



STATE OF CONNECTICUT
DEPARTMENT OF BANKING

STATE OFFICE BUILDING • HARTFORD, CT 06106



BRIAN J. WOOLF
COMMISSIONER

SECURITIES AND BUSINESS INVESTMENTS DIVISION
BULLETIN

HOWARD B. BROWN
DEPUTY COMMISSIONER

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CALEB L. NICHOLS
DIVISION DIRECTOR
(203) 566-4560

CYNTHIA ANTANAITIS
ASSISTANT COUNSEL
(203) 566-5717

RALPH A. LAMBIASE
DIRECTOR OF
ENFORCEMENT
(203) 566-4560

MARYELLEN MEARA
EXAMINER III
BROKER-DEALERS
INVESTMENT-ADVISERS
(203) 566-4257

MARGOT T. O'GRADY
EXAMINER II
SECURITIES
REGISTRATIONS
(203) 566-5783

BANKING COMMISSIONER'S COMMENTS

The 1983 calendar year was marked by several significant accomplishments of the Securities and Business Investments Division of the Department of Banking.

Substantial emphasis was placed upon the investigation of tax shelter abuses and violations of the Connecticut Uniform Securities Act and the Connecticut Business Opportunity Act. In connection with stepped up enforcement efforts, the Division has planned a Joint Enforcement Training Program featuring Securities and Business Investments Division participants from the Securities and Exchange Commission, the National Association of Securities Dealers and other states. The program is scheduled for February, 1984. A major effort is underway to implement an in-house training program which will hopefully complement the Joint Enforcement Training Program.

The implementation of the Central Registration Depository System in 1983 and the addition of an Electriever System greatly enhanced the overall operational efficiency of the Division.

I should also mention that there has been an appreciable increase in both public and private placement offerings in 1983. It is expected that this trend will continue into 1984.

I am impressed with the feedback that was received as a result of the publication of the first edition of this Bulletin. I continue to welcome your comments and suggestions.

In this issue, two brief articles have been submitted for publication. The first article was submitted by Robert B. Titus, Esq. of the law firm of Day, Berry and Howard. Mr. Titus also serves as the Chairman of the Banking Commissioner's Ad Hoc Advisory Committee on securities. The second article was submitted by Harold B. Finn, Esq. of the law firm of Cummings and Lockwood. Mr. Finn also serves on the Banking Commissioner's Ad Hoc Advisory Committee on securities.

It is my hope that this Bulletin will continue to be a vital information source to all interested parties.



Brian J. Woolf
Banking Commissioner

ANNOUNCEMENTS

Personnel Changes

In October, 1983 John P. Walsh joined the Division and was assigned to the Enforcement Section. Mr. Walsh received an undergraduate degree in business and economics from St. Anselms College and an MBA in finance from the University of Hartford. Prior to his employment with the Division, Mr. Walsh was employed by the State of Connecticut Department of Revenue as a field examiner.

In November, 1983 Paula Boivin joined the Division and was assigned to the Securities Registration Section of the Division. Ms. Boivin received an undergraduate degree in finance from the University of Connecticut. Prior to her employment with the Division, Ms. Boivin was a Claims Representative with the Hartford Insurance Group.

In December, 1983 Jeffrey Goodson joined the Division on a full time basis. Mr. Goodson has been assigned to the Broker-Dealer Registration Section. Mr. Goodson had been working in the Division on a part-time basis for four years while attending the University of Connecticut and pursuing an undergraduate degree in accounting.

ADVISORY COMMITTEE ACTIVITIES

by Robert B. Titus*

Many persons may not be aware that the Banking Commissioner has had, since 1979, an Advisory Committee to advise him with respect to the Connecticut Uniform Securities Act. The Advisory Committee is intended to provide the Banking Commissioner and his staff with a forum where legislative and regulatory proposals may be reviewed and where problems which the Securities and Business Investments Division has encountered in enforcement, interpretation or otherwise may be discussed. The objective is to afford the Commissioner and his staff with the benefit of various perspectives from representatives of the securities industry and legal practitioners.

In 1984, a number of interesting issues may come to the attention of the Advisory Committee. One activity will involve reviewing how well the comprehensive revision of the securities regulations adopted earlier in 1983 by the Banking Commissioner is working and whether any further action or clarification appears warranted. The Committee also expects to be asked to review some of the more significant legislative proposals the Commissioner will submit to the Legislature in the securities area.

A particularly timely area of interest relates to the increasing securities activities of banking institutions - whether carried on through affiliates or by contract with independent broker-dealers - and the possible need for some form of regulatory action.

Finally, I should note that there is considerable discussion currently on the national level as to both the need to update at least parts of the Uniform Securities Act and the proper relationship between the federal securities laws and the Uniform Securities Act. The Advisory Committee intends to keep abreast of developments in this area.

Persons serving as members of the Advisory Committee for the present year are the following: Steven Bartelstone (Hartford), William H. Cuddy (Hartford), Harold B. Finn (Stamford), George N. Gingold (Hartford), Joel Hartstone (Hartford), Dane Kostin (West Hartford), Lee G. Kuckro (Hartford), Willard F. Pinney (Hartford), Richard L. Rose (Stamford), and Nicholas Wolfson (Professor, University of Connecticut School of Law).

*Mr. Titus is Chairman of the Banking Commissioner's Advisory Committee on Securities and is a partner in the Hartford law firm of Day, Berry & Howard from which he has taken a sabbatical leave to teach at Western New England College of Law in Springfield, Massachusetts.

SUBCOMMITTEE ESTABLISHED TO DEFINE
"COMMISSIONS, DISCOUNTS AND OTHER SIMILAR REMUNERATION"
by Bill Finn*

The Advisory Committee to the Banking Commissioner has established a subcommittee for the purpose of advising the Banking Commissioner as to the intended scope of the phrase "commissions, discounts and other similar remuneration" as used in the provisions of the Connecticut Uniform Securities Act and the regulations promulgated thereunder relating to private placements and other limited offering transactions.

The definition of the phrase "commissions, discounts and other similar remuneration" is of critical importance in determining the availability of an exemption from the registration requirements of the Connecticut Uniform Securities Act. In particular under the new regulations promulgated under Section 36-490(b)(9) of the Connecticut General Statutes, neither a private placement exemption nor an exemption otherwise afforded under the State's counterpart of Regulation D, 17 C.F.R. §§230.501 et seq., will be available if the "commissions, discounts and other similar remuneration paid or given directly or indirectly in connection with the sale" exceed, in the aggregate, 15% of the initial offering price unless a statement itemizing such payments is filed with the Banking Commissioner

prior to the first sale in Connecticut and given to each purchaser in Connecticut prior to a sale to such purchaser. (Regulation 36-500-22(b)(9)(C)). Similarly, the availability of the limited offering exemption afforded by Section 36-490(b)(14) of the Connecticut General Statutes, where the total number of purchasers of all securities of the issuer does not exceed ten, is conditioned upon compliance with the requirement that "no commission, discount or other remuneration [be] paid or given directly or indirectly in connection with the offer and sale . . ."

In order to define the phrase "commissions, discounts and other similar remuneration", one must first seek to ascertain the underlying purpose of the statutory and regulatory provisions requiring disclosure of or prohibiting receipt of such payments. Unfortunately, it is not clear whether such provisions are intended to limit the promotion of the offering by persons other than the issuer or to curtail untoward diversion of the proceeds of the offering, and it is even possible that one or both of such provisions were intended to serve both such purposes. In the forthcoming weeks, the subcommittee of the Advisory Committee, working with the Securities and Business Investments Division, will complete its analysis of the purposes of these provisions and, based on such analysis, will attempt to articulate one or more definitions of the phrase "commissions, discounts and other [similar] remuneration".

*Mr. Finn is a member of the Banking Commissioner's Advisory Committee on Securities and a partner in the law firm of Cummings and Lockwood, Stamford, Connecticut.

ENFORCEMENT AND EXAMINATION SECTION

Investor Alert Warns Of Questionable Tax Shelters

On November 8, 1983, the Connecticut Department of Banking released an Investor Alert which focuses on questionable and fraudulent tax shelters. Brian J. Woolf, Banking Commissioner, stated that, "The last quarter of the year is the time people are searching for tax shelters. The Department's Securities and Business Investments Division sometimes receives complaints about tax write-off plans that promise four to eight times one's investment in tax savings in the first year. Some of these plans may be outright frauds which may be disallowed as tax deductions if the investors are audited by the Internal Revenue Service. If investors choose tax shelters that are disallowed, they may be penalized in four ways: (1) they may lose expected tax deductions; (2) have to pay IRS interest and penalties; (3) lose their cash investment, and (4) be liable to make payments on loans that were part of the scheme."

Typically, promoters of fraudulent tax shelters advertise in local and national newspapers or send ads through the mail. They may hold seminars or use high pressure telephone sales techniques that stress the great tax advantages of their plans. Hardly ever mentioned is the likelihood of making any money from the investment itself.

Commissioner Woolf cautioned "anyone trying to save on taxes through investments in tax shelters to look first at the underlying economics of the offer. If it does not seem likely that one could make money, regardless of the tax write-off possibilities, this should be a warning sign to avoid the deal. If the underlying economics of the deal are unsound, the investor cannot profit solely from tax losses; you cannot make money by losing money."

The Alert detailed the problems attendant to investing in questionable ventures and set out questions potential investors should ask before signing up in tax shelter plans. Abusive tax shelters are usually entered into with no expectation of a positive financial outcome, but rather with the sole expectation of avoiding taxes. Such tax shelters often involve movies, master recording tapes, lithographs, books, gold and precious metal mining ventures. In some instances, real estate ventures and oil and gas exploration ventures which have exorbitant write-offs are also candidates for investor scrutiny.

Recently, the IRS described as abusive tax shelter plans involving the leasing of master recordings overvalued by promoters at 100 times their costs, and promised investors tax write-offs not only in the future, but for prior years. Another plan the IRS has labeled abusive involved overvaluation of art works that may be donated to charitable organizations that led to 100% returns for some taxpayers and included fictitious dates of purchase and donation.

Commonly, the sales promoters will make representations stressing the tax advantages of investing in the program, but they usually fail to tell investors:

- (1) all the tax consequences of the investment, particularly what are known as the "at risk" rules of the Internal Revenue Service. These rules are complicated and in many cases investors cannot write off their taxes more than they actually invested in cash;
- (2) that the value placed on the property by the promoters or sold to investors in the project is substantially in excess of its true fair market value; or that no real market exists for the property or project and that the marketing agent has no real intention of trying to develop it;
- (3) the length of time the company has been in business and the kind of record it has in similar tax shelter programs;
- (4) whether there has been an appraisal made of the property;
Note: Make sure that the appraisal is by an independent third party. If no appraisal has been made, ask for one, and do not invest until it is obtained;

- (5) whether tax counsel has been retained, and whether there has been a tax opinion issued (if so, the Alert advised investors to ask for a copy and if not, to not invest until such representation is obtained);
- (6) how the property is to be developed; whether the marketing company is related to the promoter of the packages; Sometimes this could indicate a conflict of interest which would be closely scrutinized by the IRS. Also, in some questionable shelter programs, the marketing company is merely a sham;
- (7) whether the tax shelter program is registered with a governmental securities agency; and whether the promoters and salesmen are licensed as securities dealers and salesmen.

"Perhaps the best advice that could be given," said Commissioner Woolf, "is not to be pressured into an early purchase of the tax shelter program by promises of tax advantages and the fact that the year end is approaching." Commissioner Woolf further advised investors to "ask for all documentation, and, if you are not knowledgeable in the particular area, consult an independent tax attorney or CPA to get an opinion as to the propriety of the investment."

Cease and Desist Orders Issued

On December 12, 1983 an order to Cease & Desist was issued against Bruce Kirk, President of International Voice Machine Corporation, c/o Brielle Computer, Inc., Fountain 9 Mall, Highway 35, Sea Girt, NJ 08750. It is alleged that Mr. Kirk sold securities of International Voice Machine Corporation without prior registration of the securities.

On October 13, 1983 an order to Cease & Desist was issued against James J. Reid, President of Investment Notes Research Group, Inc., 230 East Main Street, Branford, CT 06405. It was alleged that Mr. Reid was publishing a newsletter and providing investment advice to the public without prior registration.

On August 29, 1983 an order to Cease & Desist was issued against Tony Uricioli a representative of Gourmet Coffee Corporation, 822 Main Street, Poughkeepsie, NY 12603. The order alleges that Mr. Uricioli offered and sold retail coffee distributorships without effecting a business opportunity registration.

Enforcement Statistics

	<u>SECURITIES</u>			<u>BUSINESS OPPORTUNITIES</u>		
	<u>1982</u>	<u>1983</u>	<u>Percentage Increase (Decrease)</u>	<u>1982</u>	<u>1983</u>	<u>Percentage Increase (Decrease)</u>
Investigations Opened	64	188	194%	7	11	57%
Investigations Closed	52	117	125%	6	13	117%
Complaints Processed	113	231	104%	24	4	(83%)
Cease and Desist Orders Issued	9	7	(22%)	1	5	400%
Show Cause Orders Issued	21	17	(19%)	0	1	100%
Revocation Orders Issued Broker-Dealer	3	0	-	NA	NA	-
Denial Orders Issued Broker-Dealer	1	0	-	NA	NA	-
Subpoenas Issued	17	11	(35%)	1	2	100%
Referrals for Criminal Action	1	1	Unchanged	0	0	-
Investment Advisor Exams Completed	49	4	(92%)	NA	NA	-
Broker-Dealer Exams Completed	67	22	(67%)	NA	NA	-

SECURITIES & BUSINESS
OPPORTUNITY REGISTRATION SECTION

Fees

A total of 4094 securities registration filings were received by the Securities and Business Opportunity Registration Section during the year ending December 31, 1983. 2352 filings of this type were received in 1982. This represents an increase of 1742 or 74% in number of securities registration filings.

The May 26, 1983 amendment to the Connecticut Uniform Securities Act requires non-investment companies to pay a filing fee of one-tenth of one percent of the maximum aggregate offering price of the securities to be offered in this state, such fee not to exceed fifteen hundred dollars nor to be less than three hundred dollars. A three hundred dollar filing fee had previously been required for all securities registration filings.

A fee of twenty-five dollars should accompany any filing for an exemption under Section 36-490(b)(9)(C) of the Act (i.e. offerings exempt under Rules 505 and 506 of Regulation D or under Section 4(2) of the Securities Act of 1933). A total of 3183 exemption filings were received in 1983 compared to 1402 received in 1982. 2191 exemption filings, each accompanied by a fee of twenty-five dollars, have been received since May 26, 1983, the date the filing fee requirement became law (P.A. 83-368).

Inquiries

Persons interested in determining whether a security or business opportunity has been effectively registered or whether a filing has been made in connection with an exemption from registration may telephone Jean Foto at (203) 566-4560 ext. 69. Inquiries regarding registration requirements, the availability of exemptions or exclusions or general inquiries may be directed to the following:

(203) 566-4560

Securities Registrations.....William Olesky or Paula Boivin
Private Placements.....Margot T. O'Grady
Business Opportunities.....Beth J. Briggs

BROKER-DEALER AND INVESTMENT ADVISER REGISTRATION SECTION

How to File a Broker Dealer Application

In filing an application to register a broker dealer, the Uniform BD Form is used as well as a Connecticut Supplemental Packet. Form BD may be obtained from the National Association of Securities Dealers. The Connecticut Supplemental Packet may be obtained from this office. When all the forms have been completed and checked, they should be forwarded to this Department.

Principal Exams If an officer or general partner has not passed a principal exam, a waiver must be requested. A waiver may be grounded on the fact that the person will not be active in the managerial activities of the firm.

Financials Each applicant for registration must file with its application a statement of financial condition as of a date within 60 days of the date on which such statement is filed. The statement of financial condition must be in such detail as will disclose the nature and amount of assets and liabilities and the net worth of the broker-dealer, and contain a computation of his aggregate indebtedness and net capital which shall comply with the requirements applicable to the business of such broker-dealer under Rule 15c3-1 of the Securities Exchange Act of 1934 or under the capital rule of the national securities exchange of which such broker-dealer is or has in good faith filed an application to become a member. A Registrant's Certificate to accompany the financials will be found in the Connecticut packet.

Corporation A Corporate Resolution giving authorization from the board of directors to apply and file the necessary papers for registration is also provided in the Connecticut packet. Corporations should be careful to apply their corporate seal wherever applicable throughout the application.

Fees All broker-dealer applications should be accompanied by an initial registration fee of \$250 which shall not be refunded.

Form U-4 Only one agent application on Form U-4 should be submitted at the time the broker-dealer application is filed. The agent fee for initial registration is \$50.00. Proof of passing an exam is required.

After reviewing the application for completeness and compliance with the Connecticut Uniform Securities Act, an investigation of the applicant and his affairs will be conducted to determine fitness for registration. Character, experience and financial responsibility will be considered. A registration is not effective until formally entered upon the Register of Broker-Dealers and appropriate notice forwarded to the applicant.

After registration has been granted, NASD-member firms will submit all agent U-4 applications or U-5 termination notices to the Central Registration Depository System. All other firms may submit such forms to this Division.

All registrations, unless sooner revoked or suspended, will expire on December 31st of each year. This department will bill all firms the renewal fee of \$150 on or about November 20. Payment will constitute renewal. Agents will be renewed via the CRD System. Agent renewal fees are \$30.

Questions regarding mergers or successors will be answered on a case-by-case basis by the Broker-Dealer Registration Section.

Staff Responsibilities

Broker-dealer and investment adviser registrations.....Maryellen Meara
 New broker-dealer agent registrations.....Tia Damato
 New investment adviser agent registrations
 and agent of issuer registrations.....Doris Kinsley
 Agent transfers, terminations, reinstatements
 and address changes.....Olympia Thompson
 Financial filings and billing procedures.....Thomas Dolan
 Secretarial support.....Ann Cody

Fee Schedule

Broker-dealer initial registration fee.....\$250
 Investment adviser initial registration fee.....\$250
 Agent initial registration fee.....\$ 50
 Investment adviser agent registration fee.....\$ 50
 Investment adviser agent transfer fee.....\$ 50
 Agent transfer fee.....\$ 50
 Broker-dealer renewal fee.....\$150 per year
 Investment adviser renewal fee.....\$150 per year
 Agent renewal fee.....\$ 30 per year
 Investment adviser agent renewal fee.....\$ 30 per year

Registration Statistics

12/31/83

	<u>12/31/82</u>	<u>12/31/83</u>	<u>Percent Increase/Decrease</u>
Broker Dealers	745	916	23%
Broker Dealer Agents	18,707	22,563	21%
Investment Advisers	214	263	23%
Investment Adviser Agents	775	1,095	41%
Agents of Issuer	241	151	(37%)

The Broker Dealer and Investment Adviser Registration Section handled a large volume of new registrations in 1983.

The number of registered brokerage firms increased by 171 during 1983 as compared to an increase of 98 in 1982.

Investment Adviser firms increased by 49 in 1983 as compared to 14 in the previous year. Broker-dealer agents increased by 3,856 in 1983 as compared to 4,007 in 1982.

Agents of Investment Advisers grew by 320 in 1983 as compared to 57 in 1982. Agents of Issuers decreased in number by 90 in 1983 compared to an increase of 48 in 1982.

LEGAL

Advisory Interpretation Request Procedure

The Securities and Business Investments Division of the Department of Banking is often asked to give advisory interpretations regarding Chapter 662 of the Connecticut General Statutes, The Connecticut Uniform Securities Act, and Chapter 662a of the Connecticut General Statutes, the Connecticut Business Opportunity Investment Act. Employees of the Department of Banking authorized by the Banking Commissioner may issue written advisory interpretations of these chapters.

The Department of Banking is not a substitute for private legal counsel. Therefore, prior to sending a written inquiry to this department, you should review the facts with your counsel. If you and your counsel require the assistance of the Department, you may request that the Department review your situation and issue an advisory interpretation.

When requesting an advisory interpretation the following procedure should be used and will facilitate an expeditious response.

1. State what section of the statute or regulations the request concerns.
2. State the fact situation accurately and include a copy of all relevant documents including offering materials, contracts, etc.
3. State the legal issues presented by your request.
4. Present counsel's analysis of the issues and counsel's conclusions. If counsel has not stated an opinion, provide the Department with your analysis of the issues presented and your conclusions.

The Department is not required to respond to such requests and will not consider requests based on hypothetical facts, past transactions or nameless parties. All parties must be fully identified and the facts stated completely and accurately. Requests for advisory interpretations may require in depth review and therefore, requests involving complex issues should be submitted sufficiently in advance to permit adequate time for review. Expedited treatment is not possible for ambiguous requests.

Advisory interpretations are provided only for the use of the person requesting them. Facts or conditions different from those presented may require different conclusions and persons other than those requesting the opinion or letter should not rely on it.

Requests for advisory interpretations should be directed to:

Caleb Nichols, Director
Securities and Business Investments Division
Department of Banking, Room 229
State Office Building
165 Capitol Avenue
Hartford, CT 06106

or

Cynthia Antanaitis, Assistant Counsel
Department of Banking, Room 225
State Office Building
165 Capitol Avenue
Hartford, CT 06106

Interpretation Issued on Scope of "Bad Boy"
Disqualified Provision Under State Exemption for Regulation D Offerings

On December 8, 1983, the Department of Banking issued an interpretation of Section 36-500-22(b)(9)(C)(ii)(aa) of the Regulations promulgated under Chapter 662 of the Connecticut General Statutes, the Connecticut Uniform Securities Act. Section 36-500-22(b)(9)(C)(ii)(aa) of the Regulations provides that:

No exemption [under Section 36-500-22(b)(9) of the Regulations]... shall be available...if any of the persons listed in subsections (c), (d), (e) or (f) of Section 252 of Regulation A... [h]as been convicted of a felony within five years prior to the commencement

of the offering. This felony conviction must have involved the purchase or sale of a security.

The issue was raised whether the disqualification contained in Section 36-500-22(b)(9)(C)(ii)(aa) of the Regulations extended to all officers of an underwriter involved in the offering of securities exempt under the provisions of Rules 505 and 506 of Regulation D. Noting that, among the persons listed in Section 252(d) of Regulation A are "any underwriter of the securities to be offered, or any... officer of any such underwriter," and that the term "officer" was not defined in Regulation A, the Banking Commissioner determined that the term "officer" was to be confined to a person acting in a managerial or supervisory capacity or performing a policy-making function. Consequently, the disqualifier contained in Section 36-500-22(b)(9)(C)(ii)(aa) of the Regulations would not extend to strictly titular officers of an underwriter who do not assume managerial or supervisory responsibilities.

Amendments to Regulations Promulgated Under the
Connecticut Uniform Securities Act
Effective August 17, 1983

A number of amendments to the Regulations promulgated under the Connecticut Uniform Securities Act have been implemented, effective August 17, 1983.

- 1) Section 36-500-2(f) of the Regulations has been amended to provide a new definition for the term "client" as used in Section 36-471(f) of the Act which defines the term "investment adviser". Previously, this section defined "client" to apply to "each separate billing unit or account." The amendment provides that 1) a husband and wife 2) a child and his parent or guardian 3) a corporation 4) a partnership 5) an association or other unincorporated entity and 6) a joint stock company or trust would be deemed a single client. To be deemed a single client, however, a corporation, partnership, association, unincorporated entity, joint stock company or trust could not be formed for the purpose of purchasing securities or seeking investment advice. Such a business entity, if in existence for more than one year, would presumptively be a single client unless it was originally formed for the purpose of purchasing securities or seeking investment advice. The amendment also provides that business entities in existence for at least 90 days on 9/1/83 which could have reasonably been deemed a single client at the time they were formed are presumed to be a single client.
- 2) Section 36-500-5(b)(2) of the Regulations has been amended to require a broker-dealer to file written notice with the Banking Commissioner within five days whenever 1) it hires an agent transferred from another broker-dealer or 2) an agent leaves its employ. (If employment is terminated for cause, the notice must be filed within twenty-four hours following

