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Allen S. Krakover

SOME ASPECTS OF THE SECURITIES REGULATION LAW: REGULATION "A" AND ITS REVISION

By ALLEN S. KRAKOVER
*of the Colorado, New York and District of Columbia Bars**
and
IRVING M. MEHLER *of the Colorado and New York Bars*

It is axiomatic that history in some shape or form tends to repeat itself. The mining industry fits quite well within the confines of this well known maxim. Boom and bust alternate, and we are now witnessing what may be one of the greatest booms of all. The uranium boom. The Colorado Plateau, more particularly the 65,000 acre mesa and rimrock country that extends into four states —Colorado, Utah, New Mexico and Arizona—is presently the chief source of uranium mined within the United States and the second largest producing area in the world. California, Nevada, Wyoming, Montana, South Dakota and Washington all are gripped in feverish activity. The mining industry is presently again the cynosure of the modern "get rich quick" adventurer, as well as the more conservative stock market investor. The uranium boom has struck this part of the country with forceful intensity.

With the advent of the uranium boom, it soon became apparent that the supply of investment capital had not kept pace with the financial needs of prospectors, claim stakers and mine operators to further their operations with risk capital. The usual method of raising capital by selling securities to the public in any amount exceeding $300,000 entailed strict compliance with the Securities Act of 1933 [1] and necessitated a filing by the issuer of a complete registration statement listing minutely detailed information of the security, the issuer and the underwriters.[2] This filing was an absolute condition precedent to the offering of the security for sale in interstate commerce to the general public. It is true that such a registration could be dispensed with if the issuer was inclined to limit his selling activity to the residents of one state. In such case, a mere filing with the particular State Commission would suffice. But to carry out an offering in such a manner is a feat of no small accomplishment. Every detail of the offering must be minutely attended. One slip, be it even making an offer to sell to the wrong person, is sufficient to cause all sales *ab initio* to be deemed in violation of the Securities Act of 1933. Where a wide market for distributive purposes is sought, which in turn necessarily involves interstate boundaries,[3] a compliance with the act becomes mandatory.

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* Mr. Krakover served as Attorney Adviser with the U. S. Securities and Exchange Commission in Washington, D. C., and with the Denver Regional Office.

[1] 48 Stat. 74 (1933), 15 U.S.C. Sec. 77.

[2] *Ibid.* Sec. 77 c.

[3] *Ibid.* Sec. 77 c.

SMALL ISSUES

The legislators long ago recognized the need for creating exemptions from the full registration procedure for issues of a small amount or where the limited character of the public offering indicated such exemption. The act [4] makes provision for the Commission to create exemptions by rule. However, in view of the intent of Congress to the effect that "this power is expected to be used only in a sparing manner",[5] the reluctance by the Commission to act along these lines had been quite manifest. The Commission early adopted several exemptive rules—a special regulations (now known as Regulation B) for fractional undivided interests in oil and gas rights and a number of separate rules (at one time as many as eleven, collectively known as Regulation A) for almost all types of other securities. All these rules contained various terms and conditions. Regulation B has remained more or less static, but the substance of Regulation A dates from January 1, 1941; as of that date, the Commission repealed all eleven of the old rules in favor of a single exemption. In 1945, Congress adopted the $300,000 figure pertaining to "small" issues, which formerly had been limited to $100,000. Just this summer, Congress considered a proposal to increase the exemption to $500,000. The proposal was not adopted.[6]

REGULATION A

Effective January 1, 1941, not only were the former existing eleven rules repealed in favor of a single exemption, but the Commission shifted its administrative emphasis from the disclosure requirements of the act to the fraud prevention provisions.[7] The ancient doctrine of *caveat emptor* was slowly being shelved. This trend had previously been enunciated by the highest court of the land.[8] Speaking for the court, Mr. Justice Black stated:

> There is no duty resting upon a citizen to suspect the honesty of those with whom he transacts business. Laws are made to protect the trusting as well as the suspicious. The best element of business has long since decided that honesty should govern competitive enterprises, and that the rule of *caveat emptor* should not be relied upon to reward fraud and deception.

Within a short period of time after the President had signed the bill raising the figure in Section 3 (b) from $100,000 to $300,000, the Commission followed suit by increasing the figure in Regulation A to the same amount with respect to primary offerings by

[4] *Ibid.* Sec. 77 c (b).
[5] H. R. Rep. No. 85.
[6] S. 2846.
[7] Sec. Act Rel. 2410 (1940) Rule 161.
[8] FTC v. Standard Education Society, 302 U. S. 112, 116 (1937).

the issuer.[9] Nevertheless, the Commission did not change the amount with respect to secondary offering by affiliates, presumably because the legislative background indicated that the purpose of the statutory amendment was to facilitate the raising of new capital by "small business;" and the figure still stands at $100,000 for secondaries despite pressure from certain quarters to increase it.[10]

It is interesting to note that under Regulation A, in contradistinction to the present Revised Regulation A, no prospectus or selling literature was required. If written sales material was being employed, it had to contain a certain amount of minimal information such as, the name of the person by or for whom the offering is being made, the number of units offered, the underwriting or other distribution expense per unit and in the aggregate, whether the offering is made by or for the issuer and the proposed use of the proceeds.[11] The philosophy of Regulation A was emphasized by the following note appended to Rule 223 (a):

> The material filed pursuant to this rule is required to be filed solely for the information of the Commission to aid it in the enforcement of Section 17 of the act (the fraud provision), and not for the purpose of enabling the Commission to cite any deficiency in the information contained therein. The failure of the Commission at any time to take action upon any information filed pursuant to this rule does not indicate that the Commission considers the information accurate, complete or not misleading.

Under Regulation A, a substantial growth in the amount of financing took place.[12] This growth proceeded steadily until 1952 when a tremendous surge in the amount of financing came to the fore due to the uranium boom. Fortunately, the revised regulation was then in effect.

REVISED REGULATION A

In further keeping pace with the current economic trend, the Commission shifted its emphasis from the fraud prevention provisions back to the disclosure provisions of the act. On August 15, 1952, the Securities and Exchange Commission published notice that it had under consideration a proposed revision of Regulation A under the Securities Act of 1933. This Revised Regulation A [13] provides an exemption from registration under the act for small issues of securities, i.e., not exceeding $300,000 in amount, upon compliance with the provisions of this regulation which went into effect on March 6, 1953. It is significant that one of the important changes brought about by the revision of Regulation A is the re-

[9] Rule 220 (a); Sec. Act Rel. 3066 (1945).
[10] Rule 220 (b).
[11] Rule 223.
[12] 15 SEC Ann. Rep. 11 (1950).
[13] 15 U.S.C. Sec. 77 c (b).

quirement that an offering circular [14] containing certain minimum information, in addition to specific financial facts, be employed in the sale of securities under the aforesaid regulations.[15] In promulgating this new requirement, the Securities and Exchange Commission kept in mind the congressional intent to aid small ventures by providing an exemption from the requirements of a full registration with respect to offerings not exceeding $300,000 in amount, while making possible more effective enforcement of the anti-fraud provisions of the law.[16] The statute indirectly requires that the investor be furnished with such basic information as will show a fairly complete picture of the enterprise in which he is being asked to invest his funds. And viewed from the investor's perspective, it was only fair that certain safeguards be provided for him against unscrupulous operators.

In addition, the Commission has also made known its further intent, by stating that the offering circulars proposed to be used in connection with offerings under the Revised Regulation A will be examined primarily from the standpoint of determining whether the minimum basic facts are fully disclosed and whether these facts indicate the existence of fraud in connection with the proposed offering. This attitude on the part of the Commission is in keeping with the basic purposes of the regulation to help the operator but not to deny its fullest protection to the investor.

To further aid the incipient entrepeneur, the Revised Regulation A provides for the use of limited written advertisements or other written communications [17] prior to the sending or giving of the offering circular. Persons making an offering under this regulation are thus permitted to advertise inexpensively for the purpose of obtaining inquiries from persons who may be interested in receiving the offering circular. The issuer is thus provided with an additional prop to enable him to foster his business endeavors.

In addition to the advertisement permitted by Rule 220, an issuer can also use what is known as a "tombstone" advertisement. This type of advertisement was permitted under Regulation A prior to its revision, and while the Revised Regulation does not speak on the subject the Commission has not objected to the "tombstone's" continued use.

The revised regulation also makes provision for denying or suspending the exemption in cases where the Commission finds that the conditions and terms of the exemption have not been met.[18] In other words, if it is discovered that the offering circular contains fraudulent information, or that fraud or deceit is being perpetrated or would be perpetrated in the sale of the securities, the Commission will invoke its power to deny or suspend its exemption

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[14] Revised Regulation A, Rule 219.

[15] Revised Regulation A, Rule 219 (b) provides an exception as to offerings of $50,000 or less.

[16] *Ibid.* Purpose of Revision.

[17] *Ibid.* Rule 220.

[18] *Ibid.* Rule 224.

under the act. This power is in addition to the remedy open to the Commission of applying to the courts for an injunction prohibiting further violations.[19]

As previously pointed out, the revised regulation exempts offerings up to a maximum of $300,000. An offering on behalf of any one person other than the issuer is limited to a maximum of $100,000. Subject to this limitation, persons other than the issuer may offer, in the aggregate, more than $100,000, but not more than $300,000. An offering up to the $300,000 limitation may, however, be made on behalf of the estate of a deceased person if the offering is made within two years after the death of such person.

Pursuant to the present administrative practice of the Commission, the revised regulation also provides for the filing of semi-annual reports showing the progress of the offering.[20] After completion or termination of the offering, no further reports are required after the filing of the final report.[21]

It is significant to point out at this time that the Revised Regulation A provides that a notification must be filed with the Commission and that the offering circular required by Rule 219 is filed with and is to be deemed a part of this notification.[22] Information such as the jurisdictions in which the securities are to be offered,[23] contemplated additional offerings,[24] unregistered securities sold within one year,[25] predecessors, affiliates, directors, officers and promoters of the issuer,[26] and any and all information relating to convictions, injunctions and fraud orders within the preceding five years against the issuer or any of its directors, officers, promoters, predecessors or affiliates must be disclosed.[27] The notification also calls for a filing of certain exhibits [28] and documents pertaining to the offering such as underwriting contracts and agreements of similar nature.

CONCLUSION

The writers wish to emphasize at this time that the Commission, as an administrative arm of the Federal Government, is an agency whose strength lies in its flexibility and adaptability to the vicissitudes that occur daily in the economic spheres of activity. This administrative strength was proven by the timely adoption of Revised Regulation A in further keeping with the present necessity

[19] 15 U.S.C. Sec. 77 t.

[20] *Ibid.* Rule 224.

[21] The Commission has just recently circularized uranium issuers requesting them to provide further information concerning their offering and the subsequent history of the company. The Commission desires this information in order to review the effectiveness of Revised Regulation A.

[22] Form 1-A promulgated under Revised Regulation A.

[23] *Ibid.* Item 1.

[24] *Ibid.* Item 2.

[25] *Ibid.* Item 3.

[26] *Ibid.* Items 4 and 5.

[27] *Ibid.* Item 6.

[28] *Ibid.* Item 7.

of shifting administrative emphasis from the fraud prevention requirements of the act to the disclosure aspects of the law. In the everyday administration of Revised Regulation A, numerous problems arise calling for the exercise of interpolative judgment. Decisions thus reached are then disseminated throughout the Commission and used as a basis for reaching further decisions. Thus, day by day the unwritten law of the regulation is applied as decisions are reached, not by the specific application of a written rule, but rather by an extension of the philosophy underlying the regulation.

There have been times when the Commission has been criticized for its Draconian attitude in administering the act. On the whole though, the Commission has constantly striven to foster a policy of fair treatment to all, thus seeking to insure that delicate and happy balance of aid to the entrepeneur without denying commensurate protection to the investor. The general attitude of the Commission can best be summed up by resorting to the well turned phrases of Mr. Justice Douglas in the case of *Estin v. Estin*[29] wherein he stated:

> There are few areas of the law in black and white. The greys are dominant and even among them the shades are innumerable. For the eternal problem of the law is one of making accommodations between conflicting interests.

[29] 334 U. S. 541 (1948).

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