

CSI - Ohio

The Common Sense Initiative

Business Impact Analysis

Agency Name: Securities /Commerce

Regulation/Package Title: 2014 Five Year Review / 123437

Rule Number(s): 1301:6-1-02; 1301:6-3-03; 1301:6-3-04.1; 1301:6-3-06; 1301:6-3-08;
1301:6-3-09; 1301:6-3-09.1; 1303:6-3-09.3; 1301:6-3-12; 1303:6-3-13

Date: October 14, 2014

Rule Type:

New X 5-Year Review
X Amended Rescinded

The Common Sense Initiative was established by Executive Order 2011-01K and placed within the Office of the Lieutenant Governor. Under the CSI Initiative, agencies should balance the critical objectives of all regulations with the costs of compliance by the regulated parties. Agencies should promote transparency, consistency, predictability, and flexibility in regulatory activities. Agencies should prioritize compliance over punishment, and to that end, should utilize plain language in the development of regulations.

This rule

Regulatory Intent

1. Please briefly describe the draft regulation in plain language.

Please include the key provisions of the regulation as well as any proposed amendments

These rules deal with the registration of securities – how registration of securities may be accomplished and what exemptions are available.

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- 1301:6-3-02: This rule describes how securities listed on exchanges, according to RC 1707.02(E), shall be treated as exempt. It also describes how governmental obligations and commercial paper may be exempt according to RC 1707.02 (B) and (G). The Division proposes to simplify the rule and bring it into alignment with federal law by deleting names of specific national exchanges and substituting references to the (federal) Securities Act of 1933.
- 1301:6-3-03: This rule corresponds with RC 1707.03. Certain terms used in the statute are defined; provides directions and explanations of how to claim an exemption according to certain provisions of the statute as set forth; and additional exempt transactions are recognized. The Division proposes to revise the rule by deleting references to RC 1707.03(X) because the consent to service of process requirement was eliminated for that filing by legislation.
- 1301:6-3-04.1: Ohio securities law (RC 1707.041) prohibits the making of a control bid for the securities of an Ohio subject company pursuant to a tender offer or request or invitation for tenders unless the offeror files certain information with the Division of Securities, the subject company, and any other offeror. To provide "[c]omplete information on the organization and operations of the offeror," the offeror is required to file, among other things, financial statements for the current period and for the three most recent annual accounting periods. Under the act, these financial statements are not required if the Division by rule (1) determines that they are not material or (2) permits the filing of financial statements for less than the three most recent annual accounting periods. The rule describes when financial statements may not be required or may be incorporated by reference. The rule also states the conditions when the Division shall terminate a filing and permit the reinstatement of a control bid. No change is proposed.
- 1301:6-3-06: This rule describes the procedures to register a securities offering pursuant to RC 1707.06, including the forms to use, the materials that must accompany the filing and the requirements of an offering circular and registration. Section (B) requires the Division to promptly examine every registration by description filed. No change is proposed.
- 1301:6-3-08: This rule sets out the length of time an issuer may sell their securities pursuant to a registration by description filing – 16 months. The rule also allows the Division to permit an extended period up to 24 months. At the conclusion of the effectiveness period, the issuer may file another registration by description with updated information. No change is proposed.

- 1301:6-3-09: The rule concerns registrations by qualification. The rule sets out the alternate forms that may be used, some of the materials to be submitted and the period of effectiveness. The rule requires notice of any material changes in the information submitted and certain terms dealing with escrow requirements. No change is proposed.
- 1301:6-3-09.1: This rule concerns registration by coordination, pursuant to RC 1707.091. The rule sets forth the type of documents required to comply with the type of registration, permits the Division to reduce the time period the issuer must wait to go effective and permits the issuer to notify the Division by telephone of effectiveness with the SEC. A stop order, comparable to the federal power, is to provide a mechanism to halt a proposed offer if it would defraud or deceive. Once the issuer has taken corrective action, the rule sets out a procedure to terminate the stop order, retroactively to allow sales to continue. No change is proposed.
- 1301:6-3-09.3: The rule permits, but does not require, electronic filings for certain types of files and provides how electronic filing may be made. No change is proposed.
- 1301:6-3-12: This rule provides that documents otherwise confidential pursuant to RC 1707.12 may be shared with FINRA (formerly the NASD), the self-regulatory organization for broker-dealers to allow for concomitant regulation of securities salespersons and firms. No change is proposed.
- 1301:6-3-13: This is a ministerial rule which allows the Division to withdraw a file or a notice filing that has been on file for a year without becoming effective. No change is proposed.

2. Please list the Ohio statute authorizing the Agency to adopt this regulation.

Ohio Revised Code Section 1707.20. In addition, the rules amplify, respectively, RC 1707.02, 1707.03, 1707.041, 1707.06, 1707.08, 1707.09, 1707.091, 1707.12 and 1707.13.

3. Does the regulation implement a federal requirement?

No.

Is the proposed regulation being adopted or amended to enable the state to obtain or maintain approval to administer and enforce a federal law or to participate in a federal program?

If yes, please briefly explain the source and substance of the federal requirement.

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No.

4. If the regulation includes provisions not specifically required by the federal government, please explain the rationale for exceeding the federal requirement.

Not applicable

**5. What is the public purpose for this regulation (i.e., why does the Agency feel that there needs to be any regulation in this area at all)? **

The purposes of the rules are:

- 1301:6-3-02 – This rule adds to the exempt securities in RC 1707.02 and clarifies other exemptions, recognizing those situations where investor protection is provided by other means.
- 1301:6-3-03 – The purpose of this rule is to provide clarity and uniformity by defining terms used, and requirements, in the exemptions contained in RC 1707.03. The rule also provides further exemptions to issuers where protection of the public is not required because the issuer is already regulated, the type of offer is governed by, or exempt from, federal law or the purchasers do not need protection or are not in Ohio.
- 1301:6-3-04.1 – RC 1707.04.1 permits the Division to create a rule to further the purposes of the control bid statute (in 1707.041(A)(1)(g)) by delineating when financial statements would not be required to be filed. The two conditions are both situations where the public and the Division may already obtain the financial information from the SEC’s electronic files and the where the public isn’t relying on the financial condition of the offeror (an all-cash deal). These two conditions provide sufficient investor protection and fair treatment of the target Ohio company.
- 1301:6-3-06 – This rule provides the specific direction to issuers how a registration by description may be carried out. The rule describes what an offering circular must contain and when an offering circular is required. The \$250,000 threshold is intended to be a compromise between investor protection and the cost and burden of preparing and distributing an offering circular, although many issuers will prepare and distribute an offering circular to protect themselves against civil liability. The prohibitions and restrictions are intended to both provide investor protection, to promote more efficient securities markets and to provide a level field for the issuers. The obligation to advise the Division of any material changes is intended to insure that investors are given up to date information.
- 1301:6-3-08 –After a certain period of time, the materials, including financial statements, supplied to offerees are stale and the issuer should refresh by refiling. In addition, early investors would otherwise have their money tied up indefinitely until

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sufficient proceeds are raised. The 16 months effective period has existed since at least 1983 and allows the issuer the 12 months under federal Reg A as well as four additional months to complete the offering. The rule allows the Division to grant additional time for the issuer to sell pursuant to the registration “for good cause” so that issuers trying to coordinate with other offerings or other jurisdictions may be accommodated provided there is no perceived harm to investors.

- 1301:6-3-09 – The rule provides specific directions regarding the filing of a registration by qualification under RC 1707.09. The period of effectiveness runs for 13 months to allow the filing to be coordinated with any other jurisdiction so the issuer may be able to refile, if they choose, with all the states simultaneously. The obligation to advise the Division of any material changes is intended to insure that investors are given up to date information. The forms to be filed are in the alternative, allowing the issuer to coordinate filings with other jurisdictions, and the Form U-7 is the “Small Company Offering Registration Form” that was developed to simplify the filing requirements for small businesses (adopted in 1999).
- 1301:6-3-09.1 – Registration by coordination is established for registrations that are simultaneously filed with the SEC. The materials requested are comparable to the materials required to be filed with the SEC. The procedures, and the capability of the Division to shorten the waiting time for effectiveness all relate to trying to allow the issuer to coordinate the registrations going effective in multiple jurisdictions, including federally, allowing sales to take place simultaneously. The purpose is to provide speed and efficiency to allow the Ohio filings to be coordinated with the same registration going effective with the SEC.
- 1301:6-3-09.3 – In an effort to simplify the process of certain filings, the Division permits, but does not require, that those filings may be made electronically. There are two types of notice filings that, with the external systems presently available, lend themselves to electronic filings: Reg. D and mutual funds. Both are simplistic and there is a vendor that will handle the filings and payments for these types of filings. To provide for unintentional errors due to the transmission process, the rule allows for corrective actions without penalties.
- 1301:6-3-12 – In order to share otherwise confidential documents with other regulators, specifically the self-regulatory organization for dealers, the rule allows FINRA access. The sharing of information allows more accurate and efficient regulation.
- 1301:6-3-13 – Although it happens infrequently, there are registration filings that, for various reasons, do not go forward and never become effective (e.g.: the deal falls through; the issuer cannot or will not respond to comments by the Division or the

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SEC) and are abandoned by the issuer. To avoid having an increasing number of files that are not either becoming effective or being withdrawn by the issuer, thereby clogging up the system, the rule allows the division to withdraw a file. Filings are usually effective in a much shorter period. In addition, over time, the financial and other information will become stale. The Division always contacts the issuer or counsel multiple times before a file is withdrawn.

6. How will the Agency measure the success of this regulation in terms of outputs and/or outcomes?

The Division interacts with members of the industry on a regular basis, including at the annual Securities Conference, email and telephone inquiries. Feedback from that interaction provides information for review and revision of rules, as has been the case over the multiple decades these rules have been in existence. In addition, changes in federal securities laws may require changes to Division rules and federal law will be monitored. The rules are considered successful because they achieve the dual missions of the Division: investor protection and fostering capital formation.

Development of the Regulation

7. Please list the stakeholders included by the Agency in the development or initial review of the draft regulation.

If applicable, please include the date and medium by which the stakeholders were initially contacted.

See attached list. Stakeholders were emailed a package of the rules with a cover letter indicating which rules were No Change and which were amendments. The email was sent Oct. 3, 2014, and comments were requested by Oct. 31. Prior to that, conversations were held individually with representatives of stakeholders for input on various rule changes.

8. What input was provided by the stakeholders, and how did that input affect the draft regulation being proposed by the Agency?

One stakeholder responded and indicated they did not have any comments.

9. What scientific data was used to develop the rule or the measurable outcomes of the rule? How does this data support the regulation being proposed?

Generally, these rules are meant to clarify, or provide specificity to, the statutes to which they refer. They also provide exemptions to registration where research and discussions with industry or members of the bar have demonstrated that investor protection would not be compromised, and the market would be more efficient, by such exemptions.

10. What alternative regulations (or specific provisions within the regulation) did the Agency consider, and why did it determine that these alternatives were not appropriate? If none, why didn't the Agency consider regulatory alternatives?

No other regulations were considered because these follow statutory requirements. Other than corrective changes and updating the rules to provide for changes in state law and coordinating with the federal national exchange lists, these rules have remained consistent for many years.

11. Did the Agency specifically consider a performance-based regulation? Please explain. *Performance-based regulations define the required outcome, but don't dictate the process the regulated stakeholders must use to achieve compliance.*

The statutes that the rules augment provide specific requirements relating to registrations. The rules are intended to provide clarification of the statutory scheme and to provide exceptions to registration, where warranted.

12. What measures did the Agency take to ensure that this regulation does not duplicate an existing Ohio regulation?

The Division is the only Ohio agency regulating in this area. All statutes and rules governing, or enforced by, the Division were reviewed to ensure there were no duplications or conflicts.

13. Please describe the Agency's plan for implementation of the regulation, including any measures to ensure that the regulation is applied consistently and predictably for the regulated community.

While there is some updating to rules, all these rules have been in place for many years, some dating back to 1970's. The Division does not anticipate any change in applying the rules in a consistent and predictable manner. The industry and the Bar will have access to the Division's rules to promote compliance and the Division regularly receives, and responds to, phone and written questions seeking guidance. The Division's Ohio Securities Conference annually encourages interactions between the Division and industry and the Bar.

Adverse Impact to Business

14. Provide a summary of the estimated cost of compliance with the rule. Specifically, please do the following:

- a. Identify the scope of the impacted business community;**
Securities issuers and the securities Bar.
- b. Identify the nature of the adverse impact (e.g., license fees, fines, employer time for compliance); and**

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The rules do not impose fines or penalties. There will be some additional time added to the time to comply with the statute for the rules dealing with the different registration processes. However, some rules – e.g. 1301:6-3-09.3, dealing with electronic filings and 1301:6-3-08, allowing additional time for effectiveness – should reduce the amount of time issuers spend filing, or renewing, a registration. The exemptions under 1301:6-3-02 and -03 allow issuers to avoid registration. 1301:6-3-04.1 provides for a reduction in the financial statements required to be filed under certain conditions.

c. Quantify the expected adverse impact from the regulation.

The adverse impact can be quantified in terms of dollars, hours to comply, or other factors; and may be estimated for the entire regulated population or for a “representative business.” Please include the source for your information/estimated impact.

The balance sheets required will necessitate an amount of time to prepare proportionate to the complexity of the issuer’s financials and the type of registration.

Where an issuer is registering by description a large dollar amount of securities or for an oil and gas offering, the preparation of an offering circular will take a significant amount of time, depending of the complexity of the offering and the need for full and fair disclosure.

If advertising is filed with the Division, it will require the time to prepare a cover letter describing how it will be used. In addition, it will take a minimal amount of time to create a system to store all the materials that must be retained for a sufficient period to comply with rule or statute. The time needed will be dependent on the size and complexity of the offering.

15. Why did the Agency determine that the regulatory intent justifies the adverse impact to the regulated business community?

The overall responsibility of the Division is both investor protection and to ensure and allow the markets to operate fairly and efficiently. If all regulations are applied equally, then all issuers have an equal opportunity to bring their offering to the public for the public to determine if the offering merits investment dollars. A key component of investor protection and equality in the market is full and adequate disclosure, providing investors with sufficient information to compare issues of securities as investments. The rules intend to provide disclosure and equality of treatment, promoting a fair and efficient securities market.

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Regulatory Flexibility

16. Does the regulation provide any exemptions or alternative means of compliance for small businesses? Please explain.

The rules, specifically 1301:6-3-06 and -09 provide for alternatives for small issuers, as do the comparable statutes upon which the rules are based. Registration by description provides that smaller issuers need not prepare an offering circular. Registration by description allows for the filing of a U-7 (Small Company Offerings Registration) in lieu of an offering circular.

17. How will the agency apply Ohio Revised Code section 119.14 (waiver of fines and penalties for paperwork violations and first-time offenders) into implementation of the regulation?

There are no fines or civil penalties for paperwork violation of these rules. There is the possibility of a refusal, suspension or stop order if the offering or the business is found to be fraudulently conducted or the offering is grossly unfair or tends to defraud or deceive, but that would not be a paperwork violation, as defined.

18. What resources are available to assist small businesses with compliance of the regulation?

The Division regularly responds to phone or personal inquiries, for small or large businesses or their counsel. Division forms provide instructions for filers. Generally, counsel is retained because of the inherent civil liabilities in securities offerings. In addition to the rules being readily available, the Division publishes a quarterly Bulletin, available to anyone on our web page, discussing relevant issues.

ATTACHMENT
SECURITIES STAKEHOLDER'S LIST

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