excluded in computing the ten offerees) are purchasing for investment. KY. REV. STAT. ANN. § 292.410(9) (Baldwin 1974), 2 CCH ¶ 20,111 (1972). Certification of financial statements is required. See note 28 *supra*.

LOUISIANA. Louisiana's private offering exemption is similar to USA § 402(b)(9), although there are some differences: (1) the offer may be made to not more than 25 persons; (2) purchasers must represent that they are buying for investment, rather than the seller having to reasonably believe so; (3) commissions are not prohibited; and (4) institutional investors (excluded in computing the 25 offerees) must represent that they are purchasing for investment. LA. REV. STAT. ANN. § 51:705(12) (Supp. 1975), 2 CCH ¶ 21,105 (1974).

MAINE. Maine exempts any sale of securities of a domestic corporation if before and after sale there are not more than ten security holders. ME. REV. STAT. ANN. tit. 32, § 874(9) (Supp. 1973), 2 CCH ¶ 22,124 (1975). See note 31 and accompanying text *supra*. Institutional investors, to which sales are exempt under § 874(8), are not included in determining the number of security holders. *Id.* § 874(8). However, the information required in a registration statement is much less than is required by the *Uniform Securities Act*, and is not much more than the notice required to be filed with the commissioner for a private offering in some *Uniform Securities Act* jurisdictions. ME. REV. STAT. ANN. tit. 32, § 871 (Supp. 1973), 2 CCH ¶ 22,121 (1974).

* MARYLAND. Maryland has adopted USA § 402(b)(9) with the following changes: (1) the offer may be made to not more than 25 persons; and (2) payment of commissions is not prohibited. See note 33 and accompanying text *supra*. MD. ANN. CODE § 11-602(9), 2 CCH ¶ 23,372 (1975). Furthermore, Maryland has adopted a private offering exemption coextensive with Rule 146. Md. Regs., Rule S-7 (Rule 2.02.03.07), 2 CCH ¶ 23,615 (1975). See also 1 CCH ¶ 11,653 (1974). See notes 72-86 and accompanying text *supra*. Compliance with either the *Uniform Securities Act* provision (§ 11-602(9)) or Rule 146 exempts the offering. Certification of financial statements is required. See note 28 *supra*.

* MASSACHUSETTS. Massachusetts has adopted USA § 402(b)(9) with the following changes: (1) the offer may be made to not more than 25 persons; and (2) commissions may be paid so long as the seller files a notice with the commissioner five days prior to the offer, and the commissioner does not disallow the exemption within those five days. See note 33

and accompanying text *supra*. MASS. GEN. LAWS ANN. ch. 110A, § 402(b)(9) (1975), 2 CCH ¶ 24,232 (1972). *See also* Mass. Regs., Rule VI, A(3), 2 CCH ¶ 24,606 (1975) (must keep records upon filing of notice); Rule VI, H, 2 CCH ¶ 24,606 (1975) (notice requirements).

* MICHIGAN. Michigan has adopted USA § 402(b)(9) with the following change: the offer may be made to not more than 15 persons (reduced to ten in the regulations below). MICH. STAT. ANN. § 19.776(402)(b)(9) (1975), 2 CCH ¶ 25,314 (1975). Mich. Securities Rules, R 451.802.3, 2 CCH ¶ 25,657 (1971) provides that only offers by an issuer to not more than 15 persons within 12 months of incorporation, or ten persons within any other 12 month period may be exempt under § 19.776(402)(b)(9).

* MINNESOTA. Under Minnesota law, sales by an issuer to not more than 25 persons during a 12 month period are exempt. MINN. STAT. ANN. § 80A.15(2)(h) (Supp. 1975), 2 CCH ¶ 26,175 (1974). *See note 32 and accompanying text supra*. This number includes persons to whom sales have been made under the isolated sales exemption, § 80A.15(2)(a) (which in Minnesota may be used by the issuer), and under the exemption for issuance of securities of a corporation newly incorporated in Minnesota, § 80A.15(2)(k), but does not include sales to institutional investors, which are exempt under § 80A.15(2)(g). Reasonable and customary commissions may be paid to licensed brokers. The issuer must reasonably believe that the buyers are purchasing for investment. The commissioner is granted broad discretion to modify the exemption.

MISSISSIPPI. Mississippi exempts an offer or sale of securities of a "domestic investment company" (including corporations, MISS. CODE ANN. § 75-71-5(a) (1972), 2 CCH ¶ 27,102 (1974)), if after an offer or sale there are not more than ten shareholders. *Id.* § 75-71-53(9), 2 CCH ¶ 27,125-1. *See note 31 and accompanying text supra*. Buyers must purchase for investment and no commissions may be paid. When the amount of the offering or authorized capital of the company exceeds \$50,000, affidavits of investment intent must be filed with the Secretary of State. Section 75-71-53(7) exempts sales to institutional investors, but § 75-71-53(9) does not explicitly exclude institutions from the computation of the ten shareholders. Certification of financial statements is required. *See note 28 supra*.

* MISSOURI. Missouri exempts 15 transactions (sales) by an issuer during a 12 month period. MO. REV. STAT. § 409.402(b)(10) (1969), 2 CCH ¶ 28,164 (1967). *See note 32 and accompanying text supra*. Sales to institutional investors, exempt under § 409.402(b)(8), are not included in computing the 15 transactions. No commissions may be paid. The issuer must reasonably believe that the buyer is purchasing for investment and the buyer must so represent in writing. Missouri also exempts transactions by an issuer if the number of shareholders of record and beneficial security holders known to the issuer after the sale does not exceed 25. *Id.* § 409.402(b)(9), 2 CCH ¶ 28,164 (1967). *See note 31 and accompanying text supra*. No commissions may be paid. Transactions exempt under § 402(b)(9) are not included in computing the 15 transactions under § 402(b)(10). Rule IX(N) of the Mo. Commissioner of Securities, 2 CCH ¶ 28,609 (1974), sets forth the notification requirements under § 402(b)(10). Notification includes filing of uncertified financial statements.

* MONTANA. Montana has adopted USA § 402(b)(9) with the following changes: (1) commissions may be paid to a registered broker-dealer if the offering is registered under the 1933 Act (*see note 33 and accompanying text supra*); (2) commissions may not be paid for soliciting institutional investors (excluded in computing the ten offerees) unless the offering is registered under the 1933 Act; (3) the seller must reasonably believe that institutional investors are purchasing for investment; and (4) the last clause of § 402(b)(9), which grants the Administrator wide discretion to modify the requirements of private offerings by rule or order, is omitted. MONT. REV. CODES ANN. § 15-2014(8) (Supp. 1974), 2 CCH ¶ 29,214 (1973).

* NEBRASKA. Nebraska has adopted USA § 402(b)(9) with the following changes: (1) commissions may be paid to registered broker-dealers (*see note 33 and accompanying text supra*); (2) commissions may not be paid, except to registered broker-dealers, for soliciting institutional investors (excluded in computing the ten offerees); (3) the seller must reasonably believe that institutional investors are purchasing for investment; and (4) the last clause of § 402(b)(9), which grants the Administrator wide discretion to modify the requirements of private offerings by rule or order, is omitted. NEB. REV. STAT. § 8-1111(9) (1974), 2 CCH ¶ 30,111 (1974).

* NEVADA. Nevada requires registration of intrastate offerings only. NEV. REV. STAT. § 90.140(1) (1973), 2 CCH ¶ 31,118 (1975). Transactions of an intrastate offering that are registered or exempt under the 1933 Act, other than by the intrastate offering exemption, are exempt. NEV. REV. STAT. § 90.075, 2 CCH ¶ 31,110 (1975). See notes 69-70 and accompanying text *supra*. An intrastate offering is defined as "every attempt or offer to dispose of, or solicitation of an offer to buy, a security . . . made solely within this state to 35 persons or more." *Id.* § 90.075, 2 CCH ¶ 31,110 (1975). Thus, if the offering is not interstate and is not exempt under § 90.075 because it is not registered or exempt under the 1933 Act, a private offering exemption is in effect created by the definition of "public intrastate offering." This would be an offering to 35 or fewer offerees. No time period over which these offers are aggregated is specified; thus traditional integration tests would probably be used to determine what constitutes a single offering. Commissions may be paid. See note 33 and accompanying text *supra*. Certification of financial statements is required. See note 28 *supra*.

NEW HAMPSHIRE. In New Hampshire, no securities (except those legal for investment by savings banks) may be offered or sold until approved by the commissioner. For securities to qualify for sale, such information as the commissioner may require must be submitted to him. N.H. REV. STAT. ANN. § 421:28 (Supp. 1973), 2 CCH ¶ 32,128 (1974). There is no private offering exemption.

* NEW JERSEY. New Jersey requires registration of intrastate offerings only. N.J. STAT. ANN. § 49:3-60 (1970), 2 CCH ¶ 33,114 (1974). See also *Data Access Systems, Inc. v. State*, 63 N.J. 158, 305 A.2d 427 (1973) (holding that the Division of Consumer Affairs has no authority to review the merits of a federally registered securities offering). New Jersey has adopted USA § 402(b)(9) with the following changes: (1) the seller must reasonably believe that institutional investors (excluded in computing the ten offerees) are purchasing for investment; and (2) commissions may not be paid for soliciting institutional investors. N.J. STAT. ANN. § 49:3-50(b)(9) (1970), 2 CCH ¶ 33,104 (1974). Any security or transaction registered under the 1933 Act or exempt from registration under the 1933 Act other than by the intrastate exemption is also exempt. *Id.* §§ 49:3-60(b), (c), 2 CCH ¶ 33,114. See note 68 and accompanying text *supra*. See also N.J. Regs. subch. 7, § 13:47A-9.13, 2 CCH ¶ 33,693 (1975) (denies exemption for an intrastate "private offering made to sophisticated investors" other than institutional investors).

* NEW MEXICO. New Mexico exempts the sale of a domestic corporation's securities if the number of security holders both before and after the sale does not exceed 25. N.M. STAT. ANN. § 48-18-22(J) (1966), 2 CCH ¶ 34,132 (1973). See note 31 and accompanying text *supra*. The seller must reasonably believe that all buyers are purchasing for investment, and no commissions may be paid. Offers and sales to institutional investors are exempt. *Id.* § 48-18-22(H), 2 CCH ¶ 34,132. Other than the exemption for sales to institutions, there is no private offering exemption applicable to foreign corporations. Certification of financial statements is required. See note 28 *supra*.

NEW YORK. New York only requires the filing of a prospectus for intrastate offerings. N.Y. GEN. BUS. LAW § 359-ff(1) (McKinney Supp. 1974), 2 CCH ¶ 35,116-1 (1968). Securities of an intrastate offering that are registered or exempt under the 1933 Act, other than by the intrastate offering exemption, or sold in transactions exempt under the 1933 Act, are exempt under New York law. *Id.* §§ 359-ff(5)(a), (b), 2 CCH ¶ 35,116-1. See notes 69-70 and accompanying text *supra*. Offerings by an issuer that has securities registered under the Securities and Exchange Act of 1934 are exempt. *Id.* § 359-ff(5)(c), 2 CCH ¶ 35,116-1. N.Y. GEN. BUS. LAW § 359-f(2)(d) (McKinney 1968), 2 CCH ¶ 35,116 (1967) provides that the attorney general may, upon application, exempt securities sold in a limited offering to not more than 40 persons, or in certain cases to more than 40 persons. This provision is applicable to intrastate offerings by § 359-ff(7). N.Y. Regs., tit. 13, ch. IV, part 80, § 80.9, 2 CCH ¶ 35,621 (1969), provides for automatic exemption without application for offerings made to fewer than ten persons. See also *id.* § 80.6 (offering to sophisticated investors may, upon application to the attorney general, be exempted); Policy Statement 100, N.Y. Bureau of Securities and Public Financing, Mar. 31, 1975, 2 CCH ¶ 35,651 (1975) (upon application to the attorney general, exemption coextensive with Rule 146 available for real estate syndication offerings).

* NORTH CAROLINA. North Carolina has adopted USA § 402(b)(9) with the following

changes: (1) the offer may be made to not more than 25 persons; (2) institutional investors are included in computing the 25 offerees and the seller must reasonably believe that they are purchasing for investment; and (3) commissions are not prohibited. *See* note 33 and accompanying text *supra*. N.C. GEN. STAT. § 78A-17(9), 2 CCH ¶ 36,172 (1975). The same section of the new North Carolina Blue Sky Law, effective April 1, 1975, also provides that the Administrator may by rule exempt any transaction that is exempt from federal registration under § 4(2) of the 1933 Act. *Id.* § 78A-17(9), 2 CCH ¶ 36,172 (1975). However, the Administrator has not yet promulgated such a rule.

NORTH DAKOTA. North Dakota's private offering exemption is the same as USA § 402(b)(9), except that there is the further provision that the issuer must obtain the approval of the commissioner in writing before use of the exemption. N.D. CENT. CODE § 10-04-06(9) (Supp. 1973), 2 CCH ¶ 37,106 (1973). Certification of financial statements is required. *See* note 28 *supra*.

OHIO. Ohio law provides that the sale of securities by any corporation incorporated in or qualified to do business in Ohio may be registered by description when the total number of shareholders does not, and will not after such sale, exceed 15. OHIO REV. CODE ANN. § 1707.06(A)(2) (1964), 2 CCH ¶ 38,106 (1966); § 1707.07, 2 CCH ¶ 38,107 (1966). *See* note 31 and accompanying text *supra*. Registration by description is no more burdensome than notification under many state laws; no financial statements are required. *Id.* § 1707.08, 2 CCH ¶ 38,108 (1966). *See also* Ohio Regs., 2 CCH ¶ 38,768 (1975) (treatment of joint ownership of shares in determining number of shareholders); 2 CCH ¶ 38,769 (1975) (limitations on nonpublic offerings at book value).

* **OKLAHOMA.** Oklahoma exempts sales to not more than 25 persons in the state during a 12 month period. OKLA. STAT. ANN. tit. 71, § 401(b)(9) (Supp. 1974-75), 2 CCH ¶ 39,151 (1974). *See* note 32 and accompanying text *supra*. Sales to institutional investors, exempt under OKLA. STAT. ANN. tit. 71, § 401(b)(8), are not included in computing the 25 persons. No commissions may be paid. No public advertising is allowed and the seller must reasonably believe that all buyers are purchasing for investment. *See also* Admin. Rules of the Okla. Sec. Comm., Rule R-401(b)(9), 2 CCH ¶ 39,611 (1970) (requiring written request for exemption in certain cases); 2 CCH ¶ 39,704 (1971) (general discussion of exemptions). Certification of financial statements is required. *See* note 28 *supra*.

* **OREGON.** Oregon exempts sales to not more than ten persons within the state during any 12 consecutive months. ORE. REV. STAT. § 59.035(12) (1974), 3 CCH ¶ 40,204 (1974). *See* note 32 and accompanying text *supra*. Sales to institutional investors are exempt under § 59.035(4), but are not expressly excluded from computation of the ten persons under § 59.035(12). Certification of financial statements for offerings over a certain monetary amount is required. *See* note 28 and accompanying text *supra*.

PENNSYLVANIA. Pennsylvania exempts sales by an issuer to not more than 25 persons in the state during a 12 month period. PA. STAT. ANN. tit. 70, § 1-203(d) (Supp. 1974-75), 3 CCH ¶ 41,113 (1972). *See* note 32 and accompanying text *supra*. Purchasers of registered securities, exempt securities, or securities bought in exempt transactions (§ 1-203(c) exempts sales to institutions) are not included in computing the 25 persons. No commissions may be paid; no public advertising may be used; and the issuer must obtain a written agreement from each purchaser stating that the purchaser will not sell the security for 12 months. *See also* notes 58-62 and accompanying text *supra*; Securities Commission Regs., 64 Pa. Code ch. 1, § 2.3.4.1, 3 CCH ¶ 41,302 (1975) (notice requirements and rules concerning private offerings); Commission Interpretations, 3 CCH ¶ 41,359 (1973), 3 CCH ¶ 41,362 (1974) (clarifying the private offering exemption). Certification of financial statements is required. *See* note 28 *supra*.

* **PUERTO RICO.** Puerto Rico has adopted USA § 402(b)(9) with no changes. P.R. LAWS ANN. tit. 10, § 882(b)(9) (Supp. 1974), 3 CCH ¶ 41,714 (1968). Certification of financial statements is required. *See* note 28 *supra*.

RHODE ISLAND. Rhode Island has no private offering exemption except for sales to institutional investors, which are exempt under R.I. GEN. LAWS ANN. § 7-11-9(b) (Supp. 1974), 3 CCH ¶ 42,109 (1975).

* **SOUTH CAROLINA.** South Carolina has adopted USA § 402(b)(9) with the following

change: the offer may be made to not more than 25 offerees. S.C. CODE ANN. § 62-52(9) (Supp. 1974), 3 CCH ¶ 43,223 (1972). Certification of financial statements is required. *See* note 28 *supra*.

SOUTH DAKOTA. South Dakota exempts sales by an issuer, having its principal office in South Dakota, to not more than 25 persons in the state during a 12 month period. S.D. COMPILED LAWS ANN. § 47-31-86.1 (Interim Supp. 1975), 3 CCH ¶ 44,186A (1975). *See* note 32 and accompanying text *supra*. Sales to institutional investors, exempt under S.D. COMPILED LAWS ANN. § 47-31-88 (Supp. 1975), 3 CCH ¶ 44,188 (1975), are not included in computing the 25 persons. Reasonable and customary commissions may be paid to a licensed broker; no public advertising is permitted; and the issuer must reasonably believe that purchasers are buying for investment. Certification of financial statements is required. *See* note 28 *supra*.

TENNESSEE. Tennessee exempts the sale of securities in "isolated transactions" by an issuer to not more than 15 persons. TENN. CODE ANN. § 48-1632(H) (1964), 3 CCH ¶ 45,132 (1967). *See* note 32 and accompanying text *supra*. Tenn. Reg. XVII, 3 CCH ¶ 45,648 (1967), makes clear that the 15 purchasers are counted over the total life of the corporation and include out-of-state purchasers. Under § 48-1632(H), underwriting or payment of commissions is prohibited, and the buyers must purchase for investment. Section 48-1632(H) also provides that sales to institutional investors (exempt under § 48-1632(E)) or any other transactions exempt under other provisions of § 48-1632 are not included in computing the 15 persons. *See also* Tenn. Reg. XVII, 3 CCH ¶ 45,648 (1967) (clarifying "investment intent"); Tenn. Reg. XXV, 3 CCH ¶ 45,655 (1967) (progress report filing requirements). Certification of financial statements is required. *See* note 28 *supra*.

TEXAS. Texas exempts sales by an issuer to not more than 15 persons within a 12 month period. TEX. REV. CIV. STAT. § 581-5(1)(c) (1964), 3 CCH ¶ 46,105 (1975). *See* note 32 and accompanying text *supra*. The 15 persons does not include (1) purchasers of securities in transactions exempt under other provisions of § 5 (§ 5(H) exempts sales to institutional investors); (2) purchasers of exempt securities; and (3) purchasers of registered securities. The buyers must purchase for their own accounts and not for distribution. *Id.* § 581-5(1)(c). Furthermore, § 581-5(1)(a) exempts the sale by an issuer of any security so long as there are not more than 35 shareholders after the sale. *See* note 31 and accompanying text *supra*. Such sales are not included in computing the 15 persons for purposes of § 581-5(1)(c). *See also* Tex. Administrative Interpretations, 3 CCH ¶¶ 46,639, 46,650 (1975) (containing interpretations of various terms used in private offering exemptions). Certification of financial statements is required. *See* note 28 *supra*.

* **UTAH.** Utah does not have a private offering exemption except for pre-organization certificates or subscriptions, UTAH CODE ANN. § 61-1-14(2)(i), 3 CCH ¶ 47,314 (1967), and for sales to institutional investors, *id.* § 61-1-14(2)(h). Certification of financial statements is required. *See* note 28 *supra*.

VERMONT. Vermont exempts offers by an issuer to not more than 25 persons, so long as the number of holders of all the issuer's securities, after the sale, does not exceed 25. VT. STAT. ANN. tit. 9, § 4204(10) (Supp. 1975), 3 CCH ¶ 48,104 (1972). *See* note 31 and accompanying text *supra*. The issuer must be incorporated or organized in Vermont. The 25 persons does not include institutional investors. Sales to institutions are exempt under § 4204(5). No commissions may be paid, and no advertising may be published or circulated. The commissioner may by rule or order waive the prohibition on commissions.

* **VIRGINIA.** Virginia exempts the sale of securities by an issuer if, after the sale, it has no more than 30 shareholders. VA. CODE ANN. § 13.1-514(b)(8) (Supp. 1975), 3 CCH ¶ 49,214 (1975). *See* note 31 and accompanying text *supra*. The securities may not be offered to the general public by advertisement or solicitation.

* **WASHINGTON.** Washington exempts sales by an issuer to not more than ten persons within 12 months, if the aggregate amount of sales does not exceed \$100,000. WASH. REV. CODE ANN. § 21.20.320(9), 3 CCH ¶ 50,133 (1975). *See* note 32 and accompanying text *supra*. The seller must reasonably believe that all buyers are purchasing for investment; no public or general solicitation may be utilized; and no commissions may be paid. The issuer must file a

notice of the terms of the offering, and the director may disallow the exemption within 10 business days. Certification of financial statements is required. *See* note 28 *supra*.

* WEST VIRGINIA. West Virginia has adopted USA § 402(b)(9) with no changes. W. VA. CODE ANN. § 32-4-402(b)(9) (1975), 3 CCH ¶ 51,182 (1974).

* WISCONSIN. Wisconsin has adopted USA § 402(b)(9) with the following change: the seller must reasonably believe that institutional investors (excluded in computing the ten offerees) are purchasing for investment. WIS. STAT. ANN. § 551.23(11) (1974), 3 CCH ¶ 52,213 (1974). In addition, § 551.23(10) exempts any offer or sale of securities by a corporation having its principal office in Wisconsin if after sale there are no more than 15 security holders (exclusive of institutional investors). *See* note 31 and accompanying text *supra*. Under § (10) payment of commissions is prohibited unless waived by rule of the commissioner (*see infra*), and advertising may be used only if permitted by the commissioner. Offers made under § (10) are included in computing the ten offers allowed under § (11). *See also* notes 66, 104 and accompanying text *supra*; Wis. Adm. Code § SEC 2.02(6)(c), 3 CCH ¶ 52,602 (1975) (payment of reasonable commissions to a licensed broker-dealer is allowed for offerings under §§ (10) or (11)); *id.* § 2.02(6) (filing requirements and restrictions for private offering listed); BNA SEC. REG. L. REP. No. 302, May 14, 1975, at A-17 (definition of reasonable commission); 3 CCH ¶ 52,730 (1970) (interpretation of "investment intent"); 3 CCH ¶ 52,759 (1974) (interpretation of "advertising"); and 3 CCH ¶ 52,760 (1974) (clarification of time of sale for purposes of filing requirement).

* WYOMING. Wyoming has adopted USA § 402(b)(9) with the following change: the offer may be made to not more than 15 persons. WYO. STAT. ANN. § 17-117.14(b)(9) (1965), 3 CCH ¶ 53,114 (1975). Certification of financial statements is required. *See* note 28 *supra*.