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## THE NEW IOWA "UNIFORM" SECURITIES LAW

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Iowa has had legislation regulating transactions in securities since 1913, and the Iowa Securities Law enacted in 1929 was in many respects like the Uniform Blue Sky Law which was an approved uniform act between 1929 and 1941.<sup>1</sup> Significant changes in practice in the securities industry since 1929, the impact of the Securities Act of 1933 and the Securities Exchange Act of 1934,<sup>2</sup> and the approval of a Uniform Securities Act in 1956<sup>3</sup> which has been adopted by some states and is the basis for new legislation in many others, has meant that existing Iowa law was out-of-step with current practices and current legislation. This made it more difficult for corporations to market their securities in Iowa when engaged in interstate financing programs, and for Iowans to be able to take advantage of investment opportunities; when investments were made it was more difficult to obtain adequate protection therefore than could be the case under a modernized approach.

In 1973 a committee of the Iowa State Bar Association authorized the establishment of the Iowa Securities Law Project (hereinafter "Project") to undertake the task of drafting a proposed securities law for Iowa. The Project included members of the Bar committee plus practitioners and state employees who had worked with securities law.<sup>4</sup> While the Project was pursuing its task,

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1. See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 302 (1969).

2. 15 U.S.C. § 77(a) *et seq.* (Supp. IV, 1974); 15 U.S.C. § 78(a) *et seq.* (Supp. IV, 1974).

3. 7 UNIFORM LAWS ANN. *Business and Financial Laws* 691 (1970). The text is also set out, with official comments and drafters comments to each section, as an appendix to L. LOSS & E. COWETT, *BLUE SKY LAW* (1958).

4. For much of the period it operated, the project consisted of fifteen lawyers. Co-chairman L. Call Dickinson, Jr., Professor Edward R. Hayes (the Reporter), Wilbur N.

public concern developed over the affairs of and the techniques of selling securities by two Iowa enterprises; the concern indicated that some revision of the existing law was immediately essential and could not wait for the Project to produce its draft. The Project cooperated with the Securities Department and interested legislators in preparing this revision, which was enacted in 1974.<sup>5</sup> It was understood that some of the changes were but stop-gap, until the Project was completed and enacted, but that most of the revision would be reflected in the finished proposal.

The Project met regularly over an eighteen-month period. Its basic operation was the careful examination of the Uniform Securities Act, and especially those modifications made to it when it was adopted by Massachusetts, Pennsylvania and Wisconsin, the latest of the over thirty states to base their laws on that Act (hereinafter USA). It was recognized that as the USA was written in 1956, it could be necessary to update and modernize features of it because of the evolutionary nature of securities and corporate law and practices throughout the country. The Project also notes concepts being considered in the proposed Federal Securities Code.<sup>6</sup> The Chairman and the Reporter also spent approximately six hours in an effort to "desex" the proposed act, by redrafting to eliminate references to "he," "his," and similar language. The final version, adopted by the Project and by the Bar committee in November, 1974, was approved by the Board of Governors of the Bar Association for inclusion in its recommendations of proposed legislation for 1975, and by the Iowa Insurance Commissioner.

The studied purpose of the Project was to work toward the drafting of a flexible and balanced bill having as its principal purpose the protection of the Iowa investing public in new securities issues and in other securities which are traded on the secondary market. In meeting this objective it was felt necessary that a balanced regulatory framework should be established to control the operation of all brokers and dealers which conduct business in the state of Iowa. Membership of the Project was such that the public interest should be adequately and ably represented.

The proposed bill was introduced in the 1975 Legislature, and was

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Bump, John D. Galvin (Corporations Director, Secretary of State's office), Edgar F. Hansell, Ralph H. Heninger, Roger L. Lande, Professor Paul Neuhauser, and Roy W. Van der Kamp, were members of the Iowa State Bar Association's Special Committee on Corporation and Business Law. Co-chairman A. Arthur Davis, William B. MacDonald and Brian P. Williams were non-committee members with substantial practice in the securities field. Larry J. Bryant was Superintendent of the Securities Department until shortly after the Project began its work; he is engaged in private practice. Professor Glenn W. Clark succeeded Mr. Bryant as Superintendent of the Department, and held that post through most of the deliberations. When he returned to full-time teaching, he remained a participant in the project, and his successor, Marshall Hunzelman, was added. Miss Elizabeth Nolan, an Assistant Attorney General, also participated as her assignments include the Insurance Department and the Securities Department.

5. Ch. 1238 [1974] Iowa Acts 823.

6. ALI FED. SEC. CODE (Temp. Draft No. 1, 1972).

adopted with several minor changes. The new law became effective January 1, 1976.<sup>7</sup>

As the new law will have much impact on current practices, this article proposes to examine it in detail, and to compare and contrast it with the securities law formerly applicable in Iowa and with the Uniform Securities Act. The article will consider administration processes, the procedure to register brokers, dealers and securities, the various ways in which the Act may be violated and the consequences of violation. Although the Uniform Act includes provisions for registration of investment advisors, and some states have enacted provisions along those lines, the Project felt that they could be omitted, as federal regulation of this area should be adequate to cover the small number of advisors that could be subject to regulation by Iowa.<sup>8</sup>

### I. ADMINISTRATION OF THE ACT

Securities regulation in Iowa has been a responsibility of the Commissioner of Insurance since 1939. He has appointed a superintendent in charge of the securities department; usually that superintendent supervises the day-to-day functioning of that department.<sup>9</sup> The Act continues this pattern by designating the Commissioner of Insurance as the administrator; he is to appoint a deputy administrator, to be the principal operations officer of the securities department, responsible to the administrator for the routine administration of the Act and the management of the department.<sup>10</sup> The deputy is designated as acting administrator, for those times when the administrator is absent or is disabled from functioning, or his office is vacant; the administrator may delegate to the deputy any or all of the functions assigned to himself under the Act, by order.

The USA provision making it unlawful for the administrator or securities department personnel to use for personal benefit any non-public information filed with or obtained by the department was adopted. It was expanded to permit disclosure not only when necessary and appropriate under the Act or to other department personnel, but also to other securities administrators, regulatory authorities, or governmental agencies.<sup>11</sup> The former Iowa Securities Law

7. Ch. 234 [1975] Iowa Acts 516 [hereinafter cited as Iowa Uniform Securities Act, or IUSA]. This article follows in substantial detail an explanation of the proposed bill which was made available to the chairman of the House Committee on Commerce, to which the bill was referred.

8. As a result of this decision, sections 102, 201(c) and 401(f) of the Uniform Securities Act (hereinafter USA) have no counterparts in the Iowa Uniform Securities Act, and the many sections referring to brokers, dealers and investment advisers are revised to eliminate the reference to the investment advisers.

9. IOWA CODE § 502.2 (1975); see 5 E. HAYES, IOWA PRACTICE—CORPORATION LAW AND PRACTICE § 302 (1969).

10. IUSA section 601(1), based on USA section 406(a), contains much of the substance of Iowa Code section 502.2 in this regard. Although the Project recommendation was that the deputy not be subject to the merit service system (see IOWA CODE ch. 19A (1975)), and that he serve at the pleasure of the administrator, the Insurance Commissioner insisted that the deputy be subject to merit system requirements.

11. IUSA § 601(2), based on USA § 406(b), as modified, WIS. STAT. ANN. § 551.51 (2) (1975). The words "his officers or employees" were replaced by "officer or employee

(hereinafter ISL) had a substantially comparable provision until 1973, which also said that much information was not open to public inspection. In the 1974 amendments the information was made open to public inspection, and the prohibition against its use for private purposes was dropped.<sup>12</sup> This section of the IUSA does not incorporate the 1974 amendment's statement that information contained in or filed with a registration statement or application is to be made public, but that language does appear in another section, taken from the USA, which also permits the administrator to furnish photostatic or other copies of these records, and makes a copy, if certified, *prima facie* evidence of the contents of the entry or document certified.<sup>13</sup>

The administrator has been authorized to make, amend, and rescind such rules, forms and orders as are necessary to carry out the provisions of the Act, including those governing registration statements, applications, and required reports, and in them he may define terms, whether or not used in the Act—at least unless a definition is inconsistent with the Act.<sup>14</sup> Originally the ISL contained no rule-making authority; this was remedied in 1965, and regulations relating to some aspects of the ISL have been adopted.<sup>15</sup> The section deviates from the USA by beginning: "Pursuant to the Iowa Administrative Procedure Act, . . ."<sup>16</sup> As a result of that reference, it was not considered necessary to include the USA requirement that the rules and forms be published.<sup>17</sup> The USA permits the administrator to cooperate with other states' securities administrators and the SEC in exercising his rule-making power; this was expanded to refer also to national securities exchanges and national securities associations registered under the Securities Act of 1934.<sup>18</sup> The administrator will have extensive rule-making power relating to accounting practices and statements.<sup>19</sup> Acts done in good faith reliance on a rule will not result in liability if the rule is thereafter changed, rescinded or held to be invalid.<sup>20</sup>

Most aspects of administrative hearings are governed by the Administrative Procedure Act.<sup>21</sup> The IUSA does provide that every hearing in an administrative proceeding is to be public unless all respondents request it be conducted privately, and the administrator in his discretion grants the request.<sup>22</sup>

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of the securities department" or "such officer or employee;" "privilege . . . exists" in the last sentence was changed to "privileges . . . exist," possibly by inadvertence.

12. IOWA CODE § 502.31 (1975).

13. IUSA § 608(3), (4); USA § 413(c), (d).

14. IUSA § 607(1); USA § 412(a).

15. IOWA CODE § 502.2 (1975). This section contains only a general statement that the Commissioner makes rules and regulations. See 5 E. HAYES, IOWA PRACTICE—CORPORATION LAW AND PRACTICE § 302 (1969).

16. Cf. USA § 412(a).

17. USA § 412(d).

18. IUSA § 607(2) (based on USA section 412(b)).

19. IUSA § 607(3); USA § 412(c).

20. IUSA § 607(4); USA § 412(e).

21. IOWA CODE ch. 17A (1975); cf. *id.* § 502.22.

22. IUSA § 607(5); USA § 412(f).

One section of the ISL, which the code editor had entitled "Injunctions," provided the Commissioner with broad investigatory and subpoena power, if he thought a violation of the law had occurred or was occurring, judicial aid to enforce these powers, and authority to seek injunction, receivership, or both, as a remedy.<sup>23</sup> The IUSA substantially follows the USA approach, authorizing the administrator to make such investigations concerning possible violations as he deems necessary, and providing him or his delegate with the power to administer oaths, subpoena witnesses, and compel production of books, records and documents. Most of the deviations are grammatical in nature or are designed to eliminate words like "he" and "his." However, a statement was included that the granted powers may be enforced in accordance with the Administrative Procedure Act, and this made it possible to delete the USA subsection concerning enforcement. Despite the substantial difference in language from the ISL, it appears to provide no significantly different power to investigate and to compel testimony, other than the granting of power to investigate both outside and inside Iowa, and the provision for transactional immunity when a witness claims his testimony should not be compelled or his records produced because of his privilege against self-incrimination.<sup>24</sup>

A separate section provides that whenever it appears to the administrator that a person has violated the Act, or is about to do so, the administrator may either issue a cease and desist order or bring an action in district court for injunction, restraining order, or writ of mandamus. This follows the USA except for adding the power to issue a cease and desist order, and for rewriting the last sentence to make clear that the administrator cannot be required to post bond as part of those court proceedings.<sup>25</sup> No specific procedure for enforcement of cease and desist orders was included; presumably, either this will be handled in accordance with the Administrative Procedure Act or the administrator will use his authority to seek injunctive relief.

The administrator is to keep a register of all applications for registration and registration statements currently or previously effective under the IUSA or its predecessors, plus all censure, denial or revocation orders entered under it or its predecessors. This register, too, is open for public inspection.<sup>26</sup> As will be noted in discussing the procedures for registration of securities and of brokers and dealers, the administrator also has the power to issue stop orders after a registration, and to censure brokers or dealers.

The USA provision that the administrator may honor requests from interested persons for interpretative opinions was enacted. Drafters of that Act

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23. IOWA CODE § 502.21 (1975).

24. IUSA § 603; USA § 407(a), (b), (d). Where testimony is compelled, or documents are required to be produced, the privilege against self-incrimination is not available to avoid testifying or producing the material; if the privilege is claimed and denied, the individual testifying obtains transactional immunity, but he can be prosecuted for perjury or contempt committed in testifying.

25. IUSA § 604; U.S.A. § 408.

26. IUSA § 608(2); USA § 413(b), *as modified*, WIS. STAT. ANN. § 551.64(2) (1975) (to refer to predecessor laws).

indicate that this provision contemplates opinions "which will not be in the form of orders, will not have any quasi-judicial force, and will not be subject to judicial review." It is designed to encourage the administrator to render interpretations freely and informally, on request.<sup>27</sup>

Other aspects of the administrator's role in the registration process, and his status as agent for service of process, are described in subsequent sections.

## II. REGISTRATION OF BROKER-DEALERS, AGENTS AND ISSUERS

Under the Iowa Securities Law, dealers and salesmen of securities were not to engage in business in Iowa as such nor to sell securities (except in exempt transactions) until they had registered with the Commissioner as a dealer or a salesman. An issuer of securities who sold them in Iowa without using the services of a dealer could be treated as if it were a dealer.<sup>28</sup> The Iowa Uniform Securities Act labels those people who are required to register as "broker-dealer" and "agent," and changes the rules with regard to the issuer; apart from these changes it probably does not establish a process substantially different from that under the predecessor law although the language of the Act differs in many respects and leaves more for the administrator to establish by rule or order.

"Broker-dealer" is defined as any person engaged in the business of effecting transactions in securities for the account of another or for such person's own account, unless he is: (a) an agent; (b) an issuer; (c) an institutional investor; (d) a person having no place of business in Iowa, under specified circumstances; and (e) any other person that the administrator by rule or order designates as not within the intent of the concept of "broker-dealer." Institutional investor includes (but is not limited to) insurance companies or banks except when they are engaged in the business of selling interests in a separate account that are securities, other than through a subsidiary. The person with no place of business in Iowa is outside the definition of broker-dealer if his transactions within Iowa are effected exclusively with or through issuers of the securities involved, other broker-dealers, or institutional investors,<sup>29</sup> or if during any consecutive twelve month period he does not direct more than fifteen offers to sell or to buy into Iowa in any manner. For this latter purpose it does not matter whether offeror or offeree is present in Iowa at the time the offer was so directed; but an offer within one of the three "exempting" categories just described is not to be counted as part of the fifteen.<sup>30</sup>

27. IUSA § 608(5); USA § 413(e); see L. LOSS & E. COWETT, BLUE SKY LAW 400 (1958).

28. IOWA CODE § 502.11 (1975).

29. The statute refers to "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; . . ." IUSA § 102(4)(d)(1).

30. *Id.* § 102(4).

The Uniform Act differs from the Iowa definition of "broker-dealer" substantially only in referring to "bank, savings institution, or trust company" as one of the excluded classes, rather than "institutional investor," and in not providing exclusion for any other person designated by the administrator.<sup>31</sup>

The comparable predecessor definition of "dealer" covered persons engaged for all, or part of their time, directly or through an agent, in the business of dealing in securities as agent or principal for a commission or a profit, or in futures or differences in market quotations of securities or who accepted margins on actual or "pretended" purchases or sales. Exclusions covered "salesmen," and those not having a place of business in Iowa if they only purchased securities from issuers or sold or offered to sell exclusively to brokers or dealers transacting business in securities.<sup>32</sup> An issuer was considered to be a dealer if it sold securities in Iowa other than through a dealer or through an exempt transaction; but was required to pay only the greater of the fees for registering the security or registering as a dealer, and was not required to furnish bond.<sup>33</sup> The IUSA does not treat the issuer as a broker-dealer.<sup>34</sup> "Broker" was defined to mean "dealer."<sup>35</sup>

"Agent" is defined in the IUSA as an individual, not a broker-dealer, who represents a broker-dealer or issuer in effecting or attempting to effect purchases or sales of securities. A significant difference from the comparable predecessor definition of "salesman" is that agent can include a partner, officer, or director of a broker-dealer or an issuer, or someone in a similar status or performing similar functions, if that person acts in a representative capacity in such transactions. The only exclusions from the definition are for those who represent an issuer, in effecting transactions of certain types of securities exempt from registration, in effecting transactions exempt from registration, or in effecting transactions with existing employees, partners or directors of the issuer where no remuneration is paid or given in any way for soliciting any

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31. USA § 401(c). The added exclusion is found in *Wisconsin Statutes Annotated* section 551.02(3), but several other exclusions added in Wisconsin were not included, among them those for an executor, administrator, guardian, conservator or pledgee, and for licensed real estate brokers whose transactions in securities were isolated transactions incidental to their real estate brokerage activities.

32. IOWA CODE § 502.3(4) (1975).

33. *Id.* § 502.11.

34. The ISL defined "issuer" to include "every person who proposes to issue, has issued, or shall hereafter issue any security," including "[a]ny natural person who acts as a promoter for and on behalf of a corporation, trust or unincorporated association or partnership of any kind to be formed." IOWA CODE § 502.3(5). The IUSA and USA definitions are identical, and cover any person who issues or proposes to issue any security except that where the security is a certificate of deposit, voting trust certificate, collateral trust certificate, or certificate 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 refers to those persons who perform the acts and assume the duties of depositor or manager according to the applicable agreement, and where the security is a certificate 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. IUSA § 102(7); USA § 401(g).

35. IOWA CODE § 502.3(7) (1975).

person in Iowa.<sup>36</sup> Except for one "desexing" change, this definition is the same as that of the USA.<sup>37</sup> The predecessor definition of "salesmen" included natural persons (other than dealers and partners or executive officers or a registered dealer) representing a dealer or issuer "to sell securities in any manner" in Iowa, and contained no exceptions for engaging in transactions on behalf of issuers.<sup>38</sup> "Agent" was defined to mean "salesman."<sup>39</sup>

Under the Iowa Securities Law, the process of registering as a dealer began with the filing of a verified application, which was to identify the applicant's principal place of business, its various offices in Iowa, its principals, co-partners, officers and directors, its general character and place of business, how long it had engaged in business, and such information as to its past history, record and association as the Commissioner thought necessary to establish its good repute in business, plus an irrevocable written consent to service of process upon the Commissioner in actions against the dealer. The Commissioner could establish minimum financial requirements to be met and maintained. The Commissioner had to find the applicant to be of good business repute, to have proven its competence to act as a dealer, and that it had paid the fees and filed the bond required, before registering it. Salesmen could be registered only on application filed for that purpose by a registered dealer (or an issuer in certain situations); there had to be satisfactory showing as to good character and competence of the individual plus payment of the proper fee, and if the salesman's employment with that dealer terminated his registration ceased. An examination could be required of first-time applicants. Registration expired automatically one year after issuance, but renewals could be obtained annually upon written application and payment of the filing fee, without furnishing further information unless the Commissioner required it.<sup>40</sup> The same section provided that if there were changes in personnel of a partnership or in the principals, co-partners, officers or directors of a dealer, the registration should be changed to reflect this by written application setting forth the change.

The new procedure for registration of "broker-dealers" also contemplates the filing of an application plus consent to service and the filing fee. No mandatory content of the application is specified; it may include any matter required by rule which the administrator deems relevant.<sup>41</sup> Registration

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36. IUSA § 102(2). The relevant exemptions are for securities issued by federal, state, municipal, Canadian and certain foreign governments and governmental agencies, by certain banks, for certain types of commercial paper, and for securities issued in connection with many types of employee benefit plans. *Id.* § 202(1), (2), (3), (10), (11).

37. USA § 401(b).

38. IOWA CODE § 502.3(6) (1975).

39. *Id.* § 502.3(8).

40. *Id.* § 502.11.

41. Among those matters which the statute specifies that can be inquired into are: applicant's form and place of organization, proposed method of doing business and financial condition, qualifications and experience of applicant and of any partner, officer, director or controlling person, any conviction of a felony, and any injunction, administrative order or conviction of a misdemeanor involving securities. IUSA § 302(1).

becomes effective at noon of the thirtieth day after the application is filed,<sup>42</sup> unless a denial order is in effect or a proceeding to deny, suspend, cancel or withdraw registration is pending. However, the administrator by rule or order may accelerate the effective date, or by order may defer it until noon of the thirtieth day after filing of any amendment to the application. Should there be changes in personnel of the broker-dealer, resulting in technical termination of its existence and replacement by a successor (as when a partner retires, or is added), the registered party may file for registration of its successor for the balance of the term remaining, without any fee. There is no requirement that applications for registration of agents be filed by the agent's employer; however, agents who are partners, etc., of broker-dealers are automatically registered as part of the relevant broker-dealer registration if named in the application therefor.<sup>43</sup> Except for elimination of the power to adopt a rule or order requiring newspaper announcement of initial application for registration, this portion of the IUSA follows the Uniform Act, in substance.<sup>44</sup>

While an agent may file his own application for registration, the registration is effective only during those periods when the agent is associated with a specified broker-dealer registered in Iowa or a specified issuer. Accordingly, both agent and broker-dealer or issuer have the responsibility promptly to notify the administrator that the agent's employment has begun or has terminated. An agent may represent only one broker-dealer or issuer at a time, unless permitted by order of the administrator, except that where organizations affiliated by direct or common control are registered as broker-dealers, or are issuers of securities registered under the Act, the agent may represent any of the affiliates.<sup>45</sup> This is based on Wisconsin's modification of the Uniform Act, which added the provision for representing affiliates.<sup>46</sup>

All registrations, whether of broker-dealer or of agent, expire on the last day of September of each year, instead of on a staggered basis, as occurred under the predecessor law and as would be permitted under the USA.<sup>47</sup>

As the Commissioner had to reach an affirmative determination as to the dealer's good repute and competency, before he could grant registration, it was

42. A document is "filed" when it is received by the administrator. IUSA § 608(1); USA § 413(a).

43. IUSA § 302(1), (3). The fee for these registrations was increased to \$100 from \$50, and for agent registrations from \$5 to \$10, in 1974, after the Project drafters had adopted that fee schedule. IUSA § 302(2); IOWA CODE § 502.11 (1975).

44. USA section 202(a)-(c), modified to eliminate registration of investment advisers, was also modified grammatically in several respects. The automatic registration of agents who are partners, etc., was limited to those named in the application or in amendments to it, and the reference to including the filing fee with the application was added. This latter modification should mean that the application is not "filed" unless accompanied by the fee.

45. IUSA § 301(2).

46. USA § 201(b); WIS. STAT. ANN. § 551.31(2) (1975). Pennsylvania adopted a somewhat similar modification. PA. STAT. ANN. tit. 70, § 301(b) (1975).

47. IUSA § 301(3). The Uniform Act provides for annual expirations, but permits the administrator to develop a schedule for staggering renewal times (but to end on the last day of a month in each instance). The intent is to reduce the impact of the renewal work. USA § 201(d). The members of the Project who were associated with the Securities Department indicated that they felt staggering renewals were not necessary.

not clear when registration would become effective. The USA eliminates the requirement for determining good repute, and establishes an automatic effective date, unless the administrator takes steps to deny a particular registration. Many grounds available for denial of registration are also grounds for suspending or revoking an existing registration or for censuring an applicant or registrant, and these will be examined later in this section.

The applicant for registration as broker-dealer may, by rule, be required to have a specified minimum capital, and to post a surety bond. The bond also is required of certain issuers employing agents.

Although a minimum capital provision is part of the USA, the Iowa version follows a Pennsylvania modification which also permits the rule to establish limits on aggregate debt in relation to net capital and to classify broker-dealers for this purpose. The rule may not require a higher minimum capital or lower debt-capital relation, from a broker-dealer who is an NASD member or registered with the SEC, than is required by the rules and regulations of that Association or the Commission.<sup>48</sup>

The predecessor law required posting of surety bonds in the amount of \$5,000 (increased in 1974 to \$15,000) in favor of the state, for the use and benefit of any purchaser of securities sustaining damages as a result of any breach of its conditions (which were, essentially, that the dealer would pay a judgment based on a finding that it sold securities in violation of the law or that the purchaser was defrauded in the sale). The bond could be sued on by any person injured by the breach, for damages up to the amount of the bond, within two years after the cause of action accrued. If suits in excess of the amount of the bond were commenced, the Commissioner could require posting of an additional bond, and could revoke registration if the addition was not given within ten days.<sup>49</sup> The Project proposed a much different bonding provision, which originally received House approval. The Senate amended the proposal to conform to the prior law in many respects, and this change received final approval. However, it does not include the provision for suit by any person injured by the breach, within two years after accrual of the cause. Thus, actions on the bond may be limited to actions by the state.<sup>50</sup> This requirement is based upon a Pennsylvania modification to the USA, and does not include the USA provision for deposit of cash or securities in lieu of bond, or for its

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48. IUSA § 302(4). See USA § 202(d); PA. STAT. ANN. tit. 70, § 303(d) (1975).

49. IOWA CODE § 502.18 (1975).

50. IUSA § 302(5). The Project version would have left requirements for bonds to the discretion of the administrator, in an amount not to exceed \$15,000. The administrator could have required such bonds by rule, unless the broker-dealer has a net capital in excess of an amount set in the rule. Injured customers, clients, or purchasers were to be able to sue on the bond, which was to be effective as long as the registration, unless cancelled by the surety. The surety could cancel only after thirty days notice, in writing, to the person posting the bond and to the administrator. No cancellation could affect liability incurred or accrued before the effective date of cancellation.

The section as adopted also continues the former provision that banks or trust companies under Iowa or federal supervision, if required to provide bond under the section, may execute the bond without surety.

establishment of a two-year limit on the time in which action on the bond can be maintained.<sup>51</sup>

A provision, taken from Wisconsin, permits the administrator to act by rule or order to impose any other condition in connection with registration under the IUSA that he deems appropriate, in the public interest or for the protection of investors.<sup>52</sup>

After registration, the broker-dealer is to make and keep such accounts, correspondence, memoranda, papers, books and records as the administrator by rule prescribes, and to preserve them for three years unless a different period is prescribed for particular types of records. It is also to file such financial reports as the administrator by rule prescribes, and to file promptly correcting amendments when information in any document filed with the administrator is or becomes inaccurate or incomplete in any material respect. Records required are to be kept in Iowa or, at the request of the administrator and at his option, to be made available for examination at the registrant's principal office (wherever it may be located) or by production of exact copies of these in Iowa.<sup>53</sup>

The administrator is to make a periodic examination of the business and records of each registered broker-dealer, at such time and place and in such scope as the administrator determines. He need not give prior notice of the examination. To reduce duplication of effort, the administrator may cooperate in examinations with other states' securities administrators, the SEC, and any national securities exchange or national securities association registered under the Securities Exchange Act of 1934. Information obtained in the course of an examination is not to be made public, other than when under a duty to inform one of the agencies just mentioned or to take action against the broker-dealer, except when called as a witness in any criminal or civil proceeding.<sup>54</sup> This follows the Wisconsin revision of the USA, which adds the material concerning the non-public nature of the information obtained, rewrites the section concerning the nature, place and scope of the examination, and adds the cost requirement.<sup>55</sup> Under the predecessor law, the dealer could be required to report monthly regarding all securities purchased and sold by it and its salesmen in the previous month, and its books were at all times open to inspection by securities department personnel. If examination showed the registrant to be insolvent, or if the records were in such state that its solvency could not be ascertained, the Commissioner could ask for appointment of a receiver for the business.<sup>56</sup> The registrant apparently could be required to pay for an examination, as it could be compelled to make an advance deposit of an

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51. USA § 202(e); PA. STAT. ANN. tit. 70, § 303(e) (1975).

52. IUSA § 302(6); WIS. STAT. ANN. § 551.32(7) (1975).

53. IUSA § 303(1)-(3).

54. *Id.* § 303(4).

55. USA § 203(d); WIS. STAT. ANN. § 551.33(4) (1975).

56. IOWA CODE § 502.15 (1975).

amount estimated to be sufficient to cover the expenses, from which deposit the expenses of the examination were to be paid.<sup>57</sup>

Several limitations on the dealer's conduct of its business were not carried over from the predecessor law to the IUSA—this does not mean that what was forbidden before is therefore now permitted. The old law required a dealer to segregate from his general account all trust funds, to be carried in a special trust account in a reputable depository.<sup>58</sup> It was said to be unlawful for a broker to pledge or otherwise dispose of his customer's securities, unless he had a lien on them or the client had consented.<sup>59</sup> It was unlawful for an insolvent broker to accept or receive money or securities from a customer unaware of the insolvency, except to liquidate a debt the customer owed it.<sup>60</sup>

The predecessor law required consents to service to be filed by every registered dealer, and by issuers acting as dealers if the issuer was not domiciled in Iowa. The consent agreed that actions growing out of violations of the law could be commenced against the filer in the proper court in any county in Iowa by the service of the appropriate process or pleadings on the Commissioner. Duplicate copies of the papers served were to be provided so that the Commissioner could file one and forward the other by registered mail to the principal office of the dealer or issuer involved.<sup>61</sup> The IUSA continues a requirement for filing consents to service, expanding it to include applicants for registration of securities and issuers who are Iowa domiciliaries who engage in security transactions in Iowa through agents. The consent appoints the administrator or his successor in office, and applies to the applicant or its successor, executor or administrator. However, no consent need be filed by a party who filed a consent in connection with a previous registration, if it is then in effect. Service is made by leaving a copy of the process in the administrator's office. The plaintiff in the action (which may in some circumstances be the administrator) must promptly send notice of the service and a copy of the process by registered or certified mail to the defendant or respondent at its last known address, or take such other steps as are reasonably calculated to give actual notice, and must file an affidavit of compliance with the statutory procedure on or before the return day of the process or within such time as the court allows.<sup>62</sup> This section contains several minor modifications of the comparable USA provision.<sup>63</sup>

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57. *Id.* § 502.12.

58. *Id.* § 502.13.

59. *Id.* § 502.17.

60. *Id.* § 502.16. Insolvency was defined to occur when the fair value of the broker's property was not sufficient in amount to pay its debts. (Whether the broker had to be aware of his insolvency was not stated.) *Id.*

61. *Id.* § 502.9.

62. IUSA § 609(1).

63. USA § 414(g). "As agent" was substituted for "on an agency basis in the common law sense," and "promptly" for "forthwith." A comma was inserted between "successor" and "executor." The comment that service under the section would have the same "force and validity" as personal service on the filer was changed by deleting the words

A new feature of the service of process procedure is a provision that even though no consent to service has been filed, if a person (resident or nonresident) engages in conduct prohibited or made actionable by the Act or by any rule or order under it, and personal jurisdiction over that person cannot be obtained otherwise, that conduct is the equivalent of appointment of the administrator or his successor in office as the person's attorney to receive service of process in noncriminal proceedings against the person or his successor, executor or administrator, arising from that conduct. The same procedures are to be followed as in the cases where consent to service is on file.<sup>64</sup> This is in substance the Uniform Act's provision.<sup>65</sup> Whether the necessity for it has been obviated by the "long-arm" statute<sup>66</sup> or its equivalent in the recent amendment to the *Iowa Rules of Civil Procedure*,<sup>67</sup> remains to be determined.

A provision added states that if process is served under either of the statutory methods, the court, or the administrator where administrative proceedings are being instituted, is to order such continuance as may be necessary to afford the defendant (respondent) reasonable opportunity to defend.<sup>68</sup>

In addition to the requirement that before registration is granted the Commissioner had to find that an applicant for registration as a dealer was of good repute and competent to act as dealer, and that there was to be a general satisfactory showing that an applicant for registration as a salesman was of good character and competence,<sup>69</sup> the law enumerated sixteen grounds on which registration of either could be denied (or revoked if already granted) plus two others applicable to the dealer only. These grounds (all being types of misconduct) could be used only if the Commissioner after reasonable notice and hearing determined that they had been established. Registration could be suspended, however, pending the hearing.<sup>70</sup>

The IUSA permits the administrator to deny, suspend or revoke registration or to censure an applicant or registrant, after complying with the procedural requirements of the Iowa Administrative Procedure Act (which contemplates reasonable notice and hearing).<sup>71</sup> To act, the administrator must find the order to be in the public interest, and that the applicant or registrant (or certain personnel connected with the broker-dealer involved)<sup>72</sup> has engaged in one or more of some ten acts of misconduct.<sup>73</sup> In addition, registration may be

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"force and." The sentence excusing filing where a previous consent had been filed was reorganized, and the requirement that the person's registration still be in effect was added.

64. IUSA § 609(2).

65. USA § 414(h). Similar modifications to those noted in note 63 *supra* were made.

66. IOWA CODE § 617.3 (1975).

67. IOWA R. CRV. P. 56(2).

68. IUSA § 609(3); USA § 414(i).

69. IOWA CODE § 502.11 (1975).

70. *Id.* § 502.14.

71. IUSA § 304.

72. The personnel include any partner, officer, or director, any person occupying a similar status or performing similar functions, or any person directly or indirectly controlling the broker-dealer. *Id.* § 304(1).

73. *Id.*

revoked if the administrator finds that the registrant: (1) no longer exists; (2) has ceased to do business in the capacity for which registration was granted; (3) is subject to an adjudication of mental incompetence or to the control of a committee, conservator, or guardian; or (4) cannot be located after search.<sup>74</sup> The administrator, without hearing, may summarily postpone or suspend registration pending final determination of proceedings to deny, suspend, revoke or censure; but notice of this act, and the reasons for it, must be given promptly, and the affected party must be informed that if it desires a hearing on that act the matter will be set for hearing within fifteen days after receipt of a written request therefor. After the hearing, if one is held, the order may be modified, vacated, or extended until final determination.<sup>75</sup>

The grounds for action that constitute misconduct are:

(1) filing an application for registration which as of its effective date was incomplete in any material respect or contained any statement which was, in light of the circumstances under which it was made, false or misleading with respect to any material fact;<sup>76</sup>

(2) willful violation of or failure to comply with any provision of the IUSA (or the ISL while it is applicable), or any rule or order thereunder;<sup>77</sup>

(3) conviction within the past ten years of any felony, or of any misdemeanor involving a security or any aspect of the securities business;<sup>78</sup>

(4) being the subject of a permanent or temporary injunction issued by any court of competent jurisdiction (and currently in force) against engaging in or continuing any conduct or practice involving any aspect of the securities business;<sup>79</sup>

(5) being the subject of an order of the administrator denying, suspending, or revoking registration as a broker-dealer or agent;<sup>80</sup>

(6) being the subject of an order entered within the past five years by the securities administrator of any other state or by the SEC, which denied or revoked registration as broker-dealer, agent, or investment adviser,<sup>81</sup> or by the

74. *Id.* § 304(4).

75. *Id.* § 304(3).

76. *Id.* § 304(1)(a); USA § 204(a)(2)(A). This ground also applies to similar circumstances "as of any date after filing in the case of any order denying effectiveness." IUSA § 304(1)(a); USA § 204(a)(2)(A). This compares in part with *Iowa Code* section 502.14(2) (1975), concerned with the making of material false statements in the application for registration, and *Code* section 502.14(9), concerned with misrepresentations of any essential or material facts to the commissioner.

77. IUSA § 304(1)(b); USA § 204(a)(2)(B) (substantially the same as *Iowa Code* section 502.14(1) (1975)).

78. IUSA § 304(1)(c); USA § 204(a)(2)(C) (with minor revision in punctuation). The related ISL section refers to conviction of felony, or of any misdemeanor of which fraud is an essential element. *Iowa Code* § 502.14(5) (1975).

79. IUSA § 304(1)(d); USA § 204(a)(2)(D) (no comparable provision in ISL).

80. IUSA § 304(1)(e); USA § 204(a)(2)(E). See comments in notes 76 *supra* and 82 *infra*.

81. Note that this is the sole reference to investment adviser retained in the Act, and permits revocation by a non-Iowa agency of such a registration to be a factor in registrability under another capacity.

SEC suspending or expelling applicant (or registrant) from a national securities exchange or national securities association registered under the Securities Exchange Act of 1934, or being the subject of a United States Post Office fraud order;<sup>82</sup>

(7) engaging in dishonest or unethical practices in the securities business;<sup>83</sup>

(8) insolvency, in either the equity or the bankruptcy sense (in the case of the broker-dealer, the administrator must make a finding of insolvency, before this ground can be utilized);<sup>84</sup>

(9) being unqualified, on the basis of such factors as training, experience, and knowledge of the securities business;<sup>85</sup> or

(10) failure, in the case of a broker-dealer, reasonably to supervise its agents.<sup>86</sup>

The first of these grounds may not be used for suspension or revocation where based on facts known to the administrator at the time registration became

82. IUSA § 304(1)(f); USA § 204(a)(2)(F), as rewritten, WIS. STAT. ANN. § 551.34 (1)(f) (1975) (eliminating the words "or the substantial equivalent of [broker-dealer, agent, or investment adviser] as defined in this act"). The comparable ISL provision applied only to refusals to license or to cancellation, suspension or withdrawal of license of applicant (registrant), or any officer, director, member or partner, manager or trustee thereof, in any state for fraudulent conduct or violation of the law of that state regulating the sale of securities therein. It did not apply to federal actions, and possibly not to all refusals or revocations by state authorities. IOWA CODE § 502.14(12) (1975).

83. IUSA § 304(1)(g); USA § 204(a)(2)(G). Several ISL provisions fit within this ground. These include: committing a fraudulent act in connection with any sale of securities, or having been, being engaged or about to be engaged in making fictitious or pretended sales or purchases of securities or in any practice or sale of securities which is fraudulent or in violation of the law (IOWA CODE § 502.14(3) (1975)); demonstrating unworthiness to transact the business of dealer or salesman (*id.* § 502.14(4)); making misrepresentations of false statements to, or concealing any essential or material fact from, any person in the sale of a security to (though not the purchase from) such person (*id.* § 502.14(6)); failing to account to persons interested for all money and property received (*id.* § 502.14(7)); failure to deliver to the proper parties, within a reasonable time, securities the broker-dealer held or agreed to deliver (*id.* § 502.14(8)); using or has used practices in the sale of securities that work or tend to work a fraud (*id.* § 502.14(13)); in the sale of a security, stating that a dividend would be paid on it before the issuer actually declared such a dividend (*id.* § 502.14(15)); or, in the sale of a security, promising that it would be listed on a security exchange when no application for the listing had actually been made to the exchange (*id.* § 502.14(16)).

84. IUSA § 304(1)(h) (based on USA section 204(a)(2)(H), but rewritten to state in different terms what is meant by insolvency). IOWA CODE section 502.14(10) (1975) says only "[i]s insolvent."

85. 304(1)(i). This ground is based on USA section 204(a)(2)(I), as modified by *Wisconsin Statutes Annotated* section 551.34(1)(i) (1975), to eliminate: (1) the requirement that such an order, if entered against a broker-dealer, must be based on lack of qualification of the dealer himself only when he is an individual, or on the lack of qualification of his agent; (2) the provision that there can be no denial for lack of experience if the applicant is qualified by training, or knowledge, or both, and; (3) the provision that an agent working under supervision of a registered broker-dealer need not have the same qualifications as a broker-dealer. See USA § 204(b). The administrator thus will be able to consider these matters if he thinks they are relevant, but is not required to adhere to them. There was no comparable provision under the ISL.

86. IUSA § 304(1)(j); USA § 204(a)(2)(J). The only related ISL provision was concerned with the sale of or offer to sell securities through any unregistered solicitor or agent. IOWA CODE § 504.14(11) (1975).

security of the same or another issuer is an offer of that other security, whether the right to convert or acquire is exercisable immediately or in the future.<sup>101</sup> Although this is the substance of the comparable USA provision, there is considerable difference in language; the IUSA terminology was taken from the proposed Federal Securities Code.<sup>102</sup> This reverses the predecessor law's approach that held there was no offer of the subsequent security before there was an attempt to exercise the conversion or acquisition privilege.<sup>103</sup>

The IUSA also states that these terms do not include any bona fide pledge or loan, or any stock split, reverse stock split, or security dividend payable in the same or other securities of the corporation paying the dividend when the recipient parts with nothing of value in exchange (including not surrendering a right or option to receive a cash or property dividend).<sup>104</sup> There was no comparable provision in the predecessor law. The USA treats pledges and loans in this fashion, and also any dividend in stock (but not in other securities) whether the stock is issued by the dividend payer or by some other issuer. It also excepts acts incident to class vote by shareholders (when required by statute or article) on merger, consolidation, reclassification of securities or sale of assets in exchange for securities of another corporation, and acts incident to a judicially approved reorganization in which securities are exchanged for securities, claims, property or cash, or combinations thereof.<sup>105</sup> These latter exchanges may fall within a category for which an exemption is available; if so, the effect of the Project's approach is to exclude them from necessity to register but to include them among the transactions to which rules against fraud, misrepresentation or similar misconduct will apply.

### 3. Security

The definition of security is a broad one, which enumerates various types of instruments, and then adds, in general, any interest or instrument commonly known as a "security" or a certificate of interest in or right to acquire (or a similar document) a security. Excluded are insurance or endowment policies or annuity contracts in which the issuer promises to pay money in a lump sum or at specified intervals.<sup>106</sup> This is identical with the Uniform Act, and omits

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102. USA § 401(j)(5); ALI FED. SEC. CODE § 293(d) (Temp. Draft No. 1, 1972).

103. IOWA CODE § 502.3(3) (1975).

104. IUSA § 102(10)(f).

105. USA § 401(j)(6).

106. "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 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 for some other specified period.  
IUSA § 102(12).

the optional language of that Act relating to an issuer's promise to pay "a fixed sum of money" rather than "money."<sup>107</sup> The predecessor law had a definition that was similar in many respects, though not always using identical language to describe the same concept; however, it did not cover the insurance-annuity situation, and a 1974 addition which was not carried into the Project's final proposal treated as a security a "privilege or option to purchase or sell any commodity futures contract but not the underlying commodity futures contract itself."<sup>108</sup>

### B. *The Process of Registering Securities*

A registration statement may be filed by the issuer, by any other person on whose behalf the offering is to be made, or by a registered broker-dealer.<sup>109</sup> Examination of the process requires consideration of the several types of registration, the registration statement, how long it is effective, amendments to it, limits and conditions that may be imposed, and the administrator's power to allow, deny, suspend or revoke registration.

#### 1. *Types of Registration*

The USA provides for three types of registration—by qualification, by coordination and by notification.<sup>110</sup> Qualification requires the most detailed supplying of information. The drafters of the USA assumed it would be used only when other types could not be, typically by "the promotional issue which is offered in a single state; the local offering by a company which, though beyond the promotional stage, is not eligible for registration by notification; and most of the interstate offerings which are under SEC Regulation A."<sup>111</sup> Registration by coordination permits a substantial reduction of materials to be filed at the state level because the security involved is the subject of a registration statement filed, in connection with the same offering, under the Federal Securities Act of 1933. Under registration by notification, a simpler statement is required. This latter method is available usually to issuers who have been in existence for a considerable period (often at least five years) and who meet certain earnings tests; it often may be an alternate to registration by coordination. Originally the Iowa Blue Sky Law provided only for registration by qualification; after 1959 it also included registration by notification and something akin to registration by coordination.<sup>112</sup> The Project elected not to

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107. USA § 401(I).

108. IOWA CODE § 502.3(1) (1975).

109. IUSA § 208(1); USA § 305(a). See note 31 *supra* concerning the definition of "issuer."

110. USA §§ 302-04.

111. L. LOSS & E. COWETT, BLUE SKY LAW 299 (1958).

112. IOWA CODE §§ 502.6, 502.7 (1975). Registration by notification became available in Iowa in 1959, and at the same time a provision was included that three copies of the federal prospectus could be used in lieu of portions of the required material for registration

continue this precise pattern; it did include registration by coordination but omitted registering by notification on the theory that the coordination procedure served the same function and that compliance with SEC registration requirements should meet the needs to which notification registration was addressed.<sup>113</sup>

Registration by qualification may be used for any security required to be registered in Iowa.<sup>114</sup> Registration by coordination is available for any offering for which a registration statement has been filed under the Securities Act of 1933, and for Regulation A offerings under that Act, where notifications of proposed sales are filed,<sup>115</sup> but only if the registration statement or notification of proposed sale has not become effective at the time the registration statement is filed with the administrator.<sup>116</sup> The USA language was followed in stating the eligibility to register by qualification, and also as to registration by coordination except that the Pennsylvania inclusion of Regulation A offerings was adopted.<sup>117</sup>

## 2. *The Registration Statement—Registration by Qualification*

The application for registration by qualification should be submitted on a form developed by the administrator which requires inclusion of considerable detailed information, and to which a number of exhibits must be attached; it should also be accompanied by or include information described in subsection (d) below, a consent to service of process, and the appropriate fee. The information required falls in the following categories:

(1) as to issuer and any significant subsidiary: name, address and form of organization, jurisdiction under which organized and date thereof, general character and location of business, description of its physical properties and equipment, and statement of general competitive conditions in the industry or business in which it is or expects to be engaged;

(2) as to each director, officer, or person in similar status or having similar function: name, address and principal occupation for past five years, his interest in issuer's securities and how much of the issue being registered he has indicated an intent to subscribe to, and material interest in any material transaction with issuer or significant subsidiary in past three years or being proposed;

(3) as to the same persons: the aggregate remuneration to these people during the past twelve months and estimated for the next twelve, paid directly

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by qualification. See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* §§ 303, 304 (1969).

113. Both Pennsylvania and Wisconsin omit provisions regarding registration by notification.

114. IUSA § 207(1); USA § 304(a).

115. 15 U.S.C. § 77c(b) (Supp. IV, 1974). See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 279 (1969).

116. IUSA § 206(1).

117. USA §§ 303(a), 304(a); PA. STAT. ANN. tit. 70, § 205(a) (1975).

or indirectly by issuer, all its predecessors, parents, subsidiaries and affiliates;<sup>118</sup>

(4) as to any record or beneficial owner of five percent or more of outstanding shares of any class of equity security of issuer: all information in (2) above, except occupation;

(5) as to any promoter, where issuer organized within past three years: all information in (2) above, plus amounts paid to the promoter or intended to be paid, and the consideration for such payments;

(6) as to any person on whose behalf any part of the offering is to be made in a "non-issuer" distribution:<sup>119</sup> the person's name and address, the amount of securities held by him when the statement is filed, the last item of information described in (2) above, and statement of reasons for making the offering;

(7) as to issuer and any significant subsidiary: capitalization and long term debt, description of each outstanding security or any being registered or otherwise offered, and the amount and kind of consideration for which securities were issued within the past two years or there is an obligation to issue ;

(8) as to issuer, and to non-issuer offerors: the kind and amount of securities being offered; the proposed offering price or method of computing it; any variant prices to any person or class other than underwriter, and to whom; basis of any offering other than for cash; expected selling costs, fees, discounts; copy of any applicable underwriting or selling group agreement or its proposed term; and description of plan of distribution for securities offered other than through an underwriter;

(9) as to issuer: estimated cash proceeds to be received, purpose to which to be applied and amount for each purpose, order or priority of application, and amount and sources of other funds to be used for those purposes (if to be used to acquire property other than in the ordinary course of business, a complete description of the proposed acquisition and its financing);

(10) as to issuer: stock options or other securities options outstanding or created in connection with the offer, amount held by each person to be named in (2)-(5) and (7), and by any person who holds or will hold ten percent or more of any such options;

(11) as to issuer: dates, parties and general tenor of any management or other material contract not in the ordinary course of business made within the

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118. "Affiliate" or "affiliated with," means a person who directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, the person specified. IUSA § 102(3). There is no comparable USA provision, but *Pennsylvania Statutes Annotated* section 102(b) is identical.

119. "Non-issuer" means not directly or indirectly for the benefit of the issuer." IUSA § 102(8); USA § 401(h). An offering may include both an "issuer" and a "non-issuer" distribution, if a corporation is offering securities and some of its shareholders are attempting to dispose of portions of theirs as part of the same offering.

past two years to be performed in whole or in part after the filing of the registration statement, and description of any pending litigation or proceeding involving issuer which materially affects its business or assets (including litigation known to be contemplated by governmental authorities);

(12) a copy of any prospectus and other sales literature intended, as of the effective date, to be used in connection with the offering;

(13) a copy of issuer's articles of incorporation and bylaws, a copy of any indenture or other instrument covering the security involved, and a specimen or copy of the security itself;

(14) a signed or conformed copy of opinion of counsel as to legality of the security (to be translated into English if opinion is in a foreign language); it is to be stated whether the security when sold will be legally issued, fully paid and non-assessable, and (if a debt security) that it is a binding obligation of the issuer;

(15) the written consent of any professional named as having certified or prepared a report or valuation (other than a public or official document) used in connection with the registration statement;

(16) as to issuer and any predecessor, or vendor thereto: recent balance sheet (within four months prior to filing), profit and loss statement and analysis of surplus for each of the three preceding fiscal years and for the period between the end of the latest fiscal year and the date of the balance sheet (information is required about vendors where any part of the proceeds of the offering is to be applied to purchase "any business" from vendor); and

(17) such other additional information as the administrator requires by rule or order.<sup>120</sup>

The information required is almost precisely stated in the same terms as in the USA, except for the IUSA inclusion in item 16, based on a Pennsylvania addition, that the financial statements required as to vendor should be either the same as would be required if vendor was the registrant *or* such other financial statements as can be required by IUSA section 607(3).<sup>121</sup>

The predecessor law lists nine categories of information which may be required, including a recent (within ninety days) balance sheet and an income statement for the last fiscal year, plus such additional or more detailed information as the Commissioner deems necessary. These categories are much less inclusive than under the new Act, except for a requirement that corporate issuers file their articles and other issuers file copies of their basic organizational documents. In addition, the law permits the Commissioner to accept three copies of the prospectus as of the date on which the application was filed, in

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120. IUSA § 207(2)(g).

121. USA § 304(b); PA. STAT. ANN. tit. 70, § 206(b)(16) (1975). See note 19 *supra*, and supporting text.

lieu of the required information, if the securities are also being registered under the Securities Act of 1933.<sup>122</sup>

Registration by qualification becomes effective only when the administrator so orders. However, when a statement has been on file at least thirty days, with no action thereon, and all information requested by the administrator has been furnished, applicant may request in writing that the administrator within ten days order the statement to become effective or deny or postpone effectiveness. If the administrator takes no action within that ten day period, the registration then becomes effective at the end of that time.<sup>123</sup> The predecessor law said that if the Commissioner could not find any statutory ground for denying or revoking registration, after examination, he "shall register such securities" and thereafter they could be sold, but it provided no method for compelling him to act.<sup>124</sup> The USA does not have a "compelling" provision, and the IUSA language is an adaptation of Pennsylvania's modification to this effect.<sup>125</sup>

### 3. *The Registration Statement—Registration by Coordination*

The application for registration by coordination is to include copies of certain materials filed under the Securities Act of 1933, and certain material specified in the IUSA, and it should be accompanied by or include information described in subsection (d) below, a consent to service of process, and the appropriate fee. The information required falls in the following categories:

(1) two copies of the most recent preliminary prospectus or offering circular filed under the Federal Act;

(2) if the administrator by rule requires, copies of: articles of incorporation and bylaws or currently effective equivalents, agreement with underwriters, indenture or other instruments governing the issuance of the security involved, and specimen or copy of the security;

(3) any other information, or copies of documents, filed under the Federal Act, if requested by the administrator; and

(4) an undertaking to forward to the administrator any future amendments to the prospectus or offering circular (other than amendments merely delaying effective date), not later than the first business day after forwarding to or filing with the SEC, or within such longer period as the administrator permits.<sup>126</sup>

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122. IOWA CODE § 502.7(2) (1975).

123. IUSA § 207(3).

124. IOWA CODE § 502.7(2) (1975).

125. USA § 304(2); PA. STAT. ANN. tit. 70, § 206(c) (1975) (calling for a request to "take action," and effectiveness if the commission "takes no action" within the ten day period).

126. IUSA § 206(2). The administrator by rule or order may waive any conditions specified in this subsection. *Id.* § 206(4).

This follows the Pennsylvania revision of the comparable USA provision.<sup>127</sup>

Registration under this method becomes effective automatically at the same time that the federal registration statement or notification does, if: (1) the administrator has not issued a stop order or has not instituted a proceeding to deny; (2) the statement has been on file with the administrator for at least twenty days; (3) a statement has been on file for two full business days (or such shorter period as the administrator permits), which sets forth maximum and minimum proposed offering prices and maximum underwriting discounts and commissions; and (4) the offering is made within those limitations.<sup>128</sup>

The registrant has a duty to notify the administrator promptly (by telephone or telegraph) of the time the federal registration statement became effective and the content of any "price amendment"<sup>129</sup> filed. If the administrator fails to receive either the notification or the post-effective amendment relating to price, he may enter a stop order retroactively denying effectiveness, or may suspend effectiveness until compliance has been effected. No notice or hearing is required, but the registrant is to be notified promptly of the action; if registrant can prove that it had complied as to notice and amendments, the stop order is to be vacated retroactively.<sup>130</sup>

The federal registration statement may become effective before all of the four conditions described above have been satisfied. If the administrator does not waive those conditions, the Iowa registration statement will become effective automatically when they have been satisfied. A curious registrant may advise the administrator as to the date that federal registration is expected to become effective, and if he does the administrator will advise registrant (promptly, by telephone or telegraph, at registrant's expense) whether he considers the conditions to be satisfied and whether he is contemplating institution of denial, suspension or revocation proceedings. Advice that he is

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127. USA § 303(b); PA. STAT. ANN. tit. 70, § 205(b) (1975). The principal differences are in requiring two rather than three copies of the federal prospectus, in permitting use of an offering circular, and in category (4) not specifying that the time to file runs from the earlier of the forwarding or the filing.

128. IUSA § 206(3). This is essentially the same as the first sentence of USA section 303(c), which was also set out as a separate subparagraph in *Pennsylvania Statutes Annotated* section 205(c). The administrator by rule or order may waive any condition specified in this subsection. IUSA § 206(4).

129. "Price amendment" is the final federal amendment stating offering price, underwriting and selling discounts or commissions, amount of proceeds, conversion rates, call prices and other matters dependent upon the offering price. IUSA § 206(4); USA § 303(c).

130. IUSA § 206(4). This follows USA section 303(c) with minor changes. One "promptly" was shifted in its location in the first line; a "the" appears to have been inserted inadvertently before "effectiveness;" "is effected" was inserted following "compliance" in the reference to suspension for failure to comply; and the USA statement that when the registrant proves he had complied the stop order is "void" was modified to "shall be vacated." Except for the latter, the changes have no impact; the latter would appear to require another order by the administrator, which the USA process may not require.

not then contemplating such proceedings will be no bar to his later instituting them.<sup>181</sup>

#### 4. *The Registration Statement—Provisions Generally Applicable*

The person filing the statement is to pay a filing fee of 1/10 percent of the maximum aggregate offering price at which the securities are to be offered in Iowa, with a minimum fee of \$50 and a maximum of \$1,000. If the registration statement is withdrawn before it becomes effective or a pre-effective stop order is entered, the fee is retained, not returned to registrant.<sup>182</sup>

Every registration statement is to specify:

- (1) the amount of securities to be offered in Iowa;
- (2) the states in which a registration statement or application in connection with the offering has been or is to be filed; and
- (3) any adverse order, judgment or decree relating to the offering which regulatory officers of another state, or the SEC, or any court, has entered, and any withdrawal of a registration statement or application relating to the offering.<sup>183</sup>

Documents filed under the Act or its predecessor within the five years preceding filing of the registration statement (the ISL set no time limit) may be incorporated by reference in the registration statement to the extent that the document is currently accurate.<sup>184</sup>

The administrator by rule or otherwise may permit omission of any item of information or document from any registration statement.<sup>185</sup>

Where a registration is filed in connection with a non-issuer distribution, the filer is not required to supply information called for, in the case of registration by qualification, and in the post-registration period, unless that information is known to the filer or to the persons on whose behalf the distribution is to be made or unless they can furnish the information without unreasonable effort or expense.<sup>186</sup> This follows the Uniform Act.<sup>187</sup> There is no comparable provision in the predecessor law, but it did allow the Commissioner by rule, regulation or order to waive submission of most material otherwise required, when the filer was a registered dealer, and permitted that filer to file a statement containing a limited amount of information.<sup>188</sup>

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131. IUSA § 206(5); USA § 303(c).

132. IUSA § 208(2); USA § 305(b). The predecessor differed only in setting a minimum of \$25 rather than \$50, and in not providing for retention of the fee after withdrawal. IOWA CODE § 502.7(3) (1975).

133. IUSA § 208(3); USA § 305(c) (plus the addition by Wisconsin of the reference to withdrawal). WIS. STAT. ANN. § 551.27(2)(c) (1975). Pennsylvania, making a similar addition, required the withdrawal to be "with prejudice." PA. STAT. ANN. tit. 70, § 207(b) (1975).

134. IUSA § 208(4); USA § 305(d); see IOWA CODE § 502.7(3) (1975).

135. IUSA § 208(5); USA § 305(e); IOWA CODE § 502.7(3) (1975).

136. IUSA § 208(6).

137. USA § 305(f).

138. IOWA CODE § 502.7(3) (1975).

### 5. *Conditions Which Administrator May Impose on Registration*

By rule or order the administrator may impose as a condition of registration a requirement that any security issued within the past three years, any to be issued to a promoter for a consideration substantially different from the public price, or any to be offered to any person for a non-cash consideration, be deposited in escrow. He may also require that the proceeds from the sale of the registered securities in Iowa be impounded until the issuer has received a specified amount from the sale either in Iowa or elsewhere. He may determine the conditions of the required escrow or impoundment, but cannot reject a depository solely because it is located outside Iowa.<sup>139</sup> This differs from the predecessor provision which permitted the Commissioner to require an escrow agreement in the case of stock issued or to be issued for intangible assets or promotional services and expenses. Until 1974, the escrowed shares were to be delivered to the Commissioner; thereafter they could be delivered to him or to a depository acceptable to him. The statute until 1974 also required payments of dividends of at least six percent, actually earned, to shareholders who paid cash, before the escrow could terminate; thereafter, the Commissioner could set appropriate conditions, except that in case of dissolution or insolvency during the escrow period, the escrowed shares could not participate in distribution until "after the owners of all other securities" were paid in full.<sup>140</sup> The requirement for deposit in escrow with the Commissioner could be onerous, if shares were being registered in several states and each state insisted on a local escrow arrangement for the same shares.

The administrator may also require, by rule, that securities of designated classes be issued under a trust indenture.<sup>141</sup> Neither the predecessor law nor the Uniform Act has a comparable provision, but both Pennsylvania and Wisconsin do.<sup>142</sup>

A Uniform Act provision which was not included would have allowed the administrator to require the use of specified forms of subscription or sale contracts, and the filing of a signed or conformed copy with the administrator or their preservation for up to three years.<sup>143</sup> There also is no provision comparable in form to that in the predecessor law which authorized the Commissioner to limit the price at which "the securities either of par or no par value" could be sold, and which authorized him to allow a commission of not to exceed twenty percent of the sales price, which was to cover all expenses of

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139. IUSA § 208(7); USA § 305(g).

140. IOWA CODE § 502.20 (1975).

141. IUSA § 208(8).

142. *Wisconsin Statutes Annotated* section 551.27(8) is identical. *Pennsylvania Statutes Annotated* title 70, section 207(h) is limited to debt securities, and says the provisions of the indenture may not be in addition to or inconsistent with those required or permitted by the Trust Indenture Act of 1939.

143. USA § 305(h).

selling the securities, although excessive commissions, etc., may be a ground for denial or revocation.<sup>144</sup>

A condition which may be imposed, by rule or order, on registration by qualification is that a report by an accountant, engineer, appraiser or other professional person be filed. One or more employees of the securities department may be designated to examine the business and records of the issuer. The expenses of the report or examination are to be borne by the applicant or registrant.<sup>145</sup>

A rule or order may be promulgated which requires as a condition of registration that a prospectus containing any designated part of the information required is to be provided in registration by qualification, or the final prospectus or offering circular required in registration by coordination, be delivered to each person to whom an offer is made before or concurrently with the first of four events to occur. These events are: (1) first written offer (other than by a public advertisement) by or for the person on whose behalf the offering is being made or by an underwriter or broker-dealer who took an allotment or subscription as participant in the distribution and is trying to sell parts of it; (2) confirmation of sale by or for such persons; (3) payment pursuant to such sale, or (4) delivery of the security pursuant to the sale.<sup>146</sup> This follows the USA, which, however, extends only to instances where registration was by qualification.<sup>147</sup>

## 6. Post-Registration Conditions

Every registration statement remains effective until it is withdrawn, suspended or revoked. While it is effective, all outstanding securities of the same class as the registered one are treated as registered for purposes of non-issuer transactions. If securities of the same class are outstanding, a registration statement may not be withdrawn for one year after its effective date. Any other withdrawal is at the discretion of the administrator, to be allowed by order.<sup>148</sup> This approach differs from that of the USA, Pennsylvania and Wisconsin, which limit the effective period to one year or such longer period as the initial distribution requires.<sup>149</sup> The deviation was adopted to conform to the practice under the predecessor law, which also made registration effective

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144. IOWA CODE § 502.8 (1975). See IUSA § 209(1)(f), note 171 *infra*, and supporting text.

145. IUSA § 208(10). This section is based on *Wisconsin Statutes Annotated* section 551.27(5) (1975), which does not clearly limit the report requirement to cases of registration by qualification. *Pennsylvania Statutes Annotated* section 207(e) says that the report may be required in coordination registrations if more than two-thirds of the issue is to be sold in that state.

146. IUSA § 208(12).

147. USA § 304(d).

148. IUSA § 208(9)(a).

149. USA § 305(i); PA. STAT. ANN. tit. 70, § 207(j) (1975); WIS. STAT. ANN. § 551.27 (11) (1975). These sections do, however, apply the same approach to time in which withdrawal may be made.

until revoked by the Commissioner or terminated by registrant with the Commissioner's consent.<sup>150</sup> The purpose of the deviation is to provide registration for subsequent transactions in the security that might not be within one of the statutory exemptions from requirement for registration.

If registration is to have continuing effect, the registration statement must be kept current to reflect changes in the issuer's affairs. Accordingly, the IUSA requires the issuer to do two things:

(1) while the initial offering continues, to amend the registration statement from time to time as appropriate to keep the information in it reasonably current, and to disclose the progress of the offering;

(2) whether the offering continues or has been completed, to file with the administrator and to distribute to Iowa holders of securities of the class registered, within 120 days after each fiscal year ends, an annual report including financial statements which meets standards set by the administrator, and such additional financial statements or information as he requires by rule or order( but not more frequently than semiannually.)<sup>151</sup> The USA does provide for keeping information reasonably current while the registration is effective, but does not require annual reporting to the securityholders. The Project thought this additional reporting requirement was desirable, especially so in view of the policy for continuing effectiveness of registration.

The registration statement may be amended after its effective date to increase the specified amount of securities proposed to be offered. The amendment will not be effective until the administrator so orders. An appropriate filing fee, based on the same formula as for original registration, is required.<sup>152</sup> The USA has a similar provision, which is limited to securities issued by a "face-amount certificate company" or certain mutual funds and investment companies;<sup>153</sup> Pennsylvania extended it as did Iowa, but omitted reference to the filing fee.<sup>154</sup>

#### 7. *Statutory Limit on Registering Shares by Qualification*

In order to compel issuers of substantial amounts of securities to meet federal registration requirements rather than to avoid them under the "intras-

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150. IOWA CODE § 502.7(3) (1975).

151. IUSA § 208(9)(b). When registration has been by a non-issuer or by a broker-dealer, if the administrator has no jurisdiction over the issuer, he may be unable to compel filing and distribution of the material. The material cannot be required in cases of non-issuer distribution, unless it is known to the person filing the statement or the persons on whose behalf the distribution is to be made, or can be furnished by them without unreasonable effort or expense. *Id.* § 208(6).

152. IUSA § 208(11). Apparently the fee for the amendment is computed without regard to the shares previously offered. Even if the maximum fee has already been paid, the amendment would probably require a fee.

153. USA § 305(k).

154. PA. STAT. ANN. tit. 70, § 207(l) (1975).

tate offering" exemption,<sup>155</sup> the Project included a section which has no counterpart in the USA, predecessor law, Pennsylvania or Wisconsin. It sets a maximum offering price on the shares that can be registered for sale in Iowa by qualification. The aggregate offering price of all securities of the issuer registered for sale as part of a single issue of equity securities shall not exceed:

(1) \$2,000,000, if the securities are offered or sold only on behalf of issuer, its affiliates or the estate of a decedent who owned them at the time of his death; but if the offer (or part of it) is by or on behalf of affiliates (other than an estate), the amount with respect to any one affiliate shall not exceed \$500,000; or

(2) \$750,000, if the securities are to be offered or sold by or on behalf of any other person or persons, with a limit of \$500,000 for any one such other person.<sup>156</sup>

"Securities of the issuer" includes securities issued by any "predecessor of the issuer" or by any affiliate which was organized or became an affiliate within three years before the effectiveness of registration of the securities sought to be registered in Iowa.<sup>157</sup> "Predecessor of the issuer" includes any person who provided the major portion of the issuer's assets, directly or indirectly, or who had the major portion of its assets acquired by the issuer, directly or indirectly.<sup>158</sup> "Person" includes: an individual, and his spouse, relatives and spouses of relatives, if they are "having the same home" as he does; any trust in which he and some of those people collectively own ten percent or more of the total beneficial interest, or serve as trustee or executor; and any corporation or organization (other than issuer) in which he and some of them are beneficial owners of at least ten percent of the equity interest or of any class of equity securities.<sup>159</sup>

The concept of the various limitations was taken from the SEC's Regulation A, and the terminology from that and other SEC regulations.<sup>160</sup>

#### 8. *Permitting, Denying, Suspending and Revoking Registration*

For a number of years the ISL required the Commissioner, before permitting registration by qualification, to find that the sale of the security involved would not be fraudulent or would not work or tend to work a fraud on the purchaser, and that the business of the issuer was not based on unsound business principles.<sup>161</sup> This blatantly paternalistic approach was diluted in 1959, and the Commissioner was hence permitted to register securities by

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155. 15 U.S.C. § 77a(11) (Supp. IV, 1974). See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 277 (1969).

156. IUSA § 210(1).

157. *Id.* § 210(2)(a).

158. *Id.* § 210(2)(c).

159. *Id.* § 210(2)(b).

160. 17 C.F.R. §§ 230.207(d), 231.251, 230.254(a) (1975).

161. IOWA CODE § 502.7 (1956).

notification or by qualification, after finding that there would be no grounds for denying or revoking registration of that security.<sup>162</sup> A separate section, originally providing grounds to refuse or revoke registration, was restated to provide for denying effectiveness to, or suspending or revoking registration.<sup>163</sup> Both approaches to permitting registration contemplated what is essentially an affirmative finding by the Commissioner before he granted registration. The approach adopted in the Uniform Act, and followed by the IUSA is, in a sense, negative—the administrator should allow registration to become effective unless he finds a basis for denying effectiveness.

The IUSA provides authority to the administrator to issue a stop order, which results in denying effectiveness to, or suspending or revoking effectiveness of, a registration. The stop order can be issued before a statement has become effective, or after it is effective and distribution has begun. With the exception of one circumstance,<sup>164</sup> entering of any stop order requires compliance with the Iowa Administrative Procedure Act (which means notice, hearing and possibility of appeals to courts).<sup>165</sup> Although use of the term "stop order" is new to the Iowa law, it is in substance what the Commissioner had been able to do since 1959, and is the terminology applicable to similar processes of the SEC.<sup>166</sup>

Before any stop order can be issued, the administrator must find that the order is in the public interest and that at least one of the following nine grounds for action exist:

(1) The registration statement (as of its effective date or as of any earlier date in case of an order denying effectiveness), any amendment thereto filed to keep the information in it current or to increase the amount of securities being offered (as of its effective date), or any financial statement or report required to provide shareholders with current financial information<sup>167</sup> is incomplete in any material respect, or contains any statement which was, in light of the circumstances under which it was made, false or misleading with respect to any material fact;

(2) Any provision of the Act or any rule, order or condition lawfully imposed under it has been willfully violated, in connection with the offer, by: the filer of the registration statement; the issuer; any partner, officer or director of issuer or person occupying a similar status or performing similar functions; any affiliate of issuer if filer is also an affiliate of issuer; or any broker-dealer;<sup>168</sup>

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162. IOWA CODE § 502.7(2)(i) (1975).

163. *Id.* § 502.10.

164. The exception is the summary postponement or suspension of registration, pending final determination of proceedings which meet the Administrative Procedure Act requirements for notice and hearing. IUSA § 209(3).

165. *Id.* § 209(4).

166. 15 U.S.C. § 77h(d) (Supp. IV, 1974).

167. See note 151 *supra*, and supporting text.

168. The IUSA substitutes "affiliate" for the USA language "person directly or indirectly controlling or controlled by the issuer," and thus expands the concept to include those

(3) The securities involved are the subject of an administrative stop order or similar order or of a permanent or temporary injunction of any court of competent jurisdiction, entered under any other federal or state act applicable to the offering. If the registration statement has become effective in Iowa, the administrator may not institute proceedings against that statement under this section more than one year from the date of the order or injunction relied on, nor may he rely on an order or injunction entered under the law of another state unless that order or injunction was based on facts which would currently constitute a ground for stop order in Iowa;

(4) Issuer's enterprise or method of business includes or would include activities which are illegal where performed;<sup>169</sup>

(5) The issuance or sale of the securities is or would be unfair or inequitable to purchasers or has worked or tended to work a fraud upon purchasers or would so operate;<sup>170</sup>

(6) The offering has been or would be made with unreasonable amounts of underwriters' and sellers' discounts, commissions, or other compensation, or promoters' profits or participation, or unreasonable amounts or kinds of options;<sup>171</sup>

(7) Advertising has been used in connection with the offering contrary to the new section which permits requiring of filing of sales and advertising literature to be used in the selling campaign, and prohibiting advertising deemed false or misleading;<sup>172</sup>

(8) The financial condition of issuer affects or would affect the soundness of the securities; or

(9) Applicant, or registrant, failed to pay the proper filing fee (but only a denial order may be used in this case, and it is to be vacated when the deficiency is corrected).<sup>173</sup>

As the footnotes indicate, most of these grounds have a USA counterpart, and conform substantially thereto; several exceptions draw on Wisconsin's approach. Two grounds set out in the USA were omitted as they pertained only to

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under common control. "Broker-dealer" is substituted for "underwriter." Pennsylvania made the same substitutions. PA. STAT. ANN. tit. 70, § 208(a)(ii) (1975).

169. The official comments indicate the reference is to conducting a business in a state where that business (such as a racetrack or a gambling casino) is illegal, rather than a legal business violating a statute on resale price maintenance or minimum wages. It also should not apply to a business illegal in the state of registration, if lawful in the state where the business is conducted. See L. LOSS & E. COWETT, *BLUE SKY LAW* 326 (1958).

170. The USA does not include the language "is or would be unfair or inequitable to purchasers." USA § 306(a)(E). It was inserted in Wisconsin. WIS. STAT. ANN. § 551.28 (1)(e) (1975). The entire section was omitted by Pennsylvania. PA. STAT. ANN. tit. 70, § 208(a) (1975).

171. This is comparable to the predecessor law's provision permitting the commissioner to allow a commission of up to 20 percent of the sale price, to include all expenses and advertising, but does not extend as far as that provision's permission to limit the selling price of the securities. IOWA CODE § 502.8 (1975).

172. See IUSA § 602.

173. IUSA §§ 209(1)(h), (i); USA § 306(a).

registration by notification, which was not provided for in the IUSA.<sup>174</sup>

The predecessor law described eight grounds for refusing or revoking registration (plus the issuer's refusal to permit an examination)—as many as four of them may have no counterpart in the IUSA.<sup>175</sup> Item 8, above, regarding the issuer's financial condition, may be equivalent to "is insolvent" or "its affairs are in an unsound condition." Item 2 is similar to "has violated any [ISL provision] or any order of the commissioner" of which issuer had notice. Item 5 may be similar to "has been or is engaged or is about to engage in fraudulent transactions," and with item 7 to the provision concerning dishonesty in any other way or any fraudulent representation in sales literature. None of the items is like "is of bad business repute," "does not conduct its business according to law," or "that the enterprise or business of the issuer is not based upon sound business principles." One effect is to remove from the administrator the power to conclude that because he thinks a proposed business is a poor risk for success it shouldn't be allowed to try to make a go of it, and therefore it is not based on "sound business principles."

The draftsmen of the USA comment that the standards in it are a cross-section of existing standards, somewhere between the two extremes of "fraud" and "fair, just and equitable" or "sound business principles." They think this is not a mere practical compromise but a balancing of the need for administrative flexibility with the proper claim of legitimate business to as great a degree of specificity as the public interest will permit.<sup>176</sup>

Once a registration statement becomes effective, no stop order may be entered on the basis of a fact known to the administrator on the effective date, unless the proceeding therefor is instituted within thirty days after effectiveness.<sup>177</sup> The stop order may be vacated or modified, upon a finding that the conditions which promoted its entry have changed or that it is otherwise in the public interest to do so.<sup>178</sup>

As is permitted in the case of registering broker-dealers and agents, the administrator, without any hearing, may summarily postpone or suspend registration, pending final determination of proceedings to deny, suspend, or revoke. If he does this, notice of the act must be given promptly and the reasons for it, to applicant, issuer and any person on whose behalf the securities are to be or have been offered. These persons are to be advised that if they submit a written request for a hearing, within fifteen days after receipt of their request the matter will be set down for hearing. If no hearing is requested, and none ordered by the administrator, his order remains in effect until modified or vacated. If anyone asks for a hearing, the administrator should give notice of

174. USA § 306(a) (omitting (G) and (H)); see WIS. STAT. ANN. §§ 551.28(1)(e), (h), (i) (1975).

175. IOWA CODE § 502.10 (1975).

176. L. LOSS & E. COWETT, *BLUE SKY LAW* 327 (1958).

177. IUSA § 209(2); USA § 306(a) ("[F]act" substituted for "fact or transaction").

178. IUSA § 209(5); USA § 306(d).

[the]<sup>179</sup> opportunity for hearing to each of the persons mentioned, and he may modify or vacate the order or extend it until final determination.<sup>180</sup>

### 9. *Securities and Transactions Exempt from Registration Requirements*

For many Iowa corporations the sections exempting certain securities and transactions in securities from the requirements for registration of securities before they can be sold or offered for sale and from requirements for filing sales literature are of major importance. In the past these sections have enabled a large number of corporations lawfully to issue shares, and the holders of the shares later to transfer them even though no registration had been made. The IUSA has some changes in this area that may reduce the number of transactions which are exempt from registration. It also extends to the administrator the power to deny or to revoke any exemption that would otherwise be available, for a particular security or transaction,<sup>181</sup> and it places the burden of proof that an exemption (or an exception from a definition) is applicable upon the person who claims it.<sup>182</sup>

Even though an exemption from registration is available, the sale, purchase or offer is subject to antifraud and other statutory limitations, and any violation of them can lead to liability. These new and revised rules for enforcement are discussed in the next main subdivision of this paper. This section examines the various securities and transactional exemptions, and the administrator's power to deny or revoke them.

a. *Exempt Securities*—Twelve categories of securities are provided an exemption from the requirement that they be registered before they can be sold in Iowa and that the sales literature used in connection with their sales be filed with the administrator. Several other instruments that might have been treated as securities are excluded from that category by virtue of definitions, previously noted, relating to "sale," "offer" and "security."<sup>183</sup> Those so excluded are thereby removed from the applicability of the antifraud and related provisions which do apply to the exempted securities.

(i) *Governmental Issues*—This exemption extends to revenue and other obligations issued by the United States, any state thereof, any political subdivision of a state, or agency or corporate or other instrumentality of any of them, including certificates of deposit for such obligations. The IUSA adds a limitation, not part of the USA but found in Wisconsin, that revenue obligations payable in connection with nongovernmental industrial or commercial enterpris-

179. The section should require the administrator to give notice of *and* opportunity for hearing. As originally drafted by the Project, "and" appeared as "an." This was corrected before the bill was approved by the House. The same error appears in the loose-leaf service version from which the Project was working. CCH BLUE SKY L. REP. ¶ 4926 (Sept. 23, 1971). It is correctly "and" in L. LOSS & E. COWETT, BLUE SKY LAW 331 (1958).

180. IUSA § 209(3); USA § 306(b).

181. IUSA § 204; see notes 277-80 *infra*, and supporting text.

182. *Id.* § 205.

183. See notes 98-108 *supra*, and supporting text.

es are not within the exemption, unless issued by a carrier or public utility or by an issuer of listed securities covered by another exemption.<sup>184</sup>

The predecessor law's comparable provision is, essentially, similar except it contains no reference to revenue obligations. The effect of the change, apparently, is to require registration of most securities issued in connection with municipally supported industrial projects, which, of course, involve no pledging of credit of any governmental body.<sup>185</sup>

(ii) *Securities of Foreign Governments*—The predecessor law exempted securities issued or guaranteed by the Canadian government, its provinces and political subdivisions, and their agencies or corporate or other instrumentalities, to the same extent that it did for securities of the United States and governmental units and subdivisions within the United States.<sup>186</sup> The IUSA and USA expand their comparable exemption to include securities issued or guaranteed by any other foreign government with which the United States currently maintains diplomatic relations, if the security is recognized as a valid obligation by the issuer or guarantor.<sup>187</sup>

Although grammatically the "recognized as a valid obligation" limitation can be read to apply both to Canadian securities and to those of any other foreign government, the discussion during the Project related only to its effect on the latter category and not to the possibility that the existing exemption might thereby be limited.

If the United States should cease to maintain diplomatic relations with a country, securities which were issued and outstanding no longer could be traded on the strength of this exemption; on the other hand, securities issued at a time when diplomatic relations were not maintained could later be traded within the exemption if the conditions are met. Even though this exemption is not available, transactions in the security might be within one of the transactional exemptions.

(iii) *Securities of Banks*—Exempt securities include those issued by (if an interest in or debt of) or guaranteed by any bank organized under the laws of the United States, wherever located, or by any bank, savings institution or trust company organized and supervised under Iowa law.<sup>188</sup> This is narrower than the USA provision which exempts securities issued by banks organized and supervised under the law of any state.<sup>189</sup> It is also narrower, in the same way, than the comparable exemption in the predecessor law.<sup>190</sup>

184. IUSA § 202(1); USA § 402(a)(1); WIS. STAT. ANN. § 551.22(1) (1975). "State," for this purpose, includes any state, territory or possession of the United States, plus the District of Columbia and Puerto Rico. IUSA § 102(13); USA § 401(m). See notes 202-07 *infra*, and supporting text (concerning the types of non-governmental issues which can qualify a revenue obligation for exemption).

185. IOWA CODE § 502.4(1) (1975). See also IOWA CODE ch. 419 (1975).

186. *Id.* § 502.4(1).

187. IUSA § 202(2); USA § 402(a)(2).

188. IUSA § 202(3).

189. USA § 402(a)(3).

190. IOWA CODE §§ 502.4(2), (6) (1975).

As the commentary to the Uniform Act noted, a substantial number of jurisdictions had limited this type of exemption to national banks and of domestic entities or those supervised by local banking authorities.<sup>191</sup> The Project thought it was advisable to limit reliance to local supervision.

(iv) *Securities of Savings and Loan Associations*—Securities issued by (if an interest in or debt of) or guaranteed by any federal savings and loan association, or by any savings and loan or similar association organized and supervised under the laws of Iowa are exempt from registration.<sup>192</sup> The USA applied to associations organized under the laws of any state if authorized to do business in "this state [Iowa]."<sup>193</sup> The Project thought that language parallel to that used in the bank exemption would be appropriate. The old Iowa exemption was only for issues of a "building and loan association of this state,"<sup>194</sup> so the IUSA language does not reduce the coverage.

(v) *Securities of Insurance Companies*—This exemption applies to securities of insurance companies which are both organized under Iowa law and authorized to do business in Iowa.<sup>195</sup> The USA included companies organized under any state's law, but applied the same limitation concerning being authorized to do business in Iowa; it also stated that variable annuity instruments were not within the exemption.<sup>196</sup> The predecessor law exempted only securities issued by an insurance company "under the insurance department of [Iowa]."<sup>197</sup> As an insurance company authorized to do business in Iowa would be supervised by the state's insurance department, this exemption is parallel to those for other financial institutions; it is broader than the predecessor in applying to securities guaranteed by the company as well as to those issued by it, though narrower in excluding companies authorized to conduct an insurance business in Iowa but organized under the laws of some other state.

(vi) *Securities of Credit Unions*—This exemption applies to securities issued or guaranteed by any federal credit union or any credit union or similar association organized and supervised under Iowa law.<sup>198</sup> Although the Uniform Act here contains a similar limit to corporations "organized and supervised under the laws of this State," it includes "industrial loan association" as well.<sup>199</sup> Wisconsin elected to omit the latter category, as did the Project.<sup>200</sup> Unless a credit union is within the terms "savings institution" or "bank," the predecessor law had no comparable exemption.<sup>201</sup>

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191. L. LOSS & E. COWETT, *BLUE SKY LAW* 355 (1958).

192. IUSA § 202(4).

193. USA § 402(a)(4).

194. IOWA CODE § 502.4(6) (1975).

195. IUSA § 202(5).

196. USA § 402(a)(5).

197. IOWA CODE § 502.4(6) (1975).

198. IUSA § 202(6).

199. USA § 402(a)(6).

200. WIS. STAT. ANN. § 551.22(5) (1975).

201. See IOWA CODE § 502.4(6) (1975).

(vii) *Securities of Carriers and Utilities*—An exemption is available for securities issued or guaranteed by a railroad, another common carrier, a public utility or a holding company, if the company is subject to the jurisdiction of the Interstate Commerce Commission, is a registered holding company or its subsidiary, within the meaning of those terms in the Public Utility Holding Company Act of 1935, or is regulated in respect to the security by a governmental authority of the United States, any state, Canada or any Canadian province.<sup>202</sup> This follows the Uniform Act except to omit the provision that the company qualifies if regulated in respect to its rates or charges, as well as in respect to the security.<sup>203</sup> The version adopted by the Project is in substance that found in the predecessor law.<sup>204</sup>

(viii) *Securities and Other Securities of an Issuer of Listed Securities*—A commonly found exemption in state blue sky laws applies to securities listed on stock exchanges. Usually, certain exchanges are designated by name, and the administrator has authority to approve other exchanges for purposes of the exemption. The IUSA exempts any security listed or approved for listing upon notice of issuance, on the New York, American, Midwest and Pacific Coast Stock Exchanges or on any other national securities exchange registered under the 1934 Securities Exchange Act which the administrator by rule designates. The exemption also applies to any other security of the same issuer which is of senior or substantially equal rank, any security called for in subscription rights or warrants so listed or approved, and any warrant or right to purchase or subscribe to a security which would be so exempt.<sup>205</sup> The USA does not include the Pacific Coast Exchange or the language concerning other exchanges, but does assume that others can be included.<sup>206</sup> The predecessor law provided a substantially comparable exemption for securities listed and dealt in on a "recognized and responsible" stock exchange plus other securities of the same issuer, and left it to the Commissioner to designate which exchanges met that test; it provided a procedure for an exchange to follow in obtaining consideration for inclusion, and for the Commissioner to delete either the exchange from recognition or a previously accepted security from the exemption, which are not part of the IUSA. However, the administrator's rule making power, plus his general power to deny or suspend an exemption, would seem to allow him those same powers.<sup>207</sup>

(ix) *Securities of Nonprofit Organizations*—Most state blue sky laws also exempt securities issued by many nonprofit organizations. The USA provides a comprehensive listing of types of organizations, in view of the administrator's

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202. IUSA § 202(7).

203. USA § 402(a)(7).

204. IOWA CODE § 502.4(3) (1975). Prior to 1959 this subsection had referred to regulation or supervision as to rates and charges, as well as to issue of securities. See IOWA CODE § 502.4(3) (1956).

205. IUSA § 202(8).

206. USA § 402(a)(8).

207. IOWA CODE § 502.4(5) (1975). See IUSA § 204 discussed *infra*.

power to deny or revoke the exemption in individual cases.<sup>208</sup> It applies to any security issued by any person organized and operated not for private profit but exclusively for religious, educational, benevolent, charitable, fraternal, social, athletic or reformatory purposes, or as a chamber of commerce or trade or professional association. The IUSA deviates in one important respect—to qualify for the exemption the issuer must first file with the administrator a written notice specifying the terms of the offer and the administrator must not enter an order disallowing the exemption within fifteen days thereafter.<sup>209</sup> This qualification, designed to alert the administrator to the issue, raises questions for future efforts to transfer securities issued before the IUSA became effective or issued in other jurisdictions; most of these transfers may be within one of the transactional exemptions, however.

The predecessor law limited its comparable exemption to securities of nonprofit corporations, but did not include benevolent, charitable, social or athletic among those specifically covered; and it also stated that no part of the issuer's net earnings was to inure to the benefit of any stockholder or issuer.<sup>210</sup>

(x) *Commercial Paper*—Nearly all blue sky laws contain some sort of exemption for commercial paper, but many vary as to whether the paper should be of no more than nine or twelve months maximum maturity. The USA provision, which was followed in the IUSA except to add a qualification found in Pennsylvania, adopted the nine month limit because this conforms to the comparable exemption in the federal securities act.<sup>211</sup>

The basic exemption is for any commercial paper, arising out of a current transaction or the proceeds of which are to be used for current transactions, which evidences an obligation to pay cash within nine months of the date of issue, exclusive of days of grace. The exemption also applies to renewal of such paper if likewise limited, and to any guarantee of the paper or of its renewal. The added qualification excludes from the exemption instances where the paper is proposed to be sold or offered to the public in units of less than \$5,000 to any single person.

The predecessor law originally referred to negotiable promissory notes or commercial paper issued in good faith as part of the usual course of issuer's business, with a maximum twelve month maturity; this was changed in 1974 to substantially the same language as in the IUSA except to refer to "note, draft, bill of exchange, or banker's acceptance" rather than to "commercial paper."<sup>212</sup>

(xi) *Securities Issued in Connection With Employee Benefit Plans*—The SEC and administrators of some states' blue sky laws have taken the position

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208. USA § 402(a)(9). See L. LOSS & E. COWETT, BLUE SKY LAW 360 (1958) (Draftsmen's Commentary).

209. IUSA § 202(9).

210. IOWA CODE § 502.4(4) (1975).

211. IUSA § 202(10); USA § 402(a)(10); PA. STAT. ANN. tit. 70, § 202(c) (1975); 15 U.S.C. § 77c(a)(3) (Supp. IV, 1974).

212. IOWA CODE § 502.4(7) (1975).

that employee benefit plans may involve an offer of a security, an "investment contract," especially where participation of the employee is voluntary and he must contribute in order to participate in the plan. The USA includes an exemption to deal with this situation.<sup>213</sup> There was no comparable provision in the predecessor law. The Project adopted Wisconsin's modification of the USA, plus incorporating a variation of its own.

The exemption applies to any security issued in connection with an employee stock purchase, option, savings, pension, profit sharing or similar benefit plan. (The Project deleted the words "investment contract or" between "any" and "security," and added "option.") If the plan is not qualified under *Internal Revenue Code* section 401, and if it provides for employee contributions, the exemption is not available unless the administrator is given written notice of the plan's terms at least thirty days before the plan's inception.<sup>214</sup> Both Iowa and Wisconsin omit the USA language requiring notice of the terms of all plans before they take effect, or, as to plans already in effect, within sixty days after the Act becomes effective. However, this does not clarify the position of an unqualified plan in effect when the IUSA became effective.

(xii) *Securities Issued by Cooperatives*—The USA includes a place to insert an exemption for securities issued by cooperatives, but its drafters found such variations in provisions to this effect among existing statutes that they concluded it was not practicable to draft a specific exemption for cooperatives.<sup>215</sup> The predecessor law exempted securities of cooperatives organized under Iowa law to sell, market or handle agricultural, dairy or livestock products or to manufacture products from such products, or to operate a rural telephone system among its subscribers.<sup>216</sup> The Project has included an exemption of broader scope in some respects, but narrower in others. It exempts only stock or a similar security (including a patronage refund certificate), if issued by an agricultural cooperative association,<sup>217</sup> by a cooperative housing association within *Internal Revenue Code* section 216(b)(1), whose activities are limited to owning, leasing, managing or constructing residential properties for its members (plus activities incidental thereto), or by a mutual or cooperative association organized under Iowa laws relating to cooperatives<sup>218</sup> that deals in commodities or services in transactions primarily with and for the benefit of its members.<sup>219</sup>

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213. USA § 402(a)(11). See L. LOSS & E. COWETT, BLUE SKY LAW 361 (1958) (official comment).

214. IUSA § 202(11). See WIS. STAT. ANN. § 551.22(10) (1975).

215. USA § 402(a)(12). See L. LOSS & E. COWETT, BLUE SKY LAW 362 (1958) (Draftsmen's Commentary).

216. IOWA CODE § 502.4(10) (1975).

217. The term includes a cooperative association as defined in the federal Agricultural Marketing Act (or a federation of such associations if having similar powers), if the security qualifies the holder for membership (or, if a patronage refund, is issuable only to members), and if it is transferable only to issuer or to a successor in interest of holder who qualifies for membership.

218. IOWA CODE chs. 497, 498, 499 (1975).

219. IUSA § 202(12).

To qualify for exempt status, the security must be part of a class issuable only to persons who deal in business transactions with issuer, must be transferable only to issuer or to a successor in interest who qualifies for membership in issuer, and the holder must be entitled to no dividend other than patronage refund except on complete or partial liquidation.<sup>220</sup>

(xiii) *Exemptions for Securities Provided in Predecessor Law Which Have Been Omitted*—Two categories of securities exemptions in the predecessor law were not included in the USA and have not been retained in the IUSA.

One is for securities evidencing debt due in connection with conditional sales contracts to acquire personal property.<sup>221</sup> To the extent that such an exemption is desirable, it may be met through the exemption for commercial paper, already noted, or by fitting the situation into one of the categories of exempt transactions.

The other is for stock which has been outstanding and in the hands of the public for a substantial period of time, which has a history of paying dividends (or principal or interest due) for at least the preceding five years, and which, if not common stock, has no existing default in interest, principal or dividends. Securities of a more recent vintage could qualify if issued to refund or refinance a predecessor issue that, combined, exhibited the same history.<sup>222</sup> In many instances transactions involving such a security will be within one of the transactional exemptions.

b. *Exempt Transactions*—Securities which are not exempt from registration requirements may, nevertheless, be sold or offered for sale in Iowa without registration if the transaction involved falls within one of a number of exempt transactions. In addition, the provisions regarding filing of sales literature are inapplicable. The Uniform Act provides twelve such categories; both the IUSA and its predecessor have fifteen, but the three differ in a number of respects. As will be noted later, the administrator may deny or revoke the exemption with respect to a specific security or transaction.<sup>223</sup>

(i) *Isolated Transactions*—Any isolated transaction in a security, by a person other than its issuer, is exempt whether or not the transaction is effected through a broker-dealer.<sup>224</sup> This permits many holders of unregistered securities to dispose of them without having first to get them registered. There is no attempt to define "isolated;" in some instances where it is questionable that the transaction is "isolated" the circumstances may be such that another one or more of the transactional exemptions may apply.

The comparable predecessor provision refers to a transaction by or on behalf of the owner of a security who is not its underwriter, which is not made

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220. *Id.*

221. IOWA CODE § 502.4(9) (1975).

222. *Id.* § 502.4(8).

223. See IUSA § 204. This section is discussed in notes 277-80 *infra*, and supporting text.

224. IUSA § 203(1) (following USA § 402(b)(1)).

in the course of repeated or successive transactions of a like character by the owner or on his account by his representative.<sup>225</sup> The simpler terminology of the IUSA does not suggest, as does the language of the ISL, that a holder of many securities of different issuers who wants to liquidate a large portion of his holdings could fall out of the "isolated transaction" category.

(ii) *Certain Non-Issuer Distributions*—The USA contains an exemption for transactions in outstanding securities if a recognized securities manual contains certain information about the issuer, or if the security has a fixed maturity, interest or dividend provision and there has been no default under such provision for the current and three preceding fiscal years (or for the issuer's life, if shorter than that time).<sup>226</sup> The ISL has an exemption comparable only to the "registered securities manual" aspect of this.<sup>227</sup> The IUSA adopts the first but not the second part of the exemption, and adds several other situations to the category.

Unlike the USA provision, the securities manual must not only be "recognized," whatever that may mean, but also "approved by the administrator"—this may supply some content to "recognized." The manual must contain the names of issuer's officers and directors, a balance sheet of issuer as of a date within eighteen months from the time of the transaction involved, and a profit and loss statement for either the fiscal year preceding the date of the balance sheet or the most recent year of operations. The added classes of exempt transactions apply to securities issued by an issuer who has at least one class of securities currently registered under either the Securities Exchange Act of 1934, the Investment Company Act of 1940, or the Iowa Blue Sky Law.<sup>228</sup>

The thrust of this provision seems to be to permit non-issuer transactions in unregistered securities when adequate financial information about the issuer is available, through securities manuals or public records.

(iii) *Unsolicited Non-Issuer Transactions by Broker-Dealers*—Both the IUSA and the USA exempt from registration requirements sales of outstanding securities effected by or through a registered broker-dealer pursuant to an unsolicited order or offer to buy. The administrator by rule may require that the customer acknowledge that the transaction was unsolicited by the broker-dealer.<sup>229</sup> The comparable ISL provision was along the same lines; but also provided that the transaction not be, directly or indirectly, for the benefit of the issuer.<sup>230</sup>

(iv) *Underwriting Transactions*—Both the IUSA and the USA provide exemption for any transaction between issuer (or other person on whose behalf

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225. IOWA CODE § 502.5(3) (1975).

226. USA § 402(b)(2).

227. IOWA CODE § 502.5(12) (1975).

228. IUSA § 203(2).

229. IUSA § 203(3); USA § 402(b)(3).

230. IOWA CODE § 502.5(13) (1975).

an offering is made) and underwriter, or among underwriters.<sup>231</sup> There is no comparable exception in the predecessor law. The drafters of the USA comment that most blue sky laws did not spell out this exemption but it usually was read in as a matter of necessity; and it is included as an exemption rather than as an exclusion from "sale" or "offer" to subject the transaction to the antifraud provisions of the Act.<sup>232</sup>

(v) *Whole Mortgages*—A sale of bonds or notes which are directly secured by a real estate mortgage, security interest, deed of trust, or agreement for the sale of real estate or chattels, is an exempt transaction if the security instrument and all bonds or notes secured thereby are sold as a unit.<sup>233</sup> Except for substituting "notes" for "other evidence of indebtedness," the IUSA to this extent follows the comparable USA provision.<sup>234</sup> The IUSA, however, then adds a provision that the transaction shall not be deemed to involve a sale "as a unit" if (a) the bonds and notes are part of a single issue including other bonds or notes secured by interests in real estate or chattels owned or developed by the same person or by persons affiliated with that person, or (b) there is a right to have substitution by or recourse against or guarantee by the developer or any person other than the person primarily obligated on the bond or note.<sup>235</sup> This addition was inspired by some of the recent practices in sales of securities based on real estate mortgages.

The predecessor law had two related exemptions. The first originally applied where the mortgage plus all bonds and notes secured by it were sold to a single purchaser at a single sale. In 1974 it was replaced by language substantially identical with the Project's proposal.<sup>236</sup> The second treated as an exempt transaction the sale of bonds or notes secured by mortgage on real estate or tangible personal property situated within Iowa if sold to not more than twenty purchasers and if the total face value of bonds or notes secured by a single mortgage did not exceed \$50,000.<sup>237</sup> This latter provision is not duplicated in the IUSA.

(vi) *Sales by Executors and Certain Other Fiduciaries*—A transactional exemption is available for any judicial sale or any transaction executed by an executor, administrator, sheriff, marshal, receiver, trustee in bankruptcy, guardian, custodian or conservator, made without any purpose of evading the Act.<sup>238</sup> The only variation from the USA provision is an addition, made also by Pennsylvania and Wisconsin, of the words "any judicial sale or."<sup>239</sup> The ISL

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231. IUSA § 203(4); USA § 402(b)(4).

232. L. Loss & E. Cowett, *BLUE SKY LAW* 365 (1958).

233. IUSA § 203(5).

234. USA § 402(b)(5).

235. IUSA §§ 203(5)(a), (b).

236. IOWA CODE § 502.5(7) (1975).

237. *Id.* § 502.5(10).

238. IUSA § 203(6).

239. USA § 402(a)(6); PA. STAT. ANN. tit. 70, § 203(k) (1975); WIS. STAT. ANN. § 551.23(6) (1975).

provision would seem to refer to sales by and for such persons; it omits reference to evasatory purposes.<sup>240</sup>

(vii) *Sales by Pledgees*—A transactional exemption is available for any transaction executed by a bona fide pledgee without any purpose of evading the Act.<sup>241</sup> The essentially similar ISL provision refers to pledge holders and mortgagees, offering to sell or selling a security pledged in good faith as security for the debt, in order to liquidate the debt.<sup>242</sup>

(viii) *Sales to Institutional Buyers and Broker-Dealers*—An offer or sale is exempt if made to a bank, savings institution, trust company, investment company (as defined in the Investment Company Act of 1940), pension or profit sharing trust, or other financial institution or institutional buyer, or to a broker-dealer, whether the purchaser is acting for itself or in some fiduciary capacity.<sup>243</sup> The theory of this exemption is that these purchasers are "sophisticated" buyers who do not need the protection provided by registration but who should have the benefit of antifraud protection.<sup>244</sup>

The comparable ISL provision also referred to transfer or delivery, did not refer to the capacity in which the acquisition was made, and required the broker or dealer to be actually engaged in buying and selling securities as a business; all of these points seem to be covered in the USA version, or to be unimportant. Until 1974 the ISL also exempted transfers to "any corporation."<sup>245</sup> As many corporations, especially small ones, do not have the sophistication of institutional investors, the Project decided not to include them within this category and this decision was reflected in the 1974 amendments to the ISL.<sup>246</sup>

(ix) *Offerings to a Limited Number of Persons*—Many corporations are owned by a small group of investors who are active in the business carried on or familiar with it. They do not need the protection of registration; compliance with requirements for registration could impose an excessive burden on the corporation. A wide variety of transactional exemptions intended to cope with this problem have been developed, some of which apply to preorganizational transactions and some to transactions after organization.<sup>247</sup> The IUSA provision for post-incorporation transactions differs considerably from that in the USA, less so from that in the predecessor law, but it adds some new elements which representatives of Iowa corporations must keep in mind.

The IUSA provision permits any issuer to sell, as part of a single issue, securities (other than fractional undivided interests in oil, gas or other mineral

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240. IOWA CODE § 502.5(1) (1975).

241. IUSA § 203(7); USA § 402(b)(7).

242. IOWA CODE § 502.5(2) (1975).

243. IUSA § 203(8); USA § 402(b)(8).

244. L. LOSS & E. COWETT, BLUE SKY LAW 367 (1958).

245. See IOWA CODE § 502.5(5) (1973), as amended, IOWA CODE § 502.5(5) (1975).

246. See IOWA CODE § 502.5(5) (1975).

247. L. LOSS & E. COWETT, BLUE SKY LAW 369-72 (1958).

leases, rights and royalties and other than interests in a limited or general partnership organized under the laws of or having its principal place of business outside Iowa) within any period of twelve consecutive months to not more than 35 purchasers in Iowa.<sup>248</sup> A purchaser who is a bona fide institutional investor purchasing for its own account need not be included in the 35, and sales to it are within the exemption for transactions with such investors. The issuer must reasonably believe that all of the up-to-35 purchasers are purchasing for investment. No commission or other remuneration may be paid or given, directly or indirectly, on account of such sale, *unless* the administrator has adopted a rule permitting payment, or *unless* he issues such an order for the particular transaction upon written application for it showing good cause to allow payment. Within thirty days after each of the sales under this exemption the issuer is to file with the administrator a report of the sale, setting out the names and addresses of the issuer and the purchasers involved plus the total amount of securities sold for which this exemption is claimed. However, unlike the related provision of the ISL, no report has to be filed until the number of purchasers which is to be counted towards the 35 limit exceeds ten. This means that when sales have been made to eleven, within this exemption, a report should be filed covering all eleven sales, and appropriate reports filed for each transaction thereafter during the period. Issuer also is in the position of being able to determine when the twelve-month period begins.<sup>249</sup>

The related USA provision limits to *offers* directed toward not more than ten persons (other than institutional investors) in the state, whether offeror or any of the offerees are in fact present in the state. It contains a belief in purchase for investment and a no commission requirement, and provides that the administrator by rule or order may withdraw or further condition the exemption for any security or type of security, may increase or decrease the number of offerees, and may waive either the belief or the no commission requirement.<sup>250</sup> It has no limits as to type of securities.

Until 1974 the ISL excluded the mineral types of interests, but not partnership ones, and limited the exemption to *sales* to not more than twenty excluding purchasers of exempt securities, purchasers in transactions otherwise exempt or persons purchasing part of an offering registered under the law, with the no commission requirement (but with no way to modify or waive it) and with a report of sale requirement applicable to all such sales.<sup>251</sup> This was changed in 1974 along the lines of the IUSA.<sup>252</sup>

Although the number of buyers permitted under the IUSA (35) is larger than the number specified in the ISL (20), the actual effect may be to reduce

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248. IUSA § 203(9)(a).

249. *Id.*

250. USA § 402(b)(9).

251. See IOWA CODE § 502.5(15) (1973), as amended, IOWA CODE § 502.5(15) (1975).

252. See IOWA CODE § 502.5(15) (1975).

the number of buyers that can participate in such an exempt transaction. Formerly, it was arguable, at least, that preorganization subscribers could acquire securities in exchange for their subscription and not be counted toward the twenty, with the exchange not requiring registration. Under the IUSA, any preorganization subscriber who receives a security pursuant to his subscription must be considered as within the 35 permitted to purchase without registration. Only purchasers who are institutional investors can now be disregarded in determining whether the limited offering exemption is available. It will also be important for the seller to establish a basis for his belief that the securities are being acquired by a person who is purchasing for investment. This may lead to greater use of "investment letters," to be provided by the purchaser.

(x) *Preorganization Subscriptions by a Limited Number of Persons—*

As Iowa law does not require a corporation to have any minimum capital before it begins to operate,<sup>253</sup> it is relatively easy to form a corporation in Iowa before obtaining commitments for its financing. Several members of the Project argued that the exemption for preorganization subscriptions could therefore be omitted, letting the basic limited offering exemption provide the necessary coverage. However, recognizing that there could be other jurisdictions where preorganization solicitation was more common, and that it still did occur to some extent in Iowa, the ultimate decision was to retain an exemption for this type of situation but to make it narrower than under the USA and under the predecessor law while providing some possible enlargement of the basic limited offering provision (as was noted in the preceding section).

Accordingly, any offer or sale of a preorganization subscription is exempt, if: no commission or other remuneration is paid or given, directly or indirectly, for soliciting any prospective subscriber; the number who subscribe does not exceed ten; no subscriber makes any payment as part of his subscription and before the security subscribed to is issued to him; and no public advertising of the offer is made.<sup>254</sup> This is the language of the USA except for the "no public advertising" approach. As the official comment to the USA noted, under that provision public advertising would be permitted, but that was in keeping with the assumed need to obtain minimum capital before a corporation could commence business.<sup>255</sup> The same comment noted that under the USA (true also under the IUSA), there can be no payment on the subscription before effective registration unless some other exemption is available.

The predecessor law exempted the sale of subscriptions for or securities of a corporation prior to its incorporation if no commission was received on account of the sale and if the number of subscribers did not exceed 25.<sup>256</sup> This was reduced to ten in 1974 and the no advertising requirement was added.<sup>257</sup>

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253. 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 191 (1969).

254. IUSA § 203(10).

255. USA § 402(b)(10); L. LOSS & E. COWETT, *BLUE SKY LAW* 374 (1958).

256. See IOWA CODE § 502.5(9) (1973), as amended, IOWA CODE § 502.5(9) (1975).

257. See IOWA CODE § 502.5(9) (1975).

While the IUSA reduces the number of subscribers permitted for purposes of this exemption (from 25 to 10), both it and the predecessor appear to contemplate subscribers wherever located, not just those located in Iowa.

(xi) *Offers to Existing Security Holders*—A transactional exemption is available for transactions pursuant to an offer of its securities by an issuer to persons already holding its securities, if the transaction involves the conversion of convertible securities, the exercise of non-transferable rights or warrants, the exercise after issue of transferable rights or warrants which are exercisable within ninety days of their issuance, and the purchase of securities pursuant to preemptive rights. To qualify, there must be no commission or remuneration (other than a standby commission) paid or given directly or indirectly for soliciting any security holder in Iowa.<sup>258</sup> Although based on the USA, this is a considerably different statement of the exemption, designed to narrow it to the three described types of transactions, and to eliminate the possibility of paying commission where a pre-offering notice was filed with the administrator and he did not disallow such payments.<sup>259</sup> The objective was to provide no exemption for such a transaction if it had been stimulated by compensation.

The ISL has one section which was almost identical to the USA provision except for omitting authority to pay commission if there was a pre-offering filing and no disallowance.<sup>260</sup> Another section dealt specifically with the exercise of a conversion right, limiting the exemption to those instances where the security bearing the right to convert had been registered in Iowa or, when sold, was exempt from registration, and the security delivered in exchange if sold at its conversion price would fall within the class of securities entitled to register by qualification in Iowa. It also provided that the par value of the surrendered security would be considered to be the "conversion price."<sup>261</sup> The IUSA simplifies substantially the treatment of conversion transactions.

(xii) *Offerings During SEC and Iowa Blue Sky Law Waiting Period*—An offer is available for offers, but not for any sales, of any security for which registration statements have been filed both under the IUSA and the Securities Act of 1933, if no stop order or denial order is in effect, and if no proceeding is pending under either law.<sup>262</sup> Except for substitution of commas for parentheses, this is the language of the comparable USA provision, and of the predecessor law, as well.<sup>263</sup> It permits an issuer to distribute information concerning a proposed issue after the registration is on file, during the waiting period before it can become effective.

(xiii) *Reclassification and Reorganization*—Transactions in connection with reclassification of securities or reorganization involving the exchange of

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258. IUSA § 203(11).

259. USA § 402(b)(11).

260. IOWA CODE § 502.5(4) (1975).

261. *Id.* § 502.5(8).

262. IUSA § 203(12); USA § 402(b)(12).

263. IOWA CODE § 502.5(14) (1975).

securities, merger, consolidation, or sale of assets, in consideration in whole or in part of issuance of securities of issuer or of any other person may be exempt.<sup>264</sup> The transaction must be incident to a vote by security holders of an issuer, or to a written consent or resolution of some or all such holders (as permitted in issuer's articles or the applicable statute), to issuer's partnership agreement, or to a declaration of trust or trust indenture or any agreement among security holders. One of four alternative qualifications must also be met: (1) a party to the transaction must have filed proxy or informational materials pursuant to section 14(a) or 14(c) of the Securities Exchange Act of 1934 or section 20 of the Investment Company Act of 1940 and, at least ten days before the meeting of security holders called to approve the transaction, must also have filed those materials with the administrator and distributed them to each security holder of each party to the transaction; (2) a party to the transaction excused from registration under section 12(g)(2)(G) of the Securities Exchange Act of 1934, but required by the laws of its domiciliary state to file proxy materials with an agency of that state, if it has filed those materials within that state and makes the same filings with the administrator and distribution to security holders that the preceding alternative calls for; (3) one party to a merger owns at least 90 percent of the outstanding shares of each class of stock of each other party to the merger; or (4) a party to the transaction files with the administrator and distributes to security holders of each party to the transaction such materials, within such time, as the administrator by rule or order may specify.<sup>265</sup>

The USA does not provide a similar transactional exemption, as it treats this type of transaction as "no sale."<sup>266</sup> This was the attitude originally taken as to similar transactions by the SEC in its Rule 133; that attitude no longer is being followed by the SEC. The consequence of the change is to exempt the transaction from requirements for registration of the securities involved and to make applicable antifraud and other provisions providing protection for the security holders involved.

The approach taken is also consistent with that of the ISL, which had separate transactional exemptions for securities in reorganizations and for those in mergers and consolidations.<sup>267</sup> The IUSA version drops provisions that the reorganization "be in good faith and not for the purpose of avoiding" the ISL, and that the Commissioner "approve" the proposed plan of merger and consolidation.

The genesis of the IUSA provision is in Pennsylvania's efforts to deal with the area; it has been somewhat restated, adding the second and third alterna-

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264. Since normally securities are issued by an issuer, the intent here is to include securities issued by any party to the reorganization which go to any holder of securities in any other party to the reorganization, as part of the reorganization process.

265. IUSA § 203(13).

266. USA § 401(j)(6)(C).

267. IOWA CODE §§ 502.5(4), (6) (1975).

tives, and dropping a provision that none of the alternatives need to be met if not more than 25 percent of the security holders are residents of the state.<sup>268</sup>

(xiv) *Transactions Incident to Judicially Approved Reorganization*—A transaction is exempt if incident to a judicially approved reorganization in which a security is issued in exchange for one or more outstanding securities, claims, or property interests, or is partly in such exchange and partly for cash.<sup>269</sup>

This too was treated by the USA as not a sale.<sup>270</sup> The language is taken from Wisconsin's comparable approach.<sup>271</sup>

The ISL does not have a comparable exemption, but it does provide exemption for offers or sales of securities by registered dealers in the ordinary and usual course of business, if issued in exchange for other securities as part of such a plan of reorganization. The Commissioner had authority to prohibit the resale of any such security.<sup>272</sup>

(xv) *Dividends in Securities*—An exemption is available for the distribution of securities as a dividend, if the distributor of the dividend is also issuer of those securities, and if the recipient gives no value other than surrendering a right to a dividend in cash or property when he may elect to take either cash, property, or the security tendered him.<sup>273</sup> The USA treats this as "no sale."<sup>274</sup> The IUSA approach is similar to that in Wisconsin which, however, permits the exemption to extend not only to dividends in stock but also to include stock issued by others than the distributor.<sup>275</sup>

The comparable provision in the predecessor law was limited to corporations actively engaged in the business authorized in their charter, for distributions of stock, bonds or other securities as a dividend.<sup>276</sup>

(xvi) *Transactional Exemptions Provided by Predecessor Law Which Have Been Omitted*—No transactional exemptions in the ISL are without some IUSA counterpart, although, as the discussion has indicated, those counterparts may vary in differing degrees.

c. *Denial and Suspension of Exemptions*—The administrator by order may deny or revoke any securities or transactional exemption with respect to a specific security or transaction.<sup>277</sup> The Commissioner, under the ISL, had similar power only with respect to a very limited number of transactional

268. PA. STAT. ANN. tit. 70, § 203(o) (1975); cf. WIS. STAT. ANN. § 551.23(13) (1975).

269. IUSA § 203(14).

270. USA § 401(j)(6)(D).

271. WIS. STAT. ANN. § 551.23(13) (1975).

272. IOWA CODE § 502.5(11) (1975).

273. IUSA § 203(15).

274. USA § 401(j)(6)(B).

275. WIS. STAT. ANN. § 551.23(14) (1975).

276. IOWA CODE § 502.5(4) (1975).

277. IUSA § 204.

There is no comparable section in the ISL.<sup>288</sup>

The remedies available for violation of this section are quite different from the federal remedies available under section 16(b), and are discussed later in this paper.

### C. *Market Manipulation*

Recognizing that there were various means by which the price of a security could be manipulated, and the market for the security affected not be fair and honest, Congress also made unlawful a number of such devices.<sup>289</sup> Although the USA does not include a section of this type, Pennsylvania did adopt such a section, based on three subsections from the federal act,<sup>290</sup> and the Project elected to incorporate this approach.<sup>291</sup>

Thus, it is unlawful for any person directly or indirectly, in Iowa, to try to create a false or misleading appearance of active trading in a security or as to the market for a security by effecting a transaction in it which involves no change in beneficial ownership, or by entering one or more orders to purchase or sell the security at substantially the same time and for substantially the same price that opposite orders are known to be in process for the same person or an affiliate. It is also unlawful to effect a series of transactions in a security (whether done alone or with others), to create actual or apparent active trading or to raise or depress the price, in order to induce others to buy or sell a security. The third item of unlawful conduct is to induce purchase or sale of any security by circulating or disseminating information that one or more persons are engaged in market manipulation and that this will affect the price, where the actor receives consideration from the alleged manipulator or is himself attempting to engage in transactions in the security.

Under the ISL, it was a felony to knowingly make false or fraudulent representations to another to induce him to purchase a security.<sup>292</sup> Except for this, there is no clear counterpart in the predecessor law.

### D. *Prohibited Transactions of Broker-Dealer and Agent*

The IUSA also adopts a Pennsylvania section, not found in the USA, which prohibits a broker-dealer or an agent from effecting or attempting to effect a transaction in any security in Iowa by improper means. These means are stated to include any manipulative, deceptive or other fraudulent scheme, device or contrivance, fictitious quotation, or violation of the Act or rule or order under it.<sup>293</sup> The ISL does not have similar language.

288. See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 316 (1969).

289. 15 U.S.C. § 78i (Supp. IV, 1974).

290. PA. STAT. ANN. tit. 70, § 402 (1975). See also WIS. STAT. ANN. § 551.42 (1975).

291. IUSA § 403.

292. IOWA CODE § 502.28 (1975).

293. IUSA § 404 (following PA. STAT. ANN. tit. 70, § 403 (1975)).

### E. *Misleading Filings*

The USA made unlawful any filing of any document with the administrator or in any proceeding under the Act, which contained a statement that was, at the time and in the light of the circumstances under which made, false or misleading in any material respect.<sup>294</sup> Pennsylvania and Wisconsin expand their comparable sections to include the omission to state a material fact necessary in order to make such statements not misleading.<sup>295</sup> The IUSA adopts the latter approach, but speaks in terms of a statement of material fact which is false or misleading, rather than a statement which is false or misleading in any material respect.<sup>296</sup> The ISL does not have similar language.

### F. *Misrepresentation of Governmental Approval*

The USA includes a section making it unlawful to represent that registration of a security or a broker-dealer or an agent, or the availability of an exemption, imports governmental approval or recommendation.<sup>297</sup> Pennsylvania restated the section to separate the treatment of securities from that for broker-dealers and agents.<sup>298</sup> The ISL did not have similar language, but did prohibit state officials and employees from using their official capacity to promote transactions in securities.<sup>299</sup> The Project adopted the Pennsylvania approach and added to it much of the ISL language referred to.

As a result, registration of a broker-dealer or an agent may not be asserted or implied to represent that the person registered is sponsored, recommended or approved, or that his abilities or qualifications have been passed on, by the administrator. A statement may be made that he is registered, if the effect of registration is not misrepresented.<sup>300</sup>

The fact that a registration statement for a security has been filed or has become effective, or that an exemption from registration is available for the security, may not be represented as implying that any document filed under the Act is true, complete and not misleading, or that there has been any governmental determination of the merits or qualifications of, or recommendation or approval of, any person, security, or transaction.<sup>301</sup>

A state official or employee may not use his name in his official capacity to endorse or recommend the organization or promotion of any issuer, or the sale of its securities to the public; and no one may use the stationery of the state or of any official thereof in connection with such a transaction.<sup>302</sup>

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294. USA § 404.

295. PA. STAT. ANN. tit. 70, § 407(a) (1975); WIS. STAT. ANN. § 551.54 (1975).

296. IUSA § 405.

297. USA § 405.

298. PA. STAT. ANN. tit. 70, §§ 407(b), (c) (1975).

299. IOWA CODE § 502.29 (1975).

300. IUSA § 406(1).

301. *Id.* § 406(2).

302. *Id.* § 406(3).

### G. Misstatements in Publicity

The Project discussed the fact that misleading publicity could not only induce a sale or purchase, which was being treated as unlawful, but also it could persuade the owner of a security not to sell it, and that no clear remedy was available for any injury resulting from that decision. The USA, the several state laws examined, and the ISL had no provision directed to this problem. To deal with the problem and also with possible difficulties arising when the disseminator of misleading information is not himself buying or selling or acting for someone who is, a new section was adopted. The new section provides that unlawful conduct includes the making (by any person), in any public report, or press release, or other information made generally available to the public, of any statement of material fact relating to an issuer which under the circumstances is false or misleading, if it is reasonably foreseeable that the statement will induce another to buy, sell or hold securities of the issuer.<sup>303</sup>

## V. CIVIL LIABILITY

The Uniform Act has one section on civil liability. Although the IUSA has seven sections, most are based on material in the one USA provision. The reorganization of the material and many of the additions to it are based on the Pennsylvania approach.

### A. Violation of Registration and Related Requirements

The first section pertains to the liability of any person who: (1) violates at least one of three sections of the Act;<sup>304</sup> (2) violates any material condition imposed under section 201<sup>305</sup> (referring, in part, to escrow arrangements and keeping registration current); or (3) offers or sells a security at a time when he "has committed"<sup>306</sup> a material violation of the requirement for registration as a broker-dealer or agent, or commits a material violation of any order issued by the administrator under the Act.<sup>307</sup>

This is closely akin, in substance, to the comparable USA and Pennsylvania approach, although there is considerable difference in language.<sup>308</sup> Both of the latter acts use "offers or sells . . . in violation" where Iowa uses "violates"—but the meaning should be the same. The Uniform Act includes

303. *Id.* § 407.

304. *Id.* § 201 (sales in Iowa of unregistered securities, where no security or transactional exemption is available); *id.* § 208(12) (failure to make required delivery or prospectus, final prospectus or offering circular); *id.* § 406(2)(b) (misrepresentation as to the effect of filing registration materials, so as to imply that the security has government approval).

305. See division III, §§ B(9)(a), (b) *supra*.

306. Although the language "has committed" suggests a past offense, it should be interpreted not to apply to violations at some time in the past if the person who should be registered is in fact registered at the time of the offer or sale in question, and is not violating the IUSA at those times.

307. IUSA § 501.

308. See USA §§ 410(a)(1), (2); PA. STAT. ANN. tit. 70, § 501(a) (1975).

violations of rules or orders concerning sales and advertising literature,<sup>309</sup> which Pennsylvania and Iowa do not encompass within their provision except, in Iowa, if it violates an order. The USA may not include as many violations of orders as the Iowa provision probably reaches.

The violator "shall be" (USA says "is") liable to the person "purchasing" (USA says "buying") the security "offered or sold in connection with such violation."<sup>310</sup>

The injured party may sue either at law or in equity to recover the consideration paid for the security, plus interest at the legal rate<sup>311</sup> from the date of payment, costs and reasonable attorneys' fees, less the amount of any income or distribution received on the security,<sup>312</sup> if he still owns the security and tenders it.<sup>313</sup> If he no longer owns the security, his action is for damages, defined as the amount recoverable on a tender less the *value* of the security at the time it was disposed of by purchaser and interest on that value at the legal rate from the date of disposition. The USA does not have a comparable definition of "damages;" this language is found in the Pennsylvania act.<sup>314</sup>

Iowa adds a sentence not found in other acts, that any person on whose behalf the offering is made and any underwriter of the offering are also jointly and severally liable under this section (the underwriter's liability is limited to the total price at which the securities he has underwritten and distributed to the public were offered to the public).

Notice may be given by service as in other civil actions or by certified mail to the last known address of the "person liable."

The predecessor law treated sales or contracts for sale which violated the law as voidable at the purchaser's option, and permitted a tender for a price essentially like that of the IUSA.<sup>315</sup> It also allowed the seller to offer in writing to repurchase for the purchase price plus interest, subject to acceptance of that offer in thirty days; and barred purchaser's action once this offer was made. This latter concept is now found in the IUSA section on limitations on rights of action. The new Act imposes civil liability when the offer violates one of the specified provisions, even though the sale does not; this may have been true under the predecessor law.<sup>316</sup>

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309. See IUSA § 602.

310. The USA and Pennsylvania statute have no language comparable to that in the last quotation in the text, but the concept probably is implicit in those Acts; both say "from him," which Iowa omits.

311. The USA used 6 percent per year.

312. The USA says only "income;" Iowa adds the concept that the income or distribution to be taken into consideration includes both those in cash and those in kind.

313. Tender requires only notice of willingness to exchange the security for the amount specified in the statute. The USA does not have this language, but it is found in both Pennsylvania and Wisconsin. See Wis. STAT. ANN. § 551.59(1) (1975).

314. Wisconsin also includes this.

315. Interest was at 6 percent, or at the rate on the security if it was interest-bearing. IOWA CODE § 502.23 (1975).

316. The making of a non-exempted offer before the effective date of registration can

### B. *Fraudulent Practices*

This section sets out the civil remedies available under the statute for violation of the various prohibitions in the Act against what are designated false or fraudulent practices.

The first two subsections apply to violations of the antifraud provision<sup>317</sup> and the prohibitions against broker-dealers or agents effecting (or attempting to effect) transactions by improper schemes.<sup>318</sup> Any person who offers to sell or sells a security, or offers to buy or buys in violation of those two sections can be held to be liable if the other party to the transaction did not know of the violation and if the violator fails to sustain the burden of proof that he<sup>319</sup> did not know and in the exercise of reasonable care could not have known of the violation. The relief available is identical to that described in the preceding section, as is the liability of the person on whose behalf the offering was made and the underwriter. Also, similar provisions regarding tender and notice apply.<sup>320</sup>

The persons responsible for the misleading impressions or information may, however, themselves be neither purchaser nor seller of securities. Three sections which bear on this, dealing with market manipulation,<sup>321</sup> misleading filing of material information (or omissions of such information) with the administrator,<sup>322</sup> and misstatements in publicity,<sup>323</sup> can lead to liability on the part of any person who willfully and knowingly participates in violation of these sections. The liability extends to any person who purchases or sells a security at a price which was affected by the violating act or transaction; however, someone who holds the security as a result of the violation, rather than selling it, is not entitled to relief under this subsection. Damages are not to exceed the difference between the price at which the injured party bought or sold the security and the market value that should have been applicable absent the violation (plus interest at the legal rate, costs and reasonable attorneys' fees).<sup>324</sup>

The remaining subsection applies to trading on inside information. Unlike section 16(b)<sup>325</sup> where recovery belongs to the corporation and is the wrongdoer's profits, this section permits anyone who can show that he was or might have been on the opposite end of the affected transaction to recover damages.

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create no enforceable right to civil relief in the offeree unless a sale follows. But where it does, the buyer may recover even though the contract was not made until after the registration became effective.

317. IUSA § 401.

318. *Id.* § 404.

319. The drafters were unable to come up with a neutral word that seemed adequate at this point, so here and in several other comparable places used "he, she or it."

320. IUSA §§ 502(1), (2).

321. *Id.* § 403.

322. *Id.* § 405.

323. *Id.* § 407.

324. IUSA § 502(3).

325. 15 U.S.C. § 78p(b) (Supp. IV, 1974).

In open market operations the violator may therefore be liable to a number of people, as none will have to establish that their transaction can be traced to violator's. This subsection says that the violator, who trades, "shall be deemed to be unjustly enriched," and to be liable for damages equal to the difference between the price at which the security was traded and the market value it would have had if the inside information had been publicly disseminated and a reasonable time had elapsed for the market to absorb the information (plus interest at the legal rate, costs and reasonable attorneys' fees). A defense may be available, if defendant can prove that plaintiff would have engaged in the transaction at the same price even if the information had been revealed to him.<sup>326</sup>

The approach of the first of these four subsections, applying to sellers of securities who violate antifraud provisions, originated in the Securities Act of 1933, section 12(2),<sup>327</sup> and was included in the USA.<sup>328</sup> Pennsylvania and Wisconsin expanded the concept to include purchasers as well as sellers,<sup>329</sup> and the second subsection reflects this. The principal difference between the Iowa version and those of the other two states is the placing of liability for violation of registration requirements in a section separate from that of liability of seller for violating antifraud provisions. There is no change in substance. The third subsection, involving the effects of market manipulation and certain public misstatements, does not have a corresponding USA provision but is based on language added by Pennsylvania and Wisconsin,<sup>330</sup> which, however, related only to market manipulation. The Iowa use of "willfully and knowingly," instead of "willfully" as in the other states' statutes, is to eliminate the possibility of a *Lolkus*<sup>331</sup> interpretation—not only must the violator have intended the act, he must also have known that it was in violation.

The fourth subsection is based on a Pennsylvania idea,<sup>332</sup> but expands it to apply to open market transactions as well as to those where the parties clearly dealt with each other. While the expansion could lead to substantial liability if many purchased at about the same time, the statement that defendant shall be deemed to be unjustly enriched was added, and is designed, to establish the theory of recovery and also a ceiling—it should limit recovery to all possible plaintiffs (not to each) to the maximum that defendant could unjustly have been enriched.

The predecessor law provided no civil remedy for insider trading, as such, or for dissemination of misleading information by persons who were unconnect-

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326. FUSA § 502(4).

327. 15 U.S.C. § 77l(2) (Supp. IV, 1974).

328. USA § 410(a)(2).

329. PA. STAT. ANN. tit. 70, §§ 501(a)(ii), (b) (1975); WIS. STAT. ANN. §§ 551.59(1) (b), (2) (1975).

330. PA. STAT. ANN. tit. 70, § 501(c) (1975); WIS. STAT. ANN. § 551.59(3) (1975).

331. *Lolkus v. Vander Wilt*, 258 Iowa 1074, 141 N.W.2d 600 (1966); see 5 E. HAYES, IOWA PRACTICE—CORPORATION LAW AND PRACTICE § 318 (1969).

332. PA. STAT. ANN. tit. 70, § 501(e) (1975).

ed with the transaction affected by it. As noted in the preceding section, it did make a contract for sale or purchase voidable if "made in violation of" the law. The approach of the IUSA is to provide for people who consider in engaging in securities transactions a clearer and more precise description of the possible liabilities they can face.

### C. *Joint and Several Liability; Indemnity and Contribution*

The liabilities of persons violating registration requirements and antifraud provisions, just described, extend to others who materially aid them in committing the violating acts. Those to whom this liability is extended include affiliates of violator, partners or principal executive officers or directors of violator, persons occupying an equivalent status, employees, and broker-dealers or agents. The liability exists and is joint and several with, and to the same extent as, violator's liability, unless the aider can establish 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.<sup>333</sup>

This language is the substance of the first sentence of the USA provision dealing with persons other than violators who are civilly liable;<sup>334</sup> the second subsection deals with the matter in the second sentence of that provision. Pennsylvania also divided the USA provision into subsections.<sup>335</sup> The differences involve substitution of "affiliates" for USA language describing a concept equivalent to that term, "act or transaction constituting the violation" for "sale," "any person liable" for "nonseller who is so liable," and "proves" for "sustains the burden of proof." None of these changes should affect the interpretation of the subsection (recognizing that it reaches acts other than those involved in effecting a sale).

A person who is liable under the IUSA has the right to be indemnified by any affiliate whose willful violation of any provision of the Act gave rise to the liability. He has the right of contribution against all other persons similarly liable except that if his violation was willful he has no right to contribution from another person whose violation was merely negligent.<sup>336</sup>

The second sentence of the USA provision, referred to above, provides only for "contribution . . . among the several person liable."<sup>337</sup> The Pennsylvania revision incorporates the idea of indemnification (but limits it to "any corporation" rather than "any persons"), and adds the limitation on right of the willful violator to contribution.<sup>338</sup>

These subsections deal with problems that appear not to be covered in the predecessor law.

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333. IUSA § 503(1).

334. USA § 410(b).

335. PA. STAT. ANN. tit. 70, §§ 503(a), (b) (1975).

336. IUSA § 503(2).

337. USA § 410(b).

338. PA. STAT. ANN. tit. 70, § 503(b) (1975).

#### D. *Time Limitations on Rights of Action*

The predecessor law provided that no action to recover the purchase price, where the sale violated the law, could be brought after two years from the date of the sale; and also denied the right to recover where the seller offered in writing to take back the security and to refund the purchase price plus interest<sup>339</sup> less any interest or dividend paid prior to refund, if the holder had refused or failed to accept that offer within thirty days after it was made.<sup>340</sup> The USA follows a similar pattern.<sup>341</sup> Pennsylvania and Wisconsin changed the basic limitation period to three years from the violation or one year after plaintiff discovered the facts constituting the violation, and subdivided their sections to reflect their increase in possible types of violations.<sup>342</sup> The Iowa approach is similar to that of the two states, in form, although it uses a basic two year period for most purchases, a five year period in one situation, and also establishes a one year limit on actions to obtain indemnity or contribution.

Accordingly, actions based on violation of registration requirements, whether brought against the person with whom plaintiff contracted or against an affiliate or other aider of that person, must be brought within two years after the violation on which it is based.<sup>343</sup> Actions based on violation of the fraudulent practices provision must be brought within the shorter of five years after the act (or transaction) constituting the violation or two years after plaintiff has actual notice of the facts constituting the violation or upon exercise of reasonable diligence should have known of them.<sup>344</sup> The one year period to enforce rights of indemnification or contribution begins when the judgment, upon which the liability for which that right exists, becomes final.<sup>345</sup>

No action may be commenced, for a violation of registration requirements or of prohibitions against fraudulent practices, if the "injured" party receives an offer, which he fails to accept within the period it specifies, which: (1) in reasonable detail states why liability may exist and what the party's rights are; (2) offers to rescind the transaction, or offers "damages" if the security cannot be returned (plus interest on appropriate cash adjustments); and (3) states that the offer may be accepted within a specified time (not less than thirty days, unless the administrator by rule authorizes the use of a shorter period).<sup>346</sup> The administrator is to adopt a rule prescribing the form of the offer and the information it is to contain. The offer is to be delivered to offeree personally or to be sent by certified mail addressed to offeree at his last known

339. Interest was at the rate called for in the security, if it was interest-bearing, or 6 percent if it was not.

340. IOWA CODE § 502.23 (1975).

341. USA § 410(e).

342. PA. STAT. ANN. tit. 70, § 504 (1975); WIS. STAT. ANN. §§ 551.59(5), (6) (1975).

343. IUSA § 504(1).

344. *Id.* § 504(2).

345. *Id.* § 504(3).

346. IUSA §§ 504(4), (5).

address. Unlike the predecessor law and the USA, but like the Pennsylvania-Wisconsin approach, the IUSA states that if the offeror fails to perform as proposed in his offer, after offeree accepts, offeree is then able to maintain an action for the violation.<sup>347</sup>

#### E. *Implied Liability; Liability on Other Basis*

No civil liability can arise, in favor of any person, *by implication* from or as the result of violation of any provision of the IUSA or any rule or order entered under it. However, the Act in no way limits any liability that might exist because of other statutes or under common law, if the IUSA were not in force.<sup>348</sup> The predecessor law had no similar provision. This is the substance of the comparable USA provision,<sup>349</sup> as it was restated by Pennsylvania<sup>350</sup> except that "any person" was substituted for "any private party." The effect is to make civil liabilities as specific as possible, rather than to permit the uncertainties that the possibility of implied liabilities causes.<sup>351</sup>

#### F. *Waiver of Right of Action*

Any condition, stipulation or provision binding any person to waive compliance with any provision of the IUSA or rule or order thereunder is void.<sup>352</sup> This has no counterpart in predecessor law, but is part of the USA in recognition of the usual disparity of bargaining power and sophistication between parties to transactions in securities.<sup>353</sup> However, the USA limits its provision to "any person acquiring any security," rather than "any person;" the Iowa expansion recognizes that under the IUSA civil relief is available to vendors as well as to purchasers.

#### G. *Unenforceability of Illegal Contracts*

A defense which may be asserted successfully (if proved), in an action based on a contract for the purchase or sale of a security, is that plaintiff (or its assignor) entered into the transaction giving rise to the contract under circumstances which would subject him (or his assignor) to civil liability under the IUSA.<sup>354</sup> This is in substance, but considerably restated, the comparable USA provision; however, the latter applies to actions where plaintiff is an assignee of the contracting party only if plaintiff knew of the facts by which assignor's acts violated the Act.<sup>355</sup> There is no comparable provision in predecessor law, but

347. *Id.* § 504(6); see PA. STAT. ANN. tit. 70, § 504(f) (1975); WIS. STAT. ANN. § 551.59(6)(c) (1975).

348. IUSA § 505.

349. USA § 410(h).

350. PA. STAT. ANN. tit. 70, § 506 (1975).

351. See L. LOSS & E. COWETT, BLUE SKY LAW 395 (1959).

352. IUSA § 506.

353. USA § 410(g); see L. LOSS & E. COWETT, BLUE SKY LAW 395 (1959).

354. IUSA § 507.

355. USA § 410(f).

the Official Comment says that courts generally reached the conclusion that a defense was available despite no express statutory direction to that effect.<sup>356</sup>

## VI. CRIMINAL LIABILITY

The predecessor law had three sections dealing with criminal liability. Two dealt with false statements and representations and the third with other violations.

The first made it a felony to subscribe to or cause to be made a false statement or entry in "any book required to be kept in relating to any business to be transacted in [Iowa] pursuant to the provisions of" the law, or the making of false or fraudulent statements on specified matters to personnel of the Securities Department.<sup>357</sup> Knowledge of the falsity was not essential, but whether the section applied to corporations whose securities were exempt from registration was unclear.<sup>358</sup>

The second made it a felony knowingly to make false representations as to the nature, character or value of a security or its earning power, or other false or fraudulent representations, to induce the recipient thereof to purchase the security, or to conceal any material fact in advertisement or prospectus to defraud the purchaser, and, until 1974, to knowingly violate any provision of the law with intent to defraud.<sup>359</sup> This section clearly applied to transactions in exempt securities.<sup>360</sup>

The third made it a criminal act to sell, offer for sale, or negotiate for the sale of a security, either without complying with the law or after registration had been revoked or cancelled; or otherwise to neglect or refuse to comply with the law. At one time the law required the violation to be knowingly made and with intent to evade the law. Later, the words "knowingly made and" were dropped, and violations were misdemeanors except that if intent to evade the law was found they were felonies. In 1974, the section was further revised to substitute intent to defraud for intent to evade the law.<sup>361</sup>

The IUSA, following the pattern of the USA provision for criminal liability, has only one section, which states that any person who willfully and knowingly violates any provision of this Act, or any rule or order under it, shall upon conviction be fined not more than \$5,000 or imprisoned not more than three years, or both.<sup>362</sup> The USA provision required only a willful violation except in cases of misleading filings; it also added that no person could be imprisoned for violating a rule or order if he proved he had no knowledge of

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356. L. LOSS & E. COWETT, *BLUE SKY LAW* 394 (1959).

357. IOWA CODE § 502.26 (1975).

358. 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 317 (1969).

359. IOWA CODE § 502.28 (1975).

360. See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 317 (1969).

361. IOWA CODE § 502.27 (1975); 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 318 (1969).

362. IUSA § 605(1).

it.<sup>363</sup> The USA also included as an optional provision of a five-year statute of limitations, which the Project did not elect to include.

The IUSA also provides that the administrator may refer such evidence as is available about violations to the attorney general or to the appropriate county attorney, and those attorneys may institute appropriate criminal proceedings whether or not such reference has been made.<sup>364</sup> The Act in no way limits the power of the state to punish any person for conduct which constitutes a crime under any other statute.<sup>365</sup> These ideas are taken directly from the USA.<sup>366</sup>

The IUSA approach should simplify and clarify application of the criminal penalties for violations of the securities laws of the state.

## VII. OTHER SECTIONS

### A. *Filing of Sales Literature*

The administrator by rule or order may require the filing of any prospectus, pamphlet, circular, form letter, advertisement, or other sales literature or advertising communication addressed or intended for distribution to prospective investors, except where the security or the transaction is exempt from registration. He may also prohibit publication, circulation or use of any advertising deemed false or misleading—with no exception or exemption applicable.<sup>367</sup>

The first of these matters is based on the similar approach of the USA, which, however, does not refer to "advertising communication."<sup>368</sup> The second is borrowed from Wisconsin.<sup>369</sup>

Operating under the predecessor law's provision that the Commissioner could require unspecified information, he did require that copies of the various items of sales literature be filed with him.<sup>370</sup>

### B. *Judicial Review of Orders*

The predecessor law provided for appeal by any interested person from any final order of the Commissioner, to the district court of Polk County, specifying the time to appeal, the form of notice, and requiring a bond in the penal sum of \$1,000. It then spelled out the procedures to be followed by the courts reviewing the action, and the effect of the appeal on the order while the review process went on.<sup>371</sup>

The IUSA provision relating to review was drafted to conform to the

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363. USA § 409(a).

364. IUSA § 605(2).

365. *Id.* § 605(3).

366. USA §§ 409(2), (3).

367. IUSA § 602.

368. USA § 403.

369. WIS. STAT. ANN. § 551.53 (1975).

370. 5 E. HAYES, IOWA PRACTICE—CORPORATION LAW AND PRACTICE § 303 n.37 (1969).

371. IOWA CODE § 502.24 (1975).

requirements of the Iowa Administrative Procedures Act. It merely states that review of the administrator's actions may be sought pursuant to that Act, upon execution of an appropriate bond in "the penal sum of \$1,000."<sup>372</sup>

### C. *Scope of the Act*

The predecessor law did not make clear what activities would subject a transaction to registration and other requirements of the law. It could be assumed to cover bargaining between two parties in Iowa, and possibly to soliciting activities in Iowa even though the contract to sell and delivery occurred outside Iowa. But what if the alleged violator never entered Iowa, either in person or by agent? There were a variety of situations where there was no direct contact with the state, for which different answers might be given.<sup>373</sup>

To clarify this aspect of the law, the Act follows substantially the approach taken in the USA.<sup>374</sup> This means that the provisions of the Act relating to sales or offers to sell apply when the sale or offer is made in Iowa or when the offer to purchase is made and accepted in Iowa. The provisions concerning purchases and offers to purchase apply when the purchase or offer is made in Iowa or the offer to sell is made and accepted in Iowa.<sup>375</sup>

An offer is considered to be made in Iowa, even though neither party is present there, if it originates in Iowa or is directed by the offeror to<sup>376</sup> and is received by the offeree in Iowa—except that for registration requirement purposes an offer to sell, if it is not directed to or received by the offeree in Iowa, is not deemed made in Iowa.<sup>377</sup> The USA did not include the exception, and instead of calling for receipt by offeree in Iowa provided for receipt at the place to which it was directed (or at an Iowa post office if a mailed offer).<sup>378</sup>

Acceptance occurs in Iowa if acceptance is communicated to offeror in Iowa and has not previously been communicated to him outside Iowa; if offeree sends it to offeror in Iowa, reasonably believing him to be there, even if he is not, if he does receive it in Iowa.<sup>379</sup> The USA would treat it as sufficient for the acceptance to be directed to offeror at the place he is believed to be and it is received at that place.<sup>380</sup>

An offer to sell or to purchase is not made in Iowa if made by means of a newspaper or other publication of general, regular and paid circulation which is

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372. IUSA § 606.

373. See 5 E. HAYES, *IOWA PRACTICE—CORPORATION LAW AND PRACTICE* § 310 (1969).

374. USA §§ 414(a)-(e).

375. IUSA § 610(1).

376. The Project's word here was "in," which appears to be in error, and which was corrected before initial approval by the House Committee on Commerce.

377. IUSA § 610(2).

378. USA § 414(c).

379. IUSA § 610(3).

380. USA § 414(d).

not published in Iowa or by means of a radio and television program originating outside Iowa, even though received by the offeree in Iowa.<sup>381</sup> The USA is similar, but also excepts newspapers published in the state if more than two-thirds of their circulation for the previous twelve months is outside the state.<sup>382</sup>

#### D. *Statutory Policy*

Despite the variations from the USA which have been noted, the Act is to be so construed as to make uniform the laws of those states which enact the USA and to coordinate the interpretation and administration of the IUSA with the related federal regulation.<sup>383</sup>

#### E. *Other Provisions*

The Act includes a standard severability provision, intended to allow other portions of the Act to be given effect if any provision is held invalid, or if its application to any purpose or circumstance is so treated.<sup>384</sup>

The Act became effective January 1, 1976.<sup>385</sup> Predecessor law will govern matters pending on that date or which are based on facts or circumstances occurring before that date, subject to the statute of limitations applicable when the cause of action accrued.<sup>386</sup> Effective registrations, and orders and conditions applicable to them, remain in effect for as long as they would have if the predecessor law continued in force; they are treated as filed, entered or imposed under the IUSA but are governed by predecessor law.<sup>387</sup> If an offering was begun in good faith before its effective date, on the basis of an examination available under predecessor law, that law applies to any offer or sale made before July 1, 1976.<sup>388</sup> Judicial review of administrative orders entered before 1976, if not instituted by the effective date, are subject to the IUSA review procedure. However, the period in which review may be sought is the shorter of sixty days after the IUSA's effective date or the period in which the ISL permitted review to be sought.<sup>389</sup>

The predecessor law, found in chapter 502 of the Code, was repealed, and the provisions of the IUSA from section 101 through section 614 are to be part of that chapter.<sup>390</sup> Other sections of the Code which referred to the provisions of the predecessor law are amended to refer to the appropriate portion of the IUSA.<sup>391</sup>

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381. IUSA § 610(4).

382. USA § 414(e).

383. IUSA § 611; *see* USA § 415.

384. IUSA § 612; USA § 417.

385. IUSA § 614.

386. *Id.* § 613(1).

387. *Id.* § 613(2).

388. *Id.* § 613(3).

389. *Id.* § 613(4).

390. IUSA §§ 615, 621.

391. *Id.* §§ 616-20.