

STATE OF UTAH
Office of the Attorney General
Salt Lake City

A. Pratt Kesler
Attorney General

February 9, 1962

William G. Hardy, Director
Securities Commission
B u i l d i n g

Dear Mr. Hardy:

Reference is made to your request anent an interpretation of Section 61-1-5 (7), Utah Code Annotated 1953, as amended, and the application of that statute to: (1) the sixty-day demand note of Pioneer Finance and Thrift Company, Inc.; and (2) the twelve-month promissory note of Crosbie Valley Inv. Ltd.

The 1961 Legislature amended Section 61-1-5 to read in part as follows:

"Except as otherwise expressly provided, the provisions of this chapter shall not apply to any of the following classes of securities:

* * *

"(7) Any commercial paper which arises out of a current transaction or the proceeds of which have been or are to be used for current transactions, and which evidences an obligation to pay cash within nine months of the date of issuance, exclusive of days of grace, or any renewal of such paper which is likewise limited, or any guarantee of such paper or of any such renewal." (Chapter 149, Laws of Utah 1961.)

The aforementioned exception is verbatim an exemption in the Uniform Securities Act. See Section 402 (a) (b) (10), Uniform Securities Act, Uniform Laws Annotated, p. 84 and 126, with the Commissioner's Note at 132.

Apparently, the exemption in question has never been construed in Utah or in the states which have adopted the Uniform Act. We believe that the exemption is similar to Section 3 (a) (3) of the Securities Act of 1933, 15 U.S.C.A., 77c (a) (3); however, the federal exemption is also without judicial interpretation.

Legal commentaries have considered the federal and state statutes aforementioned. See for example, Loss, "Securities Regulation" (1951 Edition with 1955 Supplement), p. 356; Loss and Corvett, "Blue Sky Law," p. 360-1.

In 1 Loss, "Securities Regulation," pp. 556-568; the author refers to the federal exemption in Section 3 (a) (3) of the Securities Act of 1933 and states:

"The House report referred to this section as an exemption for 'short-term paper of the type available for discount at a Federal Reserve bank and of a type which rarely is bought by private investors.'

"Both conditions of the exemption, of course, must be satisfied. The reference to current transactions, for example, would presumably rule out an issue of short-term notes for the purpose of refunding long-term notes or bonds. But the Commission's General Counsel has expressed the opinion that, when a finance company buys purchase-money notes given by members of the public in connection with installment purchases, deposits those notes with a trustee, and issues its own short-term collateral-trust notes against them, the latter notes may be regarded as used for current transactions.

"In 1957 the Commission's Regional Administrator in New York, in announcing the institution of injunctive proceedings against a corporation which had made a public offering of \$325,000 of nine-month notes in units of \$100, \$500, and \$1000 to finance the promotion of various real estate syndications, stated that Sec. 3(a) (3) 'was never intended by Congress to permit the widespread sale of securities to the investing public in order to provide capital for a business venture without compliance with the full and fair disclosure requirements of the Securities Act of 1933.' The case

became moot when the defendant registered and the ex parte restraining order which had been obtained was vacated by consent. But Regional Administrator presumably did not mean to rule out all public offerings under Sec. 3 (a) (3) without regard to the use of the proceeds. Notwithstanding the House report's reference to paper of a type "which rarely is bought by private investors," restricting this exemption to paper which is privately offered would make it redundant in view of the exemption in Sec. 4 (1) for private offerings generally. Some of the large finance companies do offer nine-month paper to the public from time to time in reliance on Sec. 3 (a) (3).

"So far as the maturity is concerned, presumably the renewal clause does not permit an advance provision making the notes payable by new notes of similar tenor. The question of demand notes is more difficult. There is no indication that they were brought to the attention of the legislative committees. Their treatment in the Negotiable Instruments Law seems more consistent with including them in the exemption than excluding them. The Federal Reserve Act and regulations seem to lean the other way. It is understood to be the administrative position that demand notes do not meet the maturity test of Sec. 3 (a) (3)."

It is apparent that the meaning of Section 61-1-5 (7), Utah Code Annotated 1953, as amended, is occult. The use of the phrase "current transaction /S/" leaves much to be desired, and restrictive application of the exemption seems doubtful, especially in any criminal action under the state blue sky law, where Section 61-1-5 (7), as amended, is claimed as a defense.

We answer your specific questions as follows:

(1) A demand note does not evidence "an obligation to pay cash within nine months of the date of issuance." Maturation of the demand instrument is dependent upon the payee exercising his option to demand payment, which may or may not be within the statutory period in question. We do not consider the contingency that commercial paper may mature within nine months of issuance sufficient to meet the requirements of Section 61-1-5 (7), as amended.

Therefore, the sixty day demand certificates of Pioneer Finance and Thrift Company are not exempt from registration, and opinions of this office to the contrary under former law are modified accordingly.

(2) The one-year maturity notes of Crosbie Valley Inv. Ltd. are in excess of the nine-month period provided in 61-1-5(7), as amended, and, therefore, are not exempt from registration.

We are of the opinion that anyone claiming the benefit of the exemption under 61-1-5(7), as amended, has the burden of justifying the exemption. While the language of 61-1-5(7), as amended, leaves much to be desired in the way of certainty, we are of the conviction that the commercial paper entitled to exemption must (a) arise out of the common, ordinary, and regular business transactions, or (b) the proceeds of which have been or are to be used for incidental, ordinary, or regular business transactions. The exemption would not extend to public offerings to provide equity capital, or to provide debt capital where the source or disposition of the funds arises out of transactions which are not in the ordinary, common, or regular course of business.

Yours very truly,

A PRATT KESLER
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RAYMOND W. GEE
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