OHIO SECURITIES BULLETIN

A QUARTERLY PUBLICATION OF THE OHIO DIVISION OF SECURITIES

Ted Strickland
Governor of Ohio

Kimberly Zurz
Director of Commerce

G. Brent Bishop
Commissioner of Securities

GOVERNOR STRICKLAND APPOINTS KIMBERLY A. ZURZ AS DIRECTOR OF COMMERCE

Governor Ted Strickland appointed Kimberly A. Zurz as Director of the Ohio Department of Commerce, effective January 29, 2007. Director Zurz oversees the Division of Securities and the other divisions of the department, including: Administration, Financial Institutions, Labor & Worker Safety, Liquor Control, Real Estate & Professional Licensing, State Fire Marshal and Unclaimed Funds.

"I am committed to providing strong leadership to carry out the Department's mission of consumer protection and fair, efficient regulation of business," Director Zurz said. "I look forward to working with Ohio's securities and investment adviser professionals who play an integral role in enhancing the financial security of the citizens of Ohio."

Prior to her appointment, Director Zurz served as a State Senator representing the 28th District, which includes Portage County and a portion of Summit County. While serving more than three years in the Ohio Senate, she earned a reputation as a staunch advocate for higher education and job creation.

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G. BRENT BISHOP APPOINTED NEW SECURITIES COMMISSIONER

A new Commissioner was recently appointed to helm the Ohio Division of Securities. G. Brent Bishop assumed duties as the new Commissioner of Securities on February 26, 2007. He succeeds James Turner, who had been Acting Commissioner since June 2006. Commissioner Bishop has had an extensive presence in the securities industry for many years. He is also no stranger to state government, having served as Assistant Director of the Ohio Department of Commerce and the Superintendent of Real Estate in the early 1980s.

Commissioner Bishop earned his Bachelor of Science Degree in 1971 from the Ohio State University, where he served as class president.

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Before her appointment to the Ohio Senate in 2003 and election in 2004, Director Zurz served more than 11 years on the Summit County Council, including three terms as President. During her service on the Council, she presided over a county budget of over $560 million.

Director Zurz is the President of her family's 78-year-old business, The Eckard-Baldwin Funeral Home, in Akron. As a businesswoman, she has an informed perspective about the needs and concerns of small businesses and the importance of excellent customer service.

She is married to Richard Zurz, Jr., and has three children. She and her family reside in Green in Summit County. Zurz graduated from Firestone High School in Akron and attended the University of Akron.

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He did some post-graduate work in finance at OSU and Purdue University. After completing his studies, he held positions as Assistant Treasurer of the Acceleration Corporation, a public credit and casualty insurance company based in Columbus, and Director of National Accounts at Blue Cross of Central Ohio. After his time in state government from 1981 through 1984, he served as Vice President of Alexander and Alexander, a Columbus, Ohio international investment insurance brokerage firm.

Commissioner Bishop's foray into the securities industry occurred in 1990 when he took a job as a Divisional Vice President at PaineWebber, Inc. He later also served as Vice President at McDonald & Company, Inc., a regional investment wire house and investment banking firm based in Cleveland, Ohio. In 1995, he became Chairman and CEO of FirstCapital Asset Management, Inc., a full-service financial services and investment firm operating multiple business-line groups, including a retail client investment group and a corporate finance consulting group.

Commissioner Bishop has held several civic positions, including an elected city council position from 1987-1991. He has also served on the Westerville Planning Commission and the Westerville Board of Zoning Appeals. Community activities include Governing Board Member of Catholic Social Services in 1987, Board Member, Franklin County Children Services in 2006 and Board Member of the United Methodist Children's Home in 2001.

OHIO SECURITIES BULLETIN

Desiree T. Shannon, Esq., Editor

The Ohio Securities Bulletin is a quarterly publication of the Ohio Department of Commerce, Division of Securities. The primary purpose of the Bulletin is to (i) provide commentary on timely or timeless issues pertaining to securities law and regulation in Ohio, (ii) provide legislative updates, (iii) report the activities of the enforcement section, (iv) set forth registration and licensing statistics and (v) provide public notice of various proceedings.

The Division encourages members of the securities community to submit for publication articles on timely or timeless issues pertaining to securities law and regulation in Ohio. If you are interested in submitting an article, contact the Editor for editorial guidelines and publication deadlines. The Division reserves the right to edit articles submitted for publication.

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Blue Flame Part I:
Case Gives Guidance Regarding Internet Solicitations

Editor's Note: This article constitutes the first of a two-part series which reviews the case of Blue Flame Energy Corporation et al. v. Ohio Department of Commerce, Division of Securities. The case, which arises out of the Tenth Appellate District, sets forth several important holdings, mainly regarding the Division's jurisdiction over companies who have a presence on the internet and the extent of federal pre-emption of certain provisions of the Ohio Securities Act.

The internet has provided issuers and sellers of securities an additional means of pitching their offerings to potential investors. However, as one would suspect, this relatively recent development in the securities marketplace has been accompanied with confusion among issuers, sellers and regulators. For instance, what type of internet activity constitutes a "sale" of securities as the term is used in R.C. 1707.01? Does the Division of Securities automatically obtain jurisdiction over an issuer who merely posts a website that could be accessed by in-state residents? The Tenth District Court of Appeals of Ohio has answered these questions in the case *Blue Flame Energy Corporation et al. v. Ohio Department of Commerce, Division of Securities*, (No. 05AP1053, 10th District).

The case arose when Blue Flame Energy Corporation of Kentucky made two Form D notice filings with the Division on behalf of two limited partnerships, Pine Mountain 2002, Ltd. and Pike 2002, Ltd. Blue Flame was engaged in the business of oil and natural gas exploration, development and operations. It was the managing partner of the two limited partnerships. Each Form D claimed an exemption for the limited partnerships' sales pursuant to Rule 506, which allows an exemption for transactions not involving sales to the public. The Division requires a notice filing when an issuer is claiming this federal exemption with the SEC, which is found under Regulation D of the Securities Act of 1933. At the time of the filings, each of the limited partnerships had sold an interest to one Ohio investor.

Despite the filings, the Division issued a Notice of Opportunity for Hearing against Blue Flame, Energy Group, Inc. (a related company) and the partnerships, saying the companies could not rely on a Regulation D exemption because they had engaged in general solicitation and advertising through their websites, and, therefore, had sold unregistered securities in prohibition of R.C. 1707.44(C)(1). Blue Flame and its related companies requested a hearing pursuant to Chapter 119 of the Ohio Revised Code, and after a review of joint stipulations and briefs from each party (no testimony was heard), the Hearing Officer issued a report and recommendation. The Hearing Officer found that the issuers had violated R.C. 1701.44(C)(1) and recommended that the Commissioner of Securities issue a Cease and Desist Order against the companies. On January 26, 2004 the Commissioner issued a Cease and Desist Order, which led the issuing companies to file an appeal with the Franklin County Court of Common Pleas.

Upon appeal, a trial court magistrate recommended that the trial court reverse and vacate the Cease and Desist Order. The magistrate found that federal law pre-empted the Division from regulating the sale of the issuers' securities because they were relying on a Rule 506 exemption in offering their securities for sale. The magistrate also found that the Division lacked personal jurisdiction over the companies and that they had a valid exemption under Ohio Administrative Code rule 1301:6-3-03(E)(8), which deals with internet sales. In the Division's favor, the magistrate

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found that the Division relied on reliable, probative and substantial evidence in supporting the Hearing Officer's conclusion that the offer and sale of the issuing companies' securities failed to qualify for exemptions under Rule 506 and R.C. 1707.03(X), which is the provision requiring notice filings for those meeting the federal exemption. But, since the magistrate found that federal law preempted the application of R.C. 1707.44 (C)(1), this finding was irrelevant. The trial court adopted the magistrate's decision and vacated the Cease and Desist Order. The Court's action led to the Division's appeal in the Tenth District Court of Appeals.

The Court of Appeals devoted much of its opinion discussing the jurisdictional issues of the case. It used a three-pronged test to determine whether the Division could claim personal jurisdiction over the issuers:

1. the defendant must purposefully avail itself of the privilege of acting in the forum state or causing a consequence in the forum state;

2. the litigation must arise from the defendant's activities in the forum state, and

3. the defendant must have a substantial enough connection with the forum state to make the exercise of jurisdiction over the defendant reasonable.

The Court first addressed the first prong of the test by considering a federal case, *Neogen Corp. v. Neo Gen Screening, Inc.* (C.A. 6, 2002) 282 F.3d 883, 890, which had held that "a defendant purposefully avails itself of the privilege of acting in a state through its website if the website is interactive to a degree that reveals specifically intended interaction with residents of the state." This weighed against the Division's arguments when the Court considered the issue in light of the website's interactive capabilities with potential investors. The Court noted that "personal jurisdiction exists only in forums in which a party has purposeful, deliberate contact, not fortuitous contact occasioned by the wide accessibility of the internet." The Energy Group's website provided dialogue boxes where visitors could enter contact information and personal comments. The Court determined that this was not enough to characterize the website as interactive, and there was no evidence that there was any exchange of information between Energy Group and Ohio residents. The Court reasoned that, therefore, there was no purposeful availment by Energy Group, and the Division could not claim personal jurisdiction over the company. The Court held that the Division did not have jurisdiction over Blue Flame Energy Group by virtue of the availability of its website to Ohio residents. The Court noted that the company's "website was devoted to explaining oil and gas development and operations, and to advertising Energy Group and its activities in the oil and gas field. Such communications constitute passively posted information, and cannot serve as a basis for jurisdiction."

The Court also noted that, in a jurisdictional context, the mere posting of a website does not constitute a "sale" under R.C. 1707.01(C). The Court said that if "advertising a security through a website constitutes a 'sale' in Ohio, then the Division would have jurisdiction over every issuer who maintains a promotional website, regardless of whether the issuer actually sells or intends to sell securities in Ohio." However, the Court acknowledged that because Blue Flame, Pine Mountain and Pike 2002, actually sold partnership interests in Ohio, they had "purposefully availed themselves of the privileges of acting in Ohio", thus allowing the Division to pass the first prong of the test outlined above.

The Court then reviewed the issuers' actions in relation to the second prong of its three-part test in questioning whether the Division's regulatory action in this case arose from the sale

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of the partnership interests. The Court concluded that the Division's regulatory action stemmed from the websites' content, which the Division claimed prevented the issuers from claiming private placement exemptions under Rule 506 and R.C. 1707.03(X). The Court noted that there was no evidence that the purchasers had viewed the issuers' websites, or even that "they were influenced by advertising on the websites, or that Blue Flame completed the sales after the purchasers contacted them through the websites." However, the Court found in the Division's favor that the filing of the Form Ds on behalf of the partnerships related to the facts underlying this regulatory action. Therefore, the Division fulfilled the second prong of the test determining jurisdiction.

The third prong of the test requires that the exercise of jurisdiction be reasonable, and in determining this, the Court recalled well-established law that, in order to determine reasonability of jurisdiction, several factors must be balanced: "the interest of the forum state, the plaintiff's interest in obtaining relief, the interest of other states in obtaining the most efficient resolution of controversies, and the forum state's interest in furthering fundamental substantive social policies." Upon weighing these considerations, the Court concluded that the Division's exercise of jurisdiction was reasonable, and thus, it had satisfied all prongs of the test to determine valid jurisdiction over Blue Flame, Pine Mountain and Pike 2002. *Article to be continued in the next issue.*

Division of Financial Institutions Takes Position Affecting Investment Advisers

The Division of Financial Institutions stated a position in its Mortgage Brokers and Lenders Letter No. 2006-2 that could potentially affect investment advisers. The Division cited the prohibition against mortgage brokers or loan officers "obtaining a referral fee from a party with a related interest in the transaction" found in R.C. section 1322.071(B)(3). The Letter notes that a "person acting as an investment adviser urging the refinancing or purchase of property who also acts as the loan officer in the same transaction effectively is obtaining fees through a self-referral."

The Letter added that "the notion of borrowing one's home equity to invest in the market is a risky strategy, which should not be undertaken where there is a significant conflict of interest arising from considerations of the mortgage broker or loan officer's own profit or remuneration when counseling such an investment strategy." The Division concluded that acting as both an investment adviser and a loan officer in the same transaction is an "improper and dishonest practice" which violates R.C. 1322.07(C) and recommended that registrants and licensees review their policies regarding the matter.

Licensing Statistics

License Type	YTD 2006
Dealers	2,437
Salespersons	137,286
Investment Adviser/Notice Filers	2,059
Investment Adviser Representatives	11,254

On November 14, 2006, **Gary L. McNaughton** of Elyria, Ohio was indicted by a federal grand jury in Cleveland, Ohio on thirteen felony counts. The charges included one count of securities fraud, five counts of mail fraud, two counts of money laundering, three counts of tax evasion, one count of the sale of unregistered securities and one count of false statements. McNaughton entered a not guilty plea to all the counts on November 17, 2006, in U.S. District Court for the Northern District of Ohio.

The indictment alleged that from 1999 through June 2003, McNaughton sold securities to approximately 200 investors in numerous states including Ohio for a total amount of approximately $17 million. McNaughton sold unregistered promissory and demand notes, and he told investors their funds would be invested with Andrew Lech in Canada who used a unique trading strategy to generate returns. Most of the investors were affiliated with The Church of the Open Door in Ohio. The indictment also alleged that McNaughton did not disclose that some of the funds were used to pay his personal expenses, including luxury items such as Corvette automobiles, Harley Davidson expenses, motor homes and three parcels of real estate. The indictment further charges that McNaughton engaged in financial transactions designed to hide the fraudulent proceeds and to promote the investment scheme. In addition, the indictment alleges that McNaughton sought to evade income taxes on the investor funds he received by understating his income to the Internal Revenue Service. Finally, McNaughton is charged with lying to federal investigators. The Ohio Division of Securities assisted in the investigation.

The Ohio Division of Securities previously issued three Cease and Desist Orders in this matter to Gary McNaughton and The Haven Equity Company (Division Order No. 03-217), Andrew Lech (Division Order No. 03-241), and Allen McNaughton (Division Order No. 04-106).

On December 18, 2006, in Licking County Common Pleas Court, **Carl Fanaro**, formerly of Columbus, Ohio was sentenced to nineteen years in prison and ordered to pay restitution. On October 27, 2006, a jury found Fanaro guilty of 99 counts including securities fraud, making false statements in connection with the sale of securities, unregistered sales, and unlicensed sales. Fanaro's conviction related to his sale of limited partnership units.

Martin R. Hershner was sentenced in Richland County Common Pleas Court on December 27, 2006, to five years in prison, to be followed by five years community control, and ordered to pay approximately $471,000 in restitution. Previously, Hershner pled guilty on October 11, 2006, to 33 felony counts, including one count of engaging in a pattern of corrupt activity, 11 counts of securities fraud, four counts of false representations in the sale of securities, 10 counts of forgery, one count of money laundering, one count of aggravated theft, two counts of identity fraud, one count of telecommunications fraud, and two counts of unauthorized use of property. Hershner had been indicted on April 10, 2006, on 118 counts on charges in connection with the mishandling of approximately $670,000 from 17 Ohio clients while he was licensed as a securities salesperson and investment adviser agent for MML Investors Services, Inc. *(See also Enforcement Section Reports in this issue.)*

R&C Energy Corp.

On November 22, 2006, the Division issued a Cease and Desist Order, Amended Division Order No. 06-203, to R&C Energy Corp. of New York, New York.

The Division found that R&C Energy Corp. violated Ohio Revised Code sections 1707.44(C)(1) and1707.44(G) for the sale of unregistered, non-exempted securities and securities fraud. On March 2, 2006, the Division issued a Notice of Opportunity for Hearing, Division Order 06-074, to R&C Energy Corp. The Division found that the company sold fractional undivided interests in oil leases located in Tennessee, West Virginia, Kentucky and Illinois, to Ohio investors that were sold as unregistered, non-exempted securities. In addition, the Division found that the president of R&C Energy Corp., C. Conrad Bein, had a criminal conviction for securities fraud that was not disclosed to the investors.

The Division notified R&C Energy Corp. of their right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. After legal publication was completed on the Division Order, a hearing was not requested and the Cease and Desist Order was issued on November 22, 2006.

Martin R. Hershner

On November 21, 2006, the Division issued a Cease and Desist Order, Division Order No. 06-235, to Martin R. Hershner of Lexington, Ohio.

The Division found that Martin Hershner violated Ohio Revised Code sections 1707.44(B)(4), 1707.44(G) and 1707.44(K). The Division had previously issued a Notice of Opportunity for Hearing, Division Order 06-226, to Martin Hershner on October 18, 2006. The Division found that Martin Hershner did the following: (1) forged numerous documents and signatures to obtain funds from client accounts without their permission; (2) redeemed customer funds by telephone without the clients' permission; (3) failed to invest investors' funds as he had represented to the investors; (4) changed names on checks to his own as the payee; (5) forged clients' names on their checks; (6) applied for and obtained loans and credit cards using other people's identities and personal information; (7) used his post office box for the delivery of proceeds from funds he stole from client accounts; (8) concealed the theft of client funds through transactions at the bank involving the purchase of cashier checks; (9) credited client funds to other client accounts; and (10) converted funds to his own personal use and transferred the funds into accounts he controlled. Martin Hershner conducted this activity while he was licensed as a securities salesperson and investment adviser agent for MML Investors Services, Inc.

The Division notified Martin Hershner of his right to an adjudicative hearing pursuant to Chapter 119 of the Revised Code. A hearing was not requested. The Cease and Desist Order was issued on November 21, 2006, for securities fraud, false representations in the sale of securities and making false reports of securities transactions. *(See Hershner summary in the Criminal Updates section.)*

Augrid Corporation; M.J. Shaheed

On December 7, 2006, the Division issued a Cease and Desist Order (Division Order No. 06-240) and Consent Agreement to Augrid Corporation and its CEO, M.J. Shaheed. Shaheed formerly resided in Cleveland, Ohio.

The Division had previously issued a Notice of Opportunity for Hearing on December 12, 2005 which alleged that the Respondents had violated Revised Code section 1707.44(C)(1) by selling an un-

Enforcement Section Reports

registered security in the form of a convertible subordinated debenture to an Ohio resident. The Respondents requested a hearing pursuant to Chapter 119 of the Ohio Revised Code. The Division and the Respondents agreed to enter into a Consent Agreement in which the Respondents consented, stipulated and agreed to the Division's findings. They also waived their right to appeal the final order. The Consent Agreement was issued in conjunction with the Cease and Desist Order in which the Division cited the Respondents for the violation noted above.

Great Plains Financial, LLC; Mark S. Blakemore

On October 17, 2006, the Division issued Order No. 06-219, a Cease and Desist Order, against Great Plains Financial, LLC and Mark S. Blakemore of Erie, Colorado.

Great Plains and Blakemore sold a nine-month debenture in the amount of $40,000 to one Ohio investor in October 2005. The debenture was to pay the investor four percent a month, with the accrued interest and principal due at the end of the nine-month term. Great Plains and Blakemore were involved in a purported trading program with various banks, which were to use investors' funds to buy and sell commercial paper for profit. The debenture offered by Great Plains and Blakemore is a security as defined under Ohio Revised Code section 1707.01(B) of the Ohio Securities Act. The Division found that Great Plains and Blakemore violated the provisions of Ohio Revised Code section 1707.44(C)(1), which prohibits the sale of unregistered securities. The debenture was not properly registered or exempt from registration as required by the Division.

On September 11, 2006, the Division issued Order No. 06-199, a Notice of Opportunity for Hearing, against Great Plains and Blakemore for violating Ohio Revised Code section 1707.44(C)(1). Great Plains and Blakemore did not timely request an adjudicatory hearing pursuant to Chapter 119 of the Ohio Revised Code, allowing the Division to issue Cease and Desist Order No. 06-219.

Licensing Section Reports

William Thompson

On April 19, 2006, the Division issued Order No. 06-089, a Notice of Intent to Deny the securities salesperson application of William L. Thompson, CRD No. 1710409. The Division alleged that Thompson lacked good business repute pursuant to R.C. section 1707.19(A)(1) and O.A.C. rule 1301:6-3-19(D), as the result of an NASD Acceptance, Waiver and Consent issued on November 10, 2005. The NASD entered findings that Thompson violated NASD Conduct Rule 2110 by affixing the names of individuals to enrollment forms and submitting them to his employer. Thompson was fined $10,000 and suspended from association with any NASD member in any capacity for 30 days. Thompson requested an administrative hearing, which was held on August 22, 2006. The Hearing Officer issued her Report and Recommendation on October 12, 2006, finding that the Division had sustained its burden of proving that Thompson was not of good business repute and recommended that his license application be denied. On November 21, 2006, the Division issued a Final Order Denying Application for Securities Salesperson License, Order No. 06-233.

REGISTRATION AND EXEMPTION ADVISORY COMMITTEE MINUTES

The Registration and Exemption Advisory Committee held its meeting at the Ohio Securities Conference on October 13, 2006. The meeting was well attended by securities practitioners throughout the state of Ohio. The attendees were interested in recent developments in the Division's registration section. The Division always encourages comments from practitioners concerning statutory provisions, rules, guidelines or procedures.

The Division commented that practices and procedures for registration by description have become increasingly difficult. Within the past year, Form 6 filings have had sales prior to filing. Applicants have withdrawn offerings while a few offerings have been referred to the Division's Enforcement Section. The Division has also seen securities offerings done to pay for litigation. The Division is concerned that investors may not be able to assess risks and expenses of complex litigation.

The Division has sent comments on registrations by description within two to three business days. This has left the remaining time period of four to five business days for the applicants to respond to the comments. The Division suggests that applicants waive the effective date until a resolution of all comments. This waiver will provide the Division and applicant with ample time to provide an adequate response. Unfortunately, applicants have not been timely in waiving effective dates. The registration section often prepares draft orders to suspend or refuse the offering for the Commissioner's signature. Often, the waiver is mailed on the last day just prior to the Commissioner's signature.

The committee also discussed a registration by description that was a public offering with internet and cable advertising restricted to Ohio. Password protected measures or firewalls were used to prevent the viewing of the site in other states, thereby limiting its availability to residents of Ohio. Only Ohio residents could purchase the offering. The Division suggested the applicant obtain a no-action letter from the Securities and Exchange Commission ("SEC") due to the internet distribution. The Division was aware of SEC no-action letters addressing international issuers who desired to avoid applicability of securities laws in the United States. The applicant was unable to obtain an SEC no-action letter and hence declined to distribute its advertising using the cable and the internet. While measures may be taken by issuers to keep internet offerings out of the United States, the issue remains whether an internet offering can be confined to a state for purposes of the intrastate offering exemption under section 3(a)(11) of the Securities Act of 1933.

NASDAQ has petitioned the SEC to amend Rule 146(b) to permit NASDAQ Capital Markets issues as "covered securities" under the proposal. NASDAQ argues that the listing standards exceed those of AMEX. The North American Securities Administrators Association ("NASAA"), without objecting to the petition, has expressed concern that the listing standards are being waived all too frequently. The Division will be monitoring this development throughout the year.

As a notice to the attendees, the Division mentioned that NASAA and the SEC have informally discussed the electronic filing of Form D. No formal proposals have been announced and it is uncertain whether there will be text revisions to the form. The Division will likely follow any revisions made to accommodate filers.

SUMMARY OF THE ENFORCEMENT ADVISORY COMMITTEE MEETING

After the introduction of Division staff present at the meeting, several tropics were discussed at the annual Enforcement Advisory Committee Meeting, which was held on October 13, 2006 during the Ohio Securities Conference. The proliferation of penny stock solicitations over the internet was discussed. Robert Lang, the Attorney Inspector for enforcement and meeting chairman, noted that most of these solicitations fell under the auspices of the SEC and other federal agencies, as these solicitations usually involved multi-jurisdictional issues.

Attendees also inquired whether the Division had the equivalent of the Wells Submission, which is used by the SEC to warn potential targets that they are about to be subject to enforcement action. This allows the respondent to proffer evidence in his or her defense. It was explained to attendees that the Division has no such mechanism in place to resolve enforcement actions. It was pointed out that all targets of enforcement actions have a right to challenge Division allegations laid out in the initial Notice and Opportunity for Hearing at a hearing guaranteed them by Chapter 119 of the Ohio Revised Code.

Some attendees expressed the opinion that the Division's investigatory ".23 hearings" were unfair to respondents because the information they seek is too broad in scope and they do not give respondents adequate notice of the potential charges. Division personnel pointed out that the hearings are investigatory in nature and meant to gather as much information as possible. They also pointed out that requiring these hearings to be premised on specific charges would essentially require the Division to prove its case before gathering all the evidence, a portion of which may be discovered during a .23 hearing.

Some discussion ensued regarding the Division's refusal to insert "admit or deny" language in its consent agreements, which usually accompany Cease and Desist Orders that have been settled. Inserting such language is akin to a "no contest" plea. Division officials noted that they would review the policy regarding the use of such language.

MINUTES OF THE 2006 LICENSING ADVISORY COMMITTEE MEETING

Discussion among Division staff and committee members was had on the following issues: matters related to the Form BR sole proprietor filings, legislative issues, and the effect of the change of administration on Licensing. Also discussed were common deficiencies found in exams, particularly problems with business continuity plans and compliance manuals, in addition to inconsistencies in Form ADVs. Consideration was given to the Division implementing an industry-only conference, held for investment advisers. Following discussion of the aforementioned topics, the meeting was adjourned.

TAKEOVER ADVISORY COMMITTEE MINUTES

The Division's Takeover Advisory Committee held its annual meeting at the 2006 Ohio Securities Conference. David Zagore, Co-Chair of the Takeover Advisory Committee, and Michael Miglets of the Division prepared the agenda and served as moderators for the meeting. What follows are the agenda items that were discussed.

R.C. 1707.041 was amended effective October 12, 2006 to include a three-day review period for material amendments of control bids. An offeror is required under R.C. 1707.41(A)(5) to file material amendments to a control bid, including changes in the consideration offered, increases or decreases in the percentage of the class of securities to be acquired, or changes in the dealer's soliciting fee, with the Division. The Division then has three days to review the amendment. If the disclosure is inadequate, the Division may suspend the tender offer. Following the suspension, the Division is required to schedule a hearing within three days. A final ruling on the suspension must be issued within three days of the hearing. If the offeror amends the disclosure in the offer to purchase, the suspension may be lifted by the Division. The nine-day period for Division action is designed not to conflict with the ten day period specified in Rule 14d-4(d)(2)(ii).

The Securities and Exchange Commission's revisions to the best-price rule for tender offers were effective on December 8, 2006. The tender offer best-price rule requires that all security holders tendering shares or other securities must be treated equally. The revisions include: 1) clarification that the rule applies only to the consideration paid for securities; 2) an exemption for certain compensation, severance and employee benefits; and 3) a safe harbor for the exemption from the rule for certain compensation, severance and employee benefit arrangements approved by independent committees of the board of directors. The SEC's amendments to the tender offer best-price rule appear to be consistent with the requirements in R.C. 1707.041(B)(1) that the offer to security holders in the state of Ohio be on the same terms as offered to security holders in any other state.

The Ohio Control Bid Statute currently includes an exception in R.C. 1707.041(G)(1) for public utilities and public utility holding companies as defined in section 2 of the Public Utility Holding Company Act of 1935 ("PUCHA 35") if the control bid is subject to approval by the Securities and Exchange Commission ("SEC"), but oversight of public utility holding companies has shifted to the Federal Energy Regulatory Commission ("FERC") with the repeal of the PUCHA 35 and the enactment of the Public Utility Holding Company Act of 2005 (PUCHA 05). PUCHA 05 is primarily a books and records statute giving FERC the authority to prescribe standards for record keeping and to approve cost allocations. State public utility commissions are also given access to books and records.

While the FERC has oversight over mergers and acquisitions of public utility holding companies, the review is primarily focused on the effect of the acquisition on rates, competition and regulation. *See* section 203 of the Federal Power Act, 16 U.S.C. § 824(b) (2000). While the FERC must find that the acquisition is in the "public interest," it appears that the review has a different focus than the SEC's investor protection standard.

The Division is seeking input on an appropriate amendment to R.C. 1707.041(G)(1) to insure the protection of Ohio security holders. It initially looked at the hearings required at the Ohio Public Utilities Commission ("PUCO"), but the review of mergers and acquisitions at PUCO is based on "pub-

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lic convenience" and "not contrary to the public interest" with a focus on adequate service and reasonable rates. The PUCO review of acquisitions does not appear to focus on disclosure to security holders.

The question for the Division's Takeover Advisory Committee and the OSBA Corporation Law Committee's Tender Offer Subcommittee is whether to amend R.C. 1707.041(G)(1) to include an exception for public utilities and public utility holding companies subject to regulation by FERC and/or PUCO or should a filing with the Division be required.

David Zagore raised the issue of share lending by institutional investors and brokers. These transactions involve the passing of voting rights by a nominee holder to a third party via contracts to purchase and resell the securities immediately prior and after the record date. The party borrowing the shares may have its own agenda unique from that of the long-term investor. The ultimate beneficial owners may be unaware that their voting rights have been transferred. When the ultimate beneficial owner gives instructions on voting to their broker, the instructions may be silently ignored or result in over votes. Transferring voting rights through a lending transaction should at least be based on a knowing consent by the beneficial owner. Without a knowing consent, the lending transaction raises fiduciary issues for the nominee holder or may be fraudulent.

With the preemption risk in adopting proxy rules at the state level, it was suggested that this issue be sent to the North American Securities Administrators Association, Inc. ("NASAA") for consideration. NASAA's Shareholders Rights Project Group may be able to develop a recommendation for the full NASAA membership to present to the SEC. David Zagore and Michael Miglets volunteered to send a letter to the Shareholder Rights Project Group detailing the potential abuses in share lending without the informed consent of the beneficial owners.

Editor's Note: Ohio Securities Bulletin issues 2007:1 and 2007:2 will be combined and published at the conclusion of the second quarter of 2007.

Capital Formation Statistics*

Because the Division's mission includes enhancing capital formation, the Division tabulates the aggregate dollar amount of securities to be sold in Ohio pursuant to filings made with the Division. As indicated in the notes to the table, the aggregate dollar amount includes a value of $1,000,000 for each "indefinite" investment company filing. However, the table does not reflect the value of securities sold pursuant to "self-executing exemptions" like the "exchange listed" exemption in R.C. 1707.02(E) and the "limited offering" exemption in R.C. 1707.03(O). Nonetheless, the Division believes that the statistics set out in the table are representative of the amount of capital formation taking place in Ohio.

**Categories reflect amount of securities registered, offered, or eligible to be sold in Ohio by issuers.*

***Investment companies may seek to sell an indefinite amount of securities by submitting maximum fees. Based on the maximum filing fee of $1100, an indefinite filing represents the sale of a minimum of $1,000,000 worth of securities, with no maximum. Consequently, for purposes of calculating an aggregate capital formation amount, each indefinite filing has been assigned a value of $1,000,000.*

Filing Type	4th Qtr 2006	YTD 2006
Exemptions		
Form 3(Q)	$19,488,493	$158,140,233
Form 3(W)	6,100,000	18,160,000
Form 3(X)	138,408,529,462	533,574,482,495
Form 3(Y)	25,000,000	44,125,000
Registrations		
Form .06	63,726,200	2,021,545,900
Form .09/.091	9,378,090,703	27,972,033,433
Investment Companies		
Definite	134,566,000	496,971,891
Indefinite**	592,000,000	2,241,000,000
TOTAL	**$148,627,500,858**	**$566,526,458,952**

Registration Statistics

The following table sets forth the number of registration, exemption, and notice filings received by the Division during the fourth quarter of 2006, compared to the number of filings received during the fourth quarter of 2005. Likewise, the table compares the year-to-date filings for 2005 and 2006.

Filing Type	4th Qtr '06	YTD '06	4th Qtr '05	YTD '05
1707.03(Q)	19	95	25	118
1707.03(W)	4	7	3	10
1707.03(X)	413	1811	429	1614
1707.03(Y)	1	7	1	9
1707.04/.041	0	1	0	1
1707.06	13	75	10	65
1707.09/.091	43	152	50	154
Form NF	1425	5242	1214	4835
Total	**1918**	**7390**	**1732**	**6806**