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THE UNIFORM SECURITIES ACT—A STEP FORWARD IN STATE REGULATION

ROGER W. TOMPKINS*

The Uniform Securities Act,1 recently passed by the West Virginia Legislature,2 opens new vistas for state securities regulation. The Act was drafted for the National Conference of Commissioners on Uniform State Laws by Professor Louis Loss of Harvard Law School and Edward M. Cowett, Research Associate. It was approved by the National Conference on August 25, 1956.3 The Act followed a two year study of state securities regulations. Those who participated in the study included representatives of the National Conference, the American Bar Association, the National Association of Securities Administrators, the Securities and Exchange Commission, the Investment Bankers Association of America, the National Association of Securities Dealers, Inc., and several practicing lawyers with experience in state securities regulation, commonly called "blue sky laws."4 To date, thirty-three states have adopted the Uniform Securities Act in some form.5

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1 W. VA. CODE ANN. §§ 32-1-1 to 32-4-7 (Cum. Supp. 1974) [hereinafter referred to as the Act].

2 The Uniform Securities Act was passed by both Houses of the Legislature March 9, 1974, and signed by the Governor. The Act became effective June 7, 1974.

3 L. Loss & E. Cowett, BLUE SKY LAW 246, 249 (1958) [hereinafter cited as Loss & Cowett]. This work is definitive when discussing the Uniform Securities Act. The West Virginia Act does not differ substantially from the official version. This official version together with Official Comments and Draftsmen's Commentaries on each section, appears in the work by Loss and Cowett, beginning on page 249. The Comments and Commentaries are interwoven with the substance of this article. When an idea occurred to the writer only upon reading the Comments and Commentaries, an appropriate citation appears. Otherwise, the analysis and description of the Act, with all the faults, belong to the writer, though, necessarily, some such ideas may also appear in the Comments and Commentaries.

4 Id. at 246. The name, blue sky law, comes from the idea that early state regulatory schemes were designed to prevent the sale of securities "which have no more basis than so many feet of 'blue sky' . . . ." (citations omitted). Goodwin, Blue Sky Law—West Virginia Securities Laws and the Promoter, 73 W. VA. L. REV. 11 n.2 (1970) [hereinafter cited as Goodwin].

5 1 CCH BLUE SKY L. REP. ¶ 4901 (1974). It is difficult to discover case law under the Act. In Virginia, which has substantially adopted the Uniform Securities Act, the most "significant" pronouncement is from a federal court which held the Act inapplicable to the facts of the case before it. Stevens v. Abbott, Proctor &
Basically, state law and the regulation of securities by state agencies are limited to securities transactions and issues which take place within the state. The Uniform Act was designed to accomplish this purpose. Federal law and regulation, on the other hand, apply to securities transactions and issues which take place in more than one state. An understanding of the Uniform Act is enhanced by a brief review of federal securities regulation, because the Uniform Act encompasses certain concepts and practices which have long been a part of federal securities regulation. In part, the Uniform Act reflects the basic philosophy of federal regulation, that is, full and fair disclosure. Disclosure is accomplished by requiring certain issuers of securities to the public to file a registration statement containing financial and other material information about the issuer with the Securities and Exchange Commission. A prospectus, which is part of the registration statement, contains information that enables an investor to evaluate the securities offered and to make an informed decision whether or not to buy. The prospectus must be given to all persons who are offered the security being sold. The registration statement, including the prospectus, must be filed prior to a public offering of securities and no sale may be made until the registration statement has become effective. Thus, investors are granted a "waiting period" between filing and effectiveness in which to evaluate the securities to be offered.

During the waiting period, the Securities and Exchange Commission reviews the information contained in the registration statement to insure that it complies with the requirements of full and fair disclosure. The Securities and Exchange Commission has no power to pass upon the merits or quality of a public offering of securities; however, the Commission may suspend the effective date of the offering if it finds material misstatements or omissions


Although many states have adopted the Uniform Securities Act without substantial modification, some state legislatures have considerably altered provisions of the Uniform Act to conform with prior state law and administrative practice. See Note, Uniform Securities Act, 12 STAN. L. REV. 105 (1960), with introduction by J. Sobieski, then State Securities Commissioner [hereinafter cited as Note, Uniform Securities Act].

Of course, there are no cases yet decided under the Act in the West Virginia courts. Moreover, a citation of cases under prior West Virginia securities law would not be profitable, because West Virginia cast its prior law overboard and started afresh with the Act.
in the offering material, and alternatively, the Commission may issue a deficiency letter suggesting that certain matters be amended or supplemented. The latter course is the customary practice and deficiency letters are common. After the necessary amendments are made, the registration statement will become effective, and the public sale may begin.⁶

By examining the registration statement, the Commission makes no guarantee of adequacy or accuracy. Indeed, no representation may be made to the public that the Commission has approved or otherwise passed on the merits of the securities or found that disclosure was accurate or complete. A disclaimer to this effect must appear on the front page of the prospectus in bold face type. Criminal penalties and civil liability are provided for those who violate the provisions of full and fair disclosure.⁷

The philosophy of state securities regulation is generally considered to differ sharply from the federal philosophy of disclosure. The majority of state laws grant to their commissioners the power to evaluate the merits of securities which will be offered to the public and the power to prohibit the sale of securities found to be unsafe.⁸ In some respects, the Act continues this philosophy of

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⁶ Certain securities and transactions are exempted from federal regulation. These are important, but a discussion of such exemptions is far beyond the scope of this work. It is to be noted, however, that the anti-fraud provisions of federal regulation apply to every offering of securities.

⁷ This brief account of federal securities practice is based on the writer’s experience and the experience of many attorneys with whom he has been associated. Accord, 11 H. Sowards, Business Organizations §§ 1.01, 1.02 (1974) [hereinafter cited as Sowards].


⁸ Sowards § 1.02 at 1-4. Goodwin also discusses the “merit” standards or substantive inquiry approach of state regulation. Goodwin, supra note 4, at 12-13, 22, 34. Goodwin discusses certain provisions which existed under the prior West Virginia Securities Act. W. Va. Code Ann. §§ 32-1-1 to 32-4-7 (Cum. Supp. 1974). It would not be helpful to attempt to compare the old securities law with the new. It would be an effort to compare apples and oranges. It is sufficient to note that the Act has moved toward (or permits the State Securities Commissioner to move toward) the philosophy of full disclosure and away from the “merit” approach. Nevertheless, state securities regulation still has an important role to play, particu-
state regulation. The State Commissioner of Securities has the power to deny, suspend, or revoke the registration of a security as well as the registration of certain persons dealing in securities. In this way the Commissioner can prohibit or stop a public offering of securities. As will be seen in detail, the Act uses other methods to promote the philosophy of full and fair disclosure. It can be argued that in practice there is not much difference between federal regulation and state regulation under the Act. Although the Securities and Exchange Commission has no express authority to prohibit an offering, only the most foolhardy would go forward in the face of an unanswered deficiency letter. The Act can approximate the federal philosophy of full and fair disclosure and can diminish the rule of substantive inquiry into the merits of offerings if the State Commissioner of Securities exercises the discretion granted him by the Act.

The philosophy of full and fair disclosure appears best to satisfy the two competing goals of securities regulation—on the one hand, such regulation must adequately protect the investing public, and, on the other, it must encourage an economic atmosphere in which imaginative and prosperous businesses can grow. The Act provides the Commissioner with the tools to serve both goals. It is hoped that he will depend more on full and fair disclosure methods and less on "merit" regulation, to accomplish this dual purpose. If careful review is given to the information contained in a registration statement, and this in turn is fully disclosed to the public, there would be no need to wield a slow and heavy-handed bureaucracy since criminal sanctions and civil liability are lurking behind every public offering in this state. There is a point where people, fully informed, can and should be permitted to decide for themselves.

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10 Id. § 32-2-204.
11 The West Virginia State Auditor remains the Commissioner of Securities. Id. § 32-4-406(a) [hereinafter referred to as the Commissioner]. In practice, one of his assistants, as head of the Securities Division, is more intimately involved in securities regulation than is the Auditor himself.
12 See Goodwin, supra note 4, at 34.
13 The writers of Note, Uniform Securities Law, supra note 5, are somewhat critical of the Uniform Act and prefer the merit approach to state securities regulation, but the heavy-handed bureaucracy which they praise seems to this writer both frightening and unnecessary.
Federal and state regulation should be coordinated. The public issue of securities performs a vital function in the national economy, and many issues are offered nationwide. It is in the interests of all to coordinate regulation among the several states, as well as between federal and state agencies whenever possible. To this end the Act promotes federalism. The express policy of the Act is to “effectuate the general purpose to make uniform the law of those states which enact the uniform securities act and to coordinate the interpretation and administration of this chapter with the related federal regulation.”

The Act is divided into four articles. The first prohibits fraudulent and certain other practices; the second provides for the registration of broker-dealers, agents, and investment advisors; the third sets standards for the registration of securities; and the fourth contains the general provisions, including definitions of key terms, the exemption of certain securities and transactions from registration, and provisions for the administration and enforcement of the Act. Each article of the Act will be discussed in turn. This discussion, however, paints with a broad brush the more interesting and important provisions of the Act; it is no substitute for a careful reading of the Act itself.

I. FRAUDULENT AND OTHER PROHIBITED PRACTICES

Under the Act, no person, in connection with the offer, sale, or purchase of a security, may employ any fraudulent device, scheme, or artifice nor engage in any fraudulent act or practice. Moreover, it is unlawful “to make any untrue statement of a material fact or to omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading. . . .” This first section of the Act is essentially the same as the Securities and Exchange Commission’s rule 10b-5, which is, in turn, similar to section 17(a) of the Securities Act of 1933. This is standard anti-fraud

16 Id. § 32-4-401(d).
17 Id. § 32-1-101(2).
language, and there are no exemptions or exceptions from its provisions. The language quoted above that prohibits misstatements and omissions raises interesting implications. First, it is clear from the language that one need not necessarily tell all. There is no obligation to disclose except where some statement constitutes a half-truth. Secondly, the misstatement or omission must relate to a material fact. The concept "material" refers to "those matters as to which an average prudent investor ought reasonably to be informed before purchasing the security registered." Although this definition is adequate for general purposes, it will require specific interpretation when applied to individual cases. Finally, although the prohibition of material misstatements and omissions appears in anti-fraud provisions, which would suggest that the prohibition is limited to cases of willful or knowing misstatements and omissions, the language itself does not preclude a violation based only on negligence. Thus, the very real possibility of negligent violation should make all persons dealing in securities cautious.

The Act applies to offers and sales of securities, and "sale" includes a purported gift of assessable stock, as well as the sale or offer of a warrant or a conversion right. "Security," as defined in the Act, is quite inclusive. However, it does exclude from the

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not apply to the purchase of securities. See Official Comment to § 101, Loss & Cowett, supra note 3, at 250.

Arguably, corporate insiders should have an affirmative duty to disclose all material information within their knowledge. This duty has been said to exist under federal law. Note, Uniform Securities Act, supra note 5, at 194-95.

The General Rules and Regulations promulgated by the West Virginia Commissioner of Securities were so promulgated under the prior act. For a discussion of these regulations, see text accompanying note 105 infra.

The question of liability for negligent misstatements and omissions under federal securities case law is far beyond the scope of this article. Nevertheless, it is important to remember that such negligence has been held to be a basis for liability under federal law. See, e.g., Ellis v. Carter, 291 F.2d 270 (9th Cir. 1961); Trusell v. United Underwriters Ltd., 228 F. Supp. 757 (D. Colo. 1964).

"Security" means any note; stock; treasury stock; bond; debenture; evidence of indebtedness; certificate of interest or participation in any profit-sharing agreement; collateral-trust certificate; preorganization certificate or subscription; transferable share; investment contract; voting-trust certificate; certificate of deposit for a security; certificate of interest or participation in an oil, gas, or mining title or lease or in payments out
definition of security any insurance policy, endowment policy, or annuity contract which provides for periodic or lump sum payments for life or some other specified period. But for the express statutory exclusion, an endowment policy or annuity contract could be considered a "security." The West Virginia Legislature, upon the recommendation of the State Insurance Commissioner, solved the problem in the wiser way. The Insurance Commissioner regulates insurance, which includes endowment policies and annuity contracts, and there seems to be no need to impose duplicative regulation.

The first article of the Act further provides that no person who receives consideration for giving advice regarding securities may employ any fraudulent device, scheme, or artifice, or engage in any fraudulent act or practice. This provision is not limited to an "investment advisor," that is, a person who engages in the business of advising others regarding securities for compensation, but of production under such a title or lease; or, in general, any interest or instrument commonly known as a "security", or any certificate of interest or participation in, temporary or interim certificate for, receipt for, guarantee of, or warrant or right to subscribe to or purchase, any of the foregoing. "Security" does not include any insurance or endowment policy or annuity contract under which an insurance company promises to pay money either in a lump sum or periodically for life or some other specific period.

For the derivation of this definition from federal securities law, see Official Comment to § 401(l), Loss & Cowett, supra note 3, at 350.

This writer is informed that the controversy still rebounds within the Securities and Exchange Commission.

W. VA. CODE ANN. § 32-1-102(a) (Cum. Supp. 1974). See Official Comment to § 102(a), Loss & Cowett, supra note 3, at 252, for the derivation of this provision from federal securities law.


"Investment advisor" means any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing or selling securities, or who, for compensation and as a part of a regular business, issues or promulgates analyses or reports concerning securities. "Investment advisor" does not include (1) a bank, savings institution or trust company; (2) a lawyer, accountant, engineer or teacher whose performance of those services is solely incidental to the practice of his profession; (3) a broker-dealer whose performance of these services is solely incidental to the conduct of his business as a broker-dealer and who receives no special compensation for them; (4) a publisher of any bona fide newspaper, news magazine or business or financial publication of general, regular and paid circulation; (5) a person whose advice, analyses or reports relate only to securities ex-
also applies to any person who receives consideration for giving advice regarding securities. This provision seems desirable, since it is broad enough to include a fly-by-night "advisor" as well as a professional investment advisor as defined in the Act. There are, however, restrictions on an investment advisor. The contract which an investment adviser makes with an individual must provide in writing that the investment advisor shall not be compensated on the basis of a share of the capital gains or appreciation of the client's funds; nor can the contract be assigned without the client's consent.\textsuperscript{27} Compensation, however, may be based on the total value of a fund averaged over a definite period or date. The line between appropriate and inappropriate compensation is a hazy demarcation at best and may require administrative or judicial interpretation before the honest investment advisor can be sure he is following the Act. Furthermore, an investment advisor cannot assume custody of his client's securities or funds if the Commissioner prohibits custody, unless the investment advisor notifies the Commissioner that he has or may have custody.

II. REGISTRATION OF BROKER-DEALERS, AGENTS, AND INVESTMENT ADVISORS

Broker-dealers and agents must register under the Act.\textsuperscript{28} A "broker-dealer" is a person in the business of dealing in securities

\textsuperscript{27} See Official Comment to § 401(f), Loss & Cowett, supra note 3, at 339, for the derivation of this definition from federal securities law.

\textsuperscript{28} See Official Comment to § 402(a)(1); (6) a person who has no place of business in this state if (A) his only clients in this state are other investment advisors, broker-dealers, banks, savings institutions, trust companies, insurance companies, investment companies as defined in the Investment Company Act of 1940, pension or profit-sharing trusts, or other financial institutions or institutional buyers whether acting for themselves or as trustees, or (if) (B) during any period of twelve consecutive months he does not direct business communications into this state in any manner to more than five clients other than those specified in clause (A), whether or not he or any of the persons to whom the communications are directed is then present in this state; or (7) such other persons not within the intent of this paragraph as the commissioner may by rule or order designate.

See Official Comment to § 401(f), Loss & Cowett, supra note 3, at 339, for the derivation of this definition from federal securities law.

\textsuperscript{27} W. Va. CODE ANN. § 32-1-102(b) (Cum. Supp. 1974). See Official Comment to § 102(b), Loss & Cowett, supra note 3, at 254, for the derivation of this provision from federal securities law. "Section 102(b) does not require that the entire contract be in writing. An informal exchange of letters containing the three specific provisions would be sufficient." Id.

for his own account or the account of others. An "agent" is an individual, other than a broker-dealer, who represents an issuer of securities or a broker-dealer in the offer, sale, or purchase of securities. An agent's registration is effective only if he is associated with an issuer or a broker-dealer. An investment advisor must

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29 Id. § 32-4-401(c):

"Broker-dealer" means any person engaged in the business of effecting transactions in securities for the account of others or his own account. "Broker-dealer" does not include (1) an agent, (2) an issuer, (3) a bank, savings institution or trust company; or (4) a person who has no place of business in this state if (A) he effects transactions in this state exclusively with or through (i) the issuers of the securities involved in the transactions, (ii) other broker-dealers, or (iii) banks, savings institutions, trust companies, insurance companies, investment companies as defined in the Investment Company Act of 1940, pension or profit-sharing trusts, or other financial institutions or institutional buyers, whether acting for themselves or as trustees, or (if) (B) during any period of twelve consecutive months he does not direct more than fifteen offers to sell or buy into this state in any manner to persons other than those specified in clause (A), whether or not the offeror or any of the offerees is then present in this state.

30 "Agent" is defined by the Act as:

any individual other than a broker-dealer who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities. "Agent" does not include an individual who represents an issuer in (1) effecting transactions in a security exempted by subdivisions (1), (2), (3), (10), or (11) of Section 402(a), (2) effecting transactions exempted by Section 402(b), or (3) effecting transactions with existing employees, partners or directors of the issuer if no commission or other remuneration is paid or given directly or indirectly for soliciting any person in this State. A partner, officer or director of a broker-dealer or issuer, or a person occupying a similar status or performing similar functions, is an agent only if he otherwise comes within this definition.

Id. § 32-4-401(b).

An "issuer" is defined by the Act as:

any person who issues or proposes to issue any security, except that (1) with respect to certificates of deposit, voting-trust certificates or collateral-trust certificates, or with respect to certificates of interest or shares in an unincorporated investment trust not having a board of directors or persons performing similar functions or of the fixed, restricted management, or unit type, the term "issuer" means the person or persons performing the acts and assuming the duties of depositor or manager pursuant to the provisions of the trust or other agreement or instrument under which the security is issued; and (2) with respect to certificates of interest or participation in oil, gas or mining titles or leases or in payments out of production under such titles or leases, there is not considered to be any "issuer."

Id. § 32-4-401(g). See also Id. § 32-4-401(j).

31 Id. § 32-2-201(b).
also register, unless (1) he is already registered as a broker-dealer, and the Commissioner has not ordered him to refrain from acting as an investment advisor, or (2) his only clients in the state are certain investment companies or insurance companies. All registrations for broker-dealers, agents, and investment advisors expire one year from the effective date unless renewed.

A broker-dealer is not prohibited from assuming custody of his client’s funds or securities; indeed, this is one of his customary functions. Nevertheless, if he is also an investment advisor, he may presumably be prohibited from assuming such custody by the Commissioner. This seems an anomalous result which, hopefully, can be softened by regulation. A broker-dealer, moreover, is not automatically an investment advisor if his advisory services are solely incidental to his broker-dealer business and he receives no special compensation for these services.

The information required to be filed with a registration application of a broker-dealer, agent, or investment advisor is sufficiently inclusive to provide the Commissioner a sound basis for judging the merits of each application. Moreover, the Commissioner is permitted to expand the requirements in certain respects. For example, the Commissioner may, by rule, require minimum capital for broker-dealers and investment advisors and may also require broker-dealers, agents, and investment advisors to post surety bonds up to ten thousand dollars to protect those with whom they deal. This figure seems outrageously low in light of amounts involved in many current transactions, but it nevertheless provides minimal security. The minimal capital and bonding requirements should work hand in hand. Net capital should be substantially larger than the bond required before the bond is excused. As a desirable convenience to applicants, prior approval is not required; that is, registration automatically becomes effective thirty days after the application is filed, provided no denial order has been issued and no proceeding regarding revocation, suspension, or cancellation is pending.

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2 Id. § 32-2-201(c). See also Id. § 32-2-204(b)(5).
21 Id. § 32-2-201(d). The Commissioner can avoid this administrative headache by promulgating a rule staggering registration renewals by calendar months.
24 Id. § 32-1-102(c).
2 Id. § 32-4-401(f)(3).
26 For the derivation of these provisions from federal securities law, see Official Comment to § 202(a), Loss & Cowett, supra note 3, at 261.
Subsequent to registration, every broker-dealer and investment advisor must keep such books, accounts, and other records and file any financial reports that the Commissioner by rule prescribes. These records will be subject to reasonable periodic or special examination by the Commissioner as he "deems necessary or appropriate in the public interest or for the protection of investors." In conducting examinations the Commissioner is encouraged to cooperate with, and seek the cooperation of, other state and federal securities agencies.

The Commissioner may, by order, deny, suspend, or revoke any registration if he finds that such order is in the public interest. The grounds upon which the power may be exercised are numerous: any registration may be denied, revoked, or suspended if the registrant has filed materially incomplete or misleading statements in the application, has willfully violated the Act or a rule thereunder, or has a criminal record or a history of unethical conduct in the securities business. Denial, suspension, or revocation may also be based upon the applicant's, or registrant's, lack of qualification in terms of training, experience, and knowledge of the securities business, but the Commissioner's discretion in this regard is restricted.

The Commissioner may act quickly to protect the public. He may discover, for example, that an applicant or registrant has violated the criminal law in connection with a securities transaction. Under such circumstances, the Commissioner may, by order, postpone or suspend registration pending final determination of any proceeding concerning denial, revocation, or suspension. Subsequently, the applicant or registrant is entitled to a hearing at his request or upon the order of the Commissioner. A registrant under fire cannot gracefully bow out. An application can be withdrawn but not if a revocation or suspension proceeding is pending. No order of denial, revocation, or suspension, except for a summary suspension discussed above, can be entered without notice, an op-

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28 Id. § 32-2-203. With respect to the uniformity between state and federal regulations regarding financial statements, see Official Comment to § 203(b), Loss & Cowett, supra note 3, at 288-69.
30 Cooperation in examination is a common practice among insurance regulators acting through the National Association of Insurance Commissioners.
32 For the derivation of this provision from federal securities law, see Official Comment to § 204(e), Loss & Cowett, supra note 3, at 381-82.
portunity to be heard, and written findings of fact and conclusions of law.

The Act provides the Commissioner with adequate power to protect the public while it protects the right of an individual applicant or registrant to due process. The use of incidental standards for denial, revocation, and suspension is salutary. It prevents unnecessary duplication and retains sufficient administrative discretion to distinguish among the specific grounds and the seriousness of various shortcomings on the part of applicants and registrants.

III. REGISTRATION OF SECURITIES

The anti-fraud provisions of the Act and the methods of registering and supervising persons who customarily deal in securities have been reviewed, and those provisions are important. The heart of securities regulation, however, is regulation of the product, that is, the security. A security offered to the public must be registered regardless of whether a broker-dealer, agent, or investment advisor is registered. No person, including a registered broker-dealer, agent, or investment advisor, may offer or sell any security in West Virginia unless the security is either registered or exempt. Three different methods of registration are provided—registration by notification, which is a simplified procedure for registering quality issues; registration by coordination, which relies heavily on the fact that an issue is concomitantly registered with the Securities and Exchange Commission; and registration by qualification, which constitutes a thorough but lengthy demand for all information that might seem relevant.

A. Registration by Notification

Securities that can be registered by notification include those which meet a single earnings test, that is, any security, other than one with a fixed maturity or a fixed interest or dividend provision, whose issuer and any predecessors have been in continuous opera-


4 Id. § 32-3-302.

4 The Uniform Securities Act did not exclude senior securities from registration by notification. Loss & Cowert, supra note 3, § 302(a)(1), at 284. The West Virginia Legislature may want to reconsider this exclusion in the Act.
tion for at least five years if also (A) there has been no default during the past three fiscal years on any security with a fixed maturity or a fixed interest or dividend provision, and (B) the issuer during the past three fiscal years has had average net earnings of five percent of the aggregate value of its common stock. An issuer is, of course, a person who issues or proposes to issue any security. If the issuer has no outstanding quality securities specified in subdivision (A), then presumably it need satisfy only the requirement of subdivision (B).

The determination of whether the issuer has had average net earnings of five percent of the aggregate value of its common stock involves several factors. First, valuation of the securities is based on the maximum offering price or the market price, whichever is higher, on a day selected by the registrant within thirty days of the date the registration statement is filed. The thirty day period permits a registrant to know whether the notification procedure is available. "Maximum offering price" means the highest price offered to different people at different times. The securities, for example, may be offered to existing stockholders at a price lower than that offered to the public. The use of the maximum offering price as the measure of earnings adds an element of safety for the investing public. If there is no readily determinable market price or cash offering price, then the five percent test is applied to book value on a day, selected by the registrant, within ninety days of the date the registration statement is filed. This alternative covers the case where the securities are exchanged for other securities. Secondly, under the requirement of subdivision (B), if the three year earnings test cannot be satisfied because there have been no outstanding securities during all of the period, the five percent earnings test is applied to all the securities which will be outstanding if all the securities offered are issued. In such case, the method of valuation is the same as that discussed above in connection with previously outstanding securities.

A second class of securities can be registered by notification.

47 The highest price may differ from the highest proposed price referred to in W. Va. Code Ann. § 32-3-303(c)(3) (Cum. Supp. 1974). Nevertheless, it is safer to base the five percent test on the proposed price, since the market may rise while the registration is pending. Official Comment to § 302(a), Loss & Cowett, supra note 3, at 285-86.

48 This could happen where a corporate registrant succeeded less than three years ago to a sole proprietorship or general partnership. Loss & Cowett, supra note 3, at 286.
namely, any security registered for non-issuer\textsuperscript{49} distribution if any such security has been registered previously or was originally issued pursuant to an exemption.\textsuperscript{50}

A registration statement filed pursuant to notification must contain basic information about the issuer, its organization and business, a statement by any non-issuer of his reasons for making the offering, a description of the security, and financial data under certain conditions. These requirements are considerably less than the registration requirements under federal law. The requirements are sufficient, however, for proper State regulation of "quality" securities or those which have been registered previously. Under the Act, a registration statement filed pursuant to notification becomes effective at three p.m. on the first full business day after filing the registration statement, or the last amendment to the registration statement, provided no "stop order" is in effect and no denial, suspension, or revocation proceeding is pending.

Registration by notification, despite complexities in the statutory language, is the simplest method of registration. It will be used most often for intrastate offerings or other offerings exempted from federal regulation.\textsuperscript{51}

\begin{footnotesize}
\textsuperscript{49} "Non-issuer" is defined as a person who sells or offers securities "not directly or indirectly for the benefit of the issuer." W. VA. CODE ANN. § 32-4-401(h) (Cum. Supp. 1974).

\textsuperscript{50} Oil, gas, and mineral interest securities are expressly excluded from the provisions of section 302(a)(2). Therefore, such securities may not be registered by notification as non-issuer distributions; indeed, such securities cannot be registered by notification at all. Oil, gas, and mineral interests securities have no issuer by definition under section 401(g)(2), since it is often difficult to determine the issuer of such securities. If not for their exclusion in section 302(a)(2), such securities would always be eligible for registration by notification under that section as non-issuer distributions if they otherwise qualified. See Official Comment to § 302(a), Loss & Cowert, supra note 3, at 386.

Oil, gas, and mineral interests are, nevertheless, defined as "securities" under section 401(l) and as such are required to be registered. In almost every case, such securities will be registered by qualification. The draftsmen of the Uniform Act felt they solved a complex problem by the exclusive definition of "issuer." Draftsmen's Commentary to § 401(g), Loss & Cowert, supra note 3, at 341-42. It is interesting to note that mineral interests are also regulated by W. VA. CODE ANN. §§ 32A-1-1 to -3 (Cum. Supp. 1974) (dealing with land sales; false advertising) which reenacted former W. VA. CODE ANN. §§ 32-2-1 to -3 (1973 Replacement Volume). Presumably, the Legislature wanted to preserve articles two and four of the former law, but realizing that these provisions did not fit properly into the Uniform Act, the Legislature enacted Chapter 32A with the identical provisions.

\textsuperscript{51} Draftsmen's Commentary to § 302(c), Loss & Cowert, supra note 3, at 289-90.
\end{footnotesize}
B. Registration by Coordination\textsuperscript{52}

Registration by coordination avoids duplication by federal and state agencies. Quite simply, any security for which a registration statement has been filed under the Securities Act of 1933 may be registered by coordination in connection with the same offering. The information required to be filed is essentially the same as that filed with the Securities and Exchange Commission, including the prospectus and any other documents filed with the federal agency as requested by the Commissioner. The registrant must also file all future amendments to the federal prospectus other than an amendment which merely delays the effective date. Such amendments must be filed with the Commissioner within one day after they are forwarded to, or filed with, the Securities and Exchange Commission.

A registration statement filed pursuant to coordination automatically becomes effective when the federal registration statement becomes effective, but there are certain conditions. There must be no "stop order" in effect and no denial, suspension, or revocation proceeding pending under State law. The registration statement must have been on file with the Commissioner for at least ten days, and a statement of the maximum and minimum proposed offering prices and the maximum underwriting discounts and commissions must have been on file for two business days or such shorter period as the Commissioner requires. The remaining conditions are necessarily complicated by an effort to get the price amendment to the Commissioner as quickly as possible. The price amendment is the final federal amendment and includes the offering price and matters dependent upon it. The price amendment is customarily agreed upon the evening before, or early morning of, the offering. Until that time there is no firm underwriting contract.

Accordingly, the Act permits the registrant to notify the Commissioner of the price amendment and effective date of registration by telephone or telegram, followed by filing any post-effective amendment relating to the price amendment. If this is not done timely, the Commissioner may enter a "stop order." Moreover, failure to comply can lead to civil liability under the Act. The registrant need not wait until the last minute; he may exercise his option to notify the Commissioner of the date when the final federal amendment is expected to become effective. Use of this option

\textsuperscript{52} W. VA. CODE ANN. § 32-3-303 (Cum. Supp. 1974).
will enable counsel of the issuer or underwriters to feel more secure in his final opinion.

Registration by coordination is to be applauded. A federal registration statement contains at least as much material information as that required by the Act under any of the three methods of registration. It thus provides the Commissioner with ample information to evaluate the offering and protect the investing public in West Virginia. Without coordination, a simultaneous nationwide offering would be practically impossible.

C. Registration by Qualification

The third method of registration is registration by qualification, and it may be called the long term method. Any security may be registered by qualification whether or not one, or both, of the other methods of registration is available. Qualification, however, will usually be a third choice, for no less than seventeen separate items of information must be filed with a registration by qualification. These include: basic information about the issuer, its organization and business, and the general competitive conditions in the industry; information concerning each of its officers and directors, particularly the amount of the issuer's securities held by each, the amount each intends to purchase through the offering, all material transactions between each officer and director and the issuer within the past three years, and the remuneration paid to each by the issuer in the past year; substantially the same information regarding any person owning ten percent or more of the outstanding shares of any class of equity security of the issuer, any promoter, if the issuer was organized within the past three years, or any person on whose behalf any part of the offering will be made through a non-issuer distribution; a statement of capitalization and long term debt, a description of outstanding securities and the consideration received for any securities issued within the past two years; information concerning the securities to be offered, including the price, commissions, and underwriting date; the estimated cash proceeds from the offering and the purpose for which they will be used; a description of any stock options; material contracts and pending litigation; prospectuses and sales literature to be used in connection with the offering; a specimen of the security to be offered; articles of incorporation, by-laws, and trust indentures; an opinion of counsel; consents of experts; financial statements; and

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any other information that the Commissioner requires by rule or order. The list is long. It could easily be as exhaustive as the material required by the Securities and Exchange Commission for a federal registration. The degree of specificity, however, should lead to an early adoption of a uniform registration form by the Commissioner, thus reducing the number of necessary administrative rules.

A registration statement filed pursuant to qualification becomes effective when the Commissioner so orders. Hopefully, the Commissioner will have the staff necessary to process such registrations adequately and swiftly. The Commissioner may require a prospectus containing any or all of the information described above to be given to each person to whom an offer is made. If the Commissioner takes advantage of this power, he can steer the Act toward disclosure and away from substantive inquiry. If the prospectus is reviewed by the Commissioner and given to all offerees, it seems duplicative to inquire further into the substance of an offer. Surely people, given all material information in connection with an offering, are capable of protecting themselves. If the material information is false or misleading, then remedies at law are apply provided.

D. Provisions Applicable to Registration Generally

A registration statement may be filed by the issuer, in the case of non-issuer distributions, by any person on whose behalf the offering is made, or by any broker-dealer who is registered under the Act. Thus, since a local broker-dealer can file a registration statement on his own, the issuer or underwriter is prevented from vetoing an offering or refusing to make a market in the State by choosing not to register. The effect could be far-reaching, particularly where registration is by coordination, and this could lead to additional offerings being made within the State. The fee for registering securities is one-twentieth of one percent of the maximum aggregate offering price, but this fee may not exceed fifteen hundred dollars.

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54 A prospectus is presently required to be given to each offeree by section five of the General Rules and Regulations of the West Virginia Commissioner of Securities. But see discussion accompanying note 113, infra.
56 For example, in a ten million dollar offering, one-twentieth of one percent would be five thousand dollars. The registration fee, however, would be fifteen hundred dollars.
In addition to the information required under the various methods of registration, certain information is required regardless of the method. Every registration statement must contain the amount of securities offered in this State, a list of other states where the registration statement has been or will be filed, and a recitation of any adverse action in connection with the offering taken by any court or any state or federal regulator.\footnote{W. VA. CODE ANN. § 32-3-305(c) (Cum. Supp. 1974). In addition to these requirements, each applicant, regardless of the registration method used, must file a consent to service of process pursuant to id. § 32-4-414(g).}

Documents filed within the past five years may be incorporated by reference in the registration statement, and the Commissioner has the discretion to permit the omission of any information from the registration statement. As experience is gained under the Act, the Commissioner may well discover that not all of the detailed information and documentation, particularly in the case of coordination, is necessary in every instance. In the case of non-issuer distributions, much of the information regarding the issuer need not be filed unless it can be furnished without unreasonable effort or expense.\footnote{This exception is limited to registration by qualification and to reports filed pursuant to W. VA. CODE ANN. § 32-3-305(j) (Cum. Supp. 1974). It is not applicable to registration by notification.} This, for example, will enable a five percent stockholder to sell his shares even if management refuses to provide him with information that the Commissioner might wish to review.\footnote{Draftsmen's Commentary to § 305(i), § 305(j) and Related Sections Referring to Non-Issuer Distributions, Loss & Cowert, supra note 3, at 316.}

In cases of registration by coordination or qualification, the Commissioner may escrow securities and impound the proceeds from the sale where the securities are issued to a promoter for consideration substantially different from the public offering price or to any person for consideration other than cash. The proceeds will be released when the issuer receives a specified amount from the sale. In cases of coordination and qualification the Commissioner may specify the form of subscription or sale contract.

Every registration statement is effective for one year or for a longer period if the security continues to be offered. This is in part an effort to deal with secondary offerings, that is, situations where one who purchased the security in the primary offering from the issuer now wishes to sell to others. For the first year after registration becomes effective, the security is registered for the purpose of
such non-issuer transactions. All securities of the same class may be traded by any person as if they were registered, but if the registration statement is no longer effective, and there is no exemption, the non-issuer distribution must be registered.\textsuperscript{60} Registration cannot be withdrawn for one year from its effective date if any of the same class of securities are outstanding. As long as the registration statement is effective, the Commissioner may require reports, an update of the information in the registration statement, and a statement of the progress of the offering.

E. Denial, Suspension, and Revocation of Registration\textsuperscript{61}

The Commissioner may suspend or revoke the effectiveness of any registration statement, if he finds that such order is in the public interest and any one among nine separate disjunctive grounds exists. These grounds include situations where the registration statement \textit{as of its effective date}, but not thereafter, or any report is incomplete in any material respect or contains a materially false or misleading statement.\textsuperscript{62} Additional grounds include when: there is a willful violation of the Act or any rule or order; there is a stop order or similar order or injunction in effect from any court or federal or state regulator, if such order is based on facts which would support a stop order under the Act; the issuer's business activities are unlawful where performed; the offering is fraudulent; there are unreasonable commissions, discounts, or other compensation or amounts or kinds of options; under registration by coordination, there has been a failure to forward amendments to the federal prospectus, or the proper filing fee has not been paid.

The Commissioner may, by order, summarily postpone or suspend the effectiveness of any registration statement pending final determination of a denial, suspension, or revocation proceeding. Upon the entry of such order, he must give notice to the applicant or registrant, the issuer, and the person on whose behalf the securities are offered. Upon written request by any of these persons, the matter must be set for a hearing. No other stop order may be entered until such notice is given, there is an opportunity for a hearing, and there are written findings of fact and conclusions of

\textsuperscript{60} \textit{Id.} at 316, 320-22.


\textsuperscript{62} Material omissions are not expressly prohibited by \textit{W. Va. Code Ann.} § 32-3-306(a)(A) (Cum. Supp. 1974), in either the official or State versions of the Act. Presumably, this was an oversight.
The Commissioner may vacate or modify any stop order upon a finding of changed conditions or public interest.

IV. SECURITIES AND TRANSACTIONS WHICH ARE EXEMPTED FROM REGISTRATION

Certain kinds of securities in and of themselves are exempted from registration. Other securities, although not exempt by their nature, are exempt from registration because of the kind of transaction involved. Thus, certain securities are exempt regardless of the type of transaction by which they are sold, and certain transactions are exempt regardless of the kind of security involved.

A. Exempt Securities

Twelve types of securities are exempted from registration. In light of the fact that "security" is defined broadly, these exemptions are important. Some are easily predictable. For example, securities issued or guaranteed by federal, state, or local governments, as well as those of friendly foreign governments, are exempted. So are securities issued or guaranteed by federal or state banks, savings institutions, and trust companies. The same is true of securities issued or guaranteed by federal savings and loan associations, state building and loan associations, if authorized to do business in this State, insurance companies organized and authorized to do business in this State, federal credit unions, state credit unions and industrial loan associations organized and supervised under the laws of this State, federally or state regulated railroads, other common carriers, public utilities, and holding companies. These exemptions are based on regulation of the issuer by agencies other than the Commissioner rather than upon issuance of the security, thus avoiding regulatory duplication.

There are other types of exempted securities. Securities listed on the New York, American, Midwest, and regional stock ex-

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64 "Guaranteed" means guaranteed as to payment of principal, interest or dividends." Id. § 32-4-401(e).
changes are exempted from registration. This exemption also applies to unlisted senior securities of the same corporation. Securities issued by non-profit corporations are exempted. Certain kinds of commercial paper arising out of a current transaction are exempted. So are investment contracts issued in connection with employees’ benefit plans and securities issued by agricultural cooperative associations. The reason for all of these exemptions seems rather obvious and desirable. In each case the public is protected in some other manner without introducing duplicative regulation under State securities administration.

B. Exempt Transactions

Twelve types of transactions are exempted from registration. Any isolated non-issuer transaction is exempted even though it is effected through a broker-dealer. Thus, a private individual may sell his stock in a corporation to another private individual without registering it. Closer questions will arise, however, which may have to be decided by the Commissioner or the courts, and the Act addresses the problem to some extent. Certain non-issuer distributions which are something more than an “isolated transaction” are exempted. For example, any non-issuer distribution effected through a broker-dealer who receives an unsolicited order or offer to buy is an exempted transaction. Any non-issuer distribution of an outstanding security also may be exempted if certain information about the issuer appears in a recognized securities manual, or there has been no recent default regarding a fixed maturity or a fixed interest or dividend provision in the security.

Any transaction of an executor, sheriff, guardian, trustee in bankruptcy, and like persons, together with any transaction constituting a judicial sale, is exempted. So is a transaction by a pledgee, provided the transaction is made without the purpose of evading the Act. Sales to institutional buyers and broker-dealers are exempt, since such purchasers are sophisticated in financial matters and do not need as much protection as the public generally.

One of the most important and useful exemptions relates to offers directed to not more than ten persons in West Virginia and
made during any period of twelve consecutive months. Such trans-
action is exempted provided that (A) the seller reasonably believes
that the purchase is for investment and (B) no compensation is
paid for soliciting the buyer. Thus, a small businessman can safely
raise capital from a few friends or relatives. Moreover, the Com-
missoner in the exercise of his discretion may increase, or de-
crease, the allowable number of offerees, thus permitting, for ex-
ample, a close corporation that wants to solicit twenty-five friends
or family members for additional capital to do so. The Commis-
sioner may also waive conditions (A) and (B) or further condition
or withdraw this exemption. Thus, this exemption, particularly if
the Commissioner is willing to exercise his discretion, will go far
toward alleviating the difficulties which have existed under earlier
State law concerning the financing of a new enterprise.8

8 Compare Goodwin, supra note 4, at 14 n.15, with W. VA. CODE ANN. § 32-4-
402(b)(9) (Cum. Supp. 1974). Note that under the prior law a similar exemption
applied to fifteen purchasers, whereas the present Act refers to ten offerees.

Goodwin dealt with promoters, a term which is undefined in the Act even
though it is referred to in certain substantive provisions; e.g., W. VA. CODE ANN. §
32-3-304(b)(5) (Cum. Supp. 1974) (regarding amounts paid to promoters), and id.
§ 32-3-305(g) (regarding escrow of securities and the impounding of the proceeds
from the sale).

"Promoter" is defined in section 2(19) of the West Virginia Securities Rules
and Regulations to include:

(a) Any person who, acting alone or in conjunction with one or more
other persons, directly or indirectly takes initiative in founding and or-
ganizing the business or enterprise of an issuer;

(b) Any person who, in conjunction with the founding and organiz-
ing of the business or enterprise of an issuer, directly or indirectly receives
in consideration of services or property, or both services and property, 10
per cent or more of any class of securities. However, a person who received
such securities or proceeds either solely as underwriting commissions or
solely in consideration of property shall not be deemed a promoter within
the meaning of this definition if such person does not otherwise take part
in founding and organizing the enterprise.


Subsequent to Goodwin's article and prior to the Act, the West Virginia securi-
ties law was amended to exempt "[t]ransactions by an issuer not involving any
public offering." W. VA. CODE ANN. § 32-1-4(h) (1972 Replacement Volume). This
change did not solve the problem Goodwin raised. On its face, the equivalent
exemption under the Act [W. VA. CODE ANN. § 32-4-402(b)(9) (Cum. Supp. 1974)]
is more predictable, but it also seems more rigid. The Commissioner, however, has
broad discretion to loosen or tighten the exemption. In exercising this discretion, it
is hoped that the Commissioner will protect only those persons who need protection
and broaden the exemption for sophisticated investors who can look after them-
selves. There is no magic in the number of offerees involved. It is the quality of the
investor which is important, not the quantity. If the Commissioner properly exer-
emtion, properly administered, can open this State to new business and, at the same time, adequately protect the investing public.

There is a further exemption which relates to the "ten persons" exemption. Any offer or sale of preorganization certificates or subscriptions is exempted if no compensation is paid for soliciting the subscriber, if there are no more than ten subscribers, and if no payment is made by any of them. This enables a new business to obtain the subscriptions necessary under general corporation law. The subscribers do not pay until registration is effective, unless some other exemption exists, because the "subscriber exemption" does not by itself excuse registration, it only postpones it.\(^6\)

Any transaction between the issuer and an underwriter, or among underwriters, is exempted. So are transactions involving whole mortgages. Transactions pursuant to an offer to existing security holders of the issuer are exempted, provided no commission, other than a standby commission, is paid for soliciting the security holder, the issuer first files a notice specifying the terms of the offer, and the Commissioner does not disallow the exemption within five days thereafter. It appears that this exemption is available even if part of an issue is offered to persons other than existing shareholders, and even if such shareholders give as consideration something other than stock of the issuer. If so, then the exemption could be quite broad. This provision was included in the Uniform Act to accommodate corporations whose shareholders have preemptive rights.\(^7\) Finally, offers are exempt where registration statements have been filed, both under the Act and federal law, if no stop order is in effect and no adverse proceeding is pending.

C. Exemptions Generally

In specific cases the Commissioner has the power to deny or revoke any exempted transaction, exemptions of securities issued by nonprofit organizations, and those exemptions related to employee benefit plans. The procedures he must follow are essentially the same as those involved in the denial, suspension, or revocation of his discretion, the problem of financing new enterprises, the same problem that troubled Goodwin, can be solved. The solution is also aided by section 402(b)(11), which is discussed immediately following in the text.

\(^6\) Official Comment to § 402(b)(10), Loss & Cowett, supra note 3, at 374.

\(^7\) Draftsmen's Commentary to § 402(b)(11), Loss & Cowett, supra note 3, at 377.
of a registration. A person may avoid a finding of violation of an existing order if he proves he did not know, and in the exercise of reasonable care could not have known, of the order. The burden of proving an exemption or an exception from a definition is on the person claiming it.

One further "exemption" exists which is not contained in section 402(b), and it is important. By definition, "sale" and "offer" exclude corporate mergers, consolidations, reclassifications of securities, reorganizations, and sales of corporate assets in return for securities of another corporation.\(^7\) Thus, such corporate acts are exempt from registration; this approach parallels an exemption granted under the federal securities laws. Moreover, unlike express exemptions, such acts are exempt from the anti-fraud and civil liability provisions contained in the Act. This broad exemption is justified by the existence of other remedies provided by state corporate law and common law.\(^2\)

V. Administration of the Act

In addition to the considerable power and discretion vested in the Commissioner discussed previously, the Commissioner has additional, general means of enforcing the Act, including provisions for criminal penalties and civil liability. All sales and advertising literature addressed to prospective investors must be filed with the Commissioner before it is distributed, unless the transaction is exempted. The literature, however, need not receive his express prior approval.\(^7\) This provision offers some protection to investors while it also prevents an undue burden on the Commissioner and on the individuals promoting the offering. Nevertheless, no statement in any filing or proceeding can be false or misleading in any material respect.\(^7\)

The mere fact that an application for registration or a registration statement has been filed or that a person is effectively registered does not constitute a finding by the Commissioner that any such statement is true, complete, and not misleading. No such

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\(^2\) Draftsmen's Commentary to § 401(j), Loss & Cowett, supra note 3, at 346-48. For example, under the new West Virginia Corporation Act, that becomes effective July 1, 1975, shareholders who dissent from a merger are entitled to have the value of their stock judicially appraised. W. VA. CODE ANN. § 31-1-123(e) (Cum. Supp. 1974).


\(^74\) Id. § 32-4-404.
application or filing means that the Commissioner has passed in any way upon the merits of, or given approval to, any security, person, or transaction. The same is true regarding exemptions and exceptions. This disclaimer reflects the approach of the Securities and Exchange Commission and, in the final analysis, puts the public on notice to look after itself. There is nothing wrong with this approach provided the Commissioner exercises his discretion to insure that full disclosure to the public has been made. On the other hand, if the Commissioner insists on substantively evaluating the merits of each and every offering, then the disclaimer seems unfair. Such evaluation could mislead the public to rely upon the Commissioner's final action notwithstanding his disclaimer. The Act encourages the disclosure approach, despite occasional disclaimers by the official draftsmen and further provides that no representation inconsistent with the Commissioner's disclaimers can be made to any prospective purchaser.

Neither the Commissioner nor any member of his staff may use for personal benefit any information on file which has not been made public. Whether such information must be disclosed under a subpoena is left to the general procedural law of the State. The Commissioner may conduct investigations regarding potential violations of the Act or any rule or order thereunder. He may do so inside or outside of the State and may require written statements under oath in connection with the investigation. Any person who refuses to respond to a subpoena from the Commissioner may be brought to court, and his continued failure to comply can result in a contempt citation. No witness before the Commissioner may refuse to respond on the ground of self-incrimination, but if he claims the privilege he may not thereafter be prosecuted on the basis of such evidence, other than for perjury or contempt. The Act cannot grant immunity from federal prosecution, however, and it remains to be seen whether this provision of the Act runs afoul of state or federal rights against self-incrimination.

\[\text{Id. § 32-4-405(a).}\]
\[\text{The insurance Commissioner, for example, who regulates the insurance industry through a substantive approach, cannot disclaim his approval of rates or forms. There is no apparent reason why the Commissioner should be allowed to evaluate the securities, in effect approve them, and then disclaim his action.}\]
\[\text{Id. § 32-4-407.}\]
\[\text{Official Comment to § 407, Loss & Cowett, supra note 3, at 385; Draftsmen’s Commentary to § 407, Loss & Cowett, supra note 3, at 386.}\]
The Commissioner is empowered to institute judicial proceedings to obtain an injunction if it appears to him that a violation of the Act or any rule or order thereunder has occurred or is imminent. The Act also provides for criminal penalties. A willful violation can result in a fine of not more than five thousand dollars or imprisonment for not less than one nor more than three years, or both fine and imprisonment. The statute of limitations for returning a criminal indictment for violation of the Act is five years from the date of the alleged violation. No person may be imprisoned for violating a rule or order of which he proves he had no knowledge.

The provisions for civil liability, however, may have more impact in the prevention of violations of the Act, than will provisions imposing criminal penalties. Civil liability may arise when any person offers or sells a security in violation of any one of seven separate sections, including those providing for the registration of broker-dealers and agents, the registration of non-exempt securities, and the filing of sales and advertising literature. Civil liability may also arise if a person makes a statement to a prospective purchaser inconsistent with the Commissioner’s disclaimers of approval of filings and registrations, fails to provide an offeree with a prospectus after having been directed to do so, fails to escrow securities when directed to do so, or fails to use a specified form of subscription of sale contract. Five of these seven express prohibitions relate to disclosure requirements.

In addition to these express provisions, civil liability may arise if any person

offers or sells a security by means of any untrue statement of a material fact or any omission to state a material fact necessary in order to make the statements made, in light of the circumstances under which they are made, not misleading (the buyer not knowing of the untruth or omission), and who does not sustain the burden of proof that he did not know, and in the exercise of reasonable care could not have known, of the untruth or omission. . . .

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81 Id. § 32-4-409.
82 The Securities Act of 1933 provides for a fine of five thousand dollars or imprisonment for not more than five years, or both. 15 U.S.C. § 77x (1970).
83 W. VA. CODE ANN. § 32-4-410(a)(1) (Cum. Supp. 1974). The seven sections are: § 201(a); § 301; § 304(d); § 305(g); § 305(h); § 403; § 405(b).
The phrase "by means of" is unclear. Need the buyer have relied on the untrue statement or omission, or must he show only that he did not know of it? The draftsmen intended the latter, and their interpretation is supported by the parenthetical statement quoted above. A more interesting question, perhaps, is whether a violation of the provision can result in civil liability based on a negligent misstatement or omission rather than strictly a willful misstatement or omission.

Civil liability also rests, jointly and severally, upon any person who controls the seller, every partner, officer, or director of the seller, and every employee or broker-dealer who materially aids in the sale, unless such person can prove that "he did not know, and in the exercise of reasonable care could not have known, of the existence of the facts by reason of which the liability is alleged to exist."

In the event of a violation of the provisions giving rise to civil liability, the buyer may tender the security and recover the purchase price, together with interest at nine percent annually from the date of payment, costs, and reasonable attorney's fees. Tender may be made at any time prior to entry of judgement. The buyer, however, need not tender the security. If he has sold it before learning of the misstatement or omission, he can recover as damages the difference between the price at which he bought and sold it, plus interest at nine percent annually. The statute of limitations for commencement of a civil action under the Act is three years from the date of sale. No person who enters a contract in violation of the Act may base a suit upon that contract if he knew the facts which constituted the violation. No person may waive compliance with any provision of the Act or any rule or order thereunder. Thus, the unsophisticated investor is protected against himself.

The Act creates a cause of action only with regard to sections 410 and 202(e), the latter relating to bonds posted by broker-dealers, agents, and investment advisors. The draftsmen of the
Uniform Act believe that no civil cause of action could be created by the general anti-fraud provisions as has been done under federal law. Presumably, however, one can recover under a common law action based on fraud in violation of article one.

The Act provides for judicial review of final orders of the Commissioner, who, presumably, is also subject to the State Administrative Procedures Act. Similarly, the Act establishes rule making procedures which are also apparently governed by the State Administrative Procedures Act. The Act, however, gives the Commissioner one important power not granted by the Administrative Procedures Act. He may prescribe the form and content of required financial statements, the circumstances under which consolidated financial statements have to be filed, and whether financial statements must be certified by independent or certified public accountants. The Commissioner cannot, however, make or amend rules, forms, or orders unless he finds that such action "is necessary or appropriate in the public interest or for the protection of investors and consistent with the purposes fairly intended by the policy and provisions" of the Act. It is also pleasing to note that throughout the Act the Commissioner's power to act is conditioned

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upon the prescription that he do so openly, "by rule or order." This will avoid, to some extent, the regulation by silence which pervades so many administrative agencies.

It is important to note that no liability of any kind arises when a person acts in good faith in conformity with a rule, form, or order of the Commissioner even though such prescription is subsequently rescinded, amended, or determined to be invalid. This protection, however, is not extended to reliance upon interpretive opinions of the Commissioner, which seems unfortunate despite the draftsmen's desire to encourage the Commissioner to render such opinions. It seems unfair to fail to protect reliance upon an official opinion even though it does not rise through procedural magic to the status of a rule. There is no room for contrary interpretation of these statutory provisions, however; if this is to be corrected, it must be done by the Legislature.

The Act applies only to transactions that occur in West Virginia. The Act offers some guidance as to what transactions have occurred in this State. For example, an offer to buy or sell in the form of advertisements which are essentially national, such as those appearing in nationwide periodicals or on nationwide radio and television, is not an offer made in West Virginia by express provision in the Act. Other, close questions, will arise, however, that will have to be determined administratively or judicially. Certainly, offers, sales, and purchases can be made in the State even though one or more persons involved are not physically present within the State, but the surrounding circumstances will not always be clear.

The Act attempts to coordinate securities regulation among the several states and between state and federal agencies wherever possible. Thus, the express policy of the Act with regard to construction is to make the Act uniform in all states which enact it and to interpret it consistently with related federal regulation. This policy constitutes yet another clue to the philosophy of the Act—that regulation should move away from old concepts of substantive inquiry toward the approach of full disclosure. As has been seen, the Commissioner can make strides in this direction

\[\text{id § 32-4-412(e).}\\
\text{Draftsmen's Commentary to § 412, Loss & Cowett, supra note 3, at 399.}\\
\text{id § 32-3-304.}\\
\]
by requiring a prospectus to be given to offerees pursuant to section 304(d). There appears to be no reason why the Commissioner could not impose similar requirements regarding registration by notification and coordination under his general rule-making power.

VI. Administration in Fact

The Commissioner has considerable power and discretion regarding the registration and regulation of securities and the persons intimately involved in securities transactions. Although the old regulations are "proposed to be readopted" pursuant to the Act, such regulations for the most part, simply will not do the job required by the Act. Several of the definitions seem unnecessary or meaningless in light of the Act. For example, the term "certified" regarding financial statements in no way elaborates upon the Commissioner's power to require such financials, nor do the regulations prescribe when and under what circumstances such financials are required. "Equity security" is a much narrower definition than that of "security" in the Act. "Fraud" is in no way defined, rather the purported definition in the regulations merely repeats the language of the first section of the Act. The definition of a trust as a "person" differs between the regulations and the Act. "Prospectus" refers to "Section 2 of the Act," but there is no Section two. Section three of the regulations defines and gives examples of acts or omissions which "tend to work a fraud upon the investor" and are usually "unfair" and "detrimental to the interests of investors or prospective investors." These words and phrases belong to an older rubric of regulation. They do not fit the scheme of the Act and do not exhibit any sympathy whatsoever for the philosophy of disclosure. Section four, dealing with registration of securities, does not set forth requirements relating to the three separate statutory methods of registration, and certain provisions of this regulation may tend to conflict with the requirements re-

103 W. Va. Sec. Regs. § 1.02 (3 CCH Blue Sky L. Rep. ¶ 51,602 (1964)). Arguably, under the West Virginia Administrative Procedures Act, W. Va. Code Ann. §§ 29A-1-1 to 29A-7-4 (1971 Replacement Volume), the prior regulations would have to be refiled, as well as "readopted."


105 Id. § 2(11) (¶ 51,606).

106 Id. § 2(13).

107 Id. § 2(17).

108 Id. § 2(20).

109 Id. § 2(24).

110 Id. § 3 (¶ 51,607).

111 Id. § 4 (¶ 51,613).
UNIFORM SECURITIES ACT

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garding registration by coordination set forth in the Act. Section five requires that a prospectus be given to each offeree,\textsuperscript{113} which is laudatory, but the statutory reference for such power is "Section 6 of the Act" and there is no such section. There is a serious question whether such regulations can withstand judicial scrutiny. Finally, Section eight of the regulations, dealing with "intrastate over-the-counter transactions,"\textsuperscript{114} contains references to the predecessor statute of the Act, and the regulation speaks of "intrastate dealers" rather than broker-dealers, agents, and investment advisors, who are the key persons under the Act.

Not all of the material in the regulations is redundant or in-applicable. Some of it may be relevant to securities regulation under the Act. No one would suggest that the Commissioner cast his experience to the winds. Moreover, it will take time and new experience to formulate meaningful regulations under the Act. Nevertheless, outdated rules, terms, and statutory references are inappropriate to the new and vital scheme of regulation under the Act. It is hoped that, in time, the Commissioner will promulgate modern, relevant regulations and will not be inclined to sink into the former perspectives of securities regulation.

CONCLUSION

The Act contains new terminology, and its provisions have not yet been construed. It will raise at least as many questions for interpretation as it purports to answer. Some of these issues have been raised in this article, but the basic approach has been simply to explain the Act, not to cover every contingency or subtlety. For example, what is an "isolated" transaction within the meaning of section 402(b)(1)?\textsuperscript{115} In answering this among many questions, the Commissioner and the courts will have to rely on experience, the general purposes of the Act, and such precedents as can be found. Nevertheless, the Act is a step forward in state securities regulation, and West Virginia is helped to have it. If the philosophy of full and fair disclosure is pursued vigorously, public investors can be adequately protected without creating an excessive bureaucracy which so often stifles new and imaginative enterprises. This will

\begin{footnotesize}
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\item \textsuperscript{113} Id. § 5 (¶ 51,614).
\item \textsuperscript{114} Id. § 8 (¶ 51,617).
\item \textsuperscript{115} One work devoted ten pages to this point alone. Note, Uniform Securities Act, supra note 5, at 136-46. A separate article could be written on each of innumerable questions.
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depend upon the Commissioner and members of the bar who practice before him. Ultimately, the Act, like most laws, will be only as effective as those who administer it.