

2565.

SYNDICATE—DEFINITION OF SYNDICATE UNDER SECTION 8624-2,
GENERAL CODE—DISCUSSION OF SYNDICATE CERTIFICATES
AND SALE OF SECURITIES REQUIRING REGISTRATION.

SYLLABUS:

1. *When two or more persons pool together a portion of their funds under an agreement that the net profits expected to be derived from the use of such pooled funds shall be distributed pro rata among the contributors, and that the pooled fund shall be similarly owned by the contributors, such association is a syndicate, and the certificates representing the interests of the contributors are syndicate certificates within the meaning of Section 8624-2, General Code.*

2. *When an investor deposits his funds with an agent or with a third party, and enters into an agreement with such agent that he is to use such funds in the business of speculation on stock exchanges or boards of trade, which agreement, further provides that in addition to a stipulated commission the agent is to receive a percentage of the profits, the writing evidencing such deposit of money and sharing of profits is a certificate in, or under a profit sharing or participation agreement within the meaning of Section 8624-2, General Code.*

3. *Where a syndicate agent or manager solicits members for a syndicate or pool, for the purpose of engaging in speculations on the stock exchange or board of trade, with a view to dividing the prospective profits proportionately among such syndicate members and issues certificates or indentures poll, as evidence of the rights and interest of the syndicate members such transaction is a sale of securities within the meaning of Section 8624-2 of the General Code.*

COLUMBUS, OHIO, April 25, 1934.

HON. THEO. H. TANGEMAN, *Director of Commerce, Columbus, Ohio.*

DEAR SIR:—I am in receipt of your request for my opinion, which reads:

“EXHIBIT No. 1, attached hereto, contains a copy of a contract into which the I. A. Corporation intends to enter with various individuals.

EXHIBIT No. 2, is a similar contract into which D. & Company likewise proposes to enter with individuals in Ohio.

EXHIBIT No. 3, is a similar contract likewise proposed to be used by one D. E. L.

EXHIBIT No. 4, is a similar contract likewise proposed to be used by the C. T. Company.

EXHIBIT No. 5, is a similar contract proposed to be used by one W. V.

EXHIBIT No. 6, is a similar contract proposed to be used by one G. C. B.

EXHIBIT No. 7, is a transcript of testimony before the Division of Securities concerning a similar proposition of H. T. K. & Co.

In view of the provisions of Section 8624-2, subsection 2, of the General Code of Ohio, in defining the term security, your opinion is respect-

fully requested as to whether the various instruments attached hereto are in themselves securities within the definition of this section.

If you determine this question in the affirmative, your opinion is further respectfully requested as to whether the solicitation of persons in Ohio to enter into such contracts constitutes a 'sale' within the meaning of that term as defined by Section 8624-2, subsection 3, of the General Code of Ohio."

Exhibit 1, attached to your request is a prospectus and proposed contract form, which contract might be summarized as setting forth the following plan of operation:

The I. A. Corporation proposes being employed as "Agent, to manage" for the account of the contracting party, such moneys as may be entrusted to it. Such moneys are to be used by the "agent" for trading in "bonds, stocks and other securities or commodities traded in upon the New York Stock and Curb Exchanges and Chicago Board of Trade". It is further contemplated to give such agent full power to hypothecate such securities for the purpose of borrowing money. Such agent further has the right to commingle the funds of one contractee with those of other like contractees and therefrom to make joint purchases of securities. The "agent" is further given power to manage the entire investments and on behalf of the contractee to execute any and all papers necessary for the management of the speculation. The agreement purports to limit the liability in the venture to the amount of his assets in the hands of the "agent". The compensation of the agent is computed as follows:

When the money is deposited by the contractee with the "agent", 10% thereof is credited to the "agent", as a retainer fee. All income from the speculations is to be credited to the account of the contractee until such account is equal to the amount paid thereto by the contractee; after such time all profits are to be divided between the contractee and the agent, on the basis of 75% and 25% respectively.

The contractee has the right to terminate the agreement on reasonable notice, and upon termination, receives a pro rata share of the pool.

Exhibit 2, attached to your request, sets forth two proposed contracts, the first of which is in all material respects similar to Exhibit 1. The second is substantially equivalent.

Exhibit 3 purports to be a power of attorney, giving the agent the right of control over certain securities or moneys to be deposited by the contractee with a depository. The contract does not set forth with any degree of definiteness, the powers of the "agent" with reference to the securities or moneys. There are limitations on the right of withdrawal of securities by the contractee but no specific definition of the duties of the "agent". The contract states that it is entered into "for the purpose of facilitating the trading of any and all kinds of securities in the stock market (dealing through various brokerage offices), such trading operations to be governed entirely by the terms hereinafter set forth". The terms and conditions of reinvestment are not set forth in the agreement. There is, however, a statement that all gross profits realized are to be divided 15% to the agent and 85% to the contractee.

Exhibit 4 purports to be a letter of transmittal of certain funds to be deposited in a "trading pool", and further to authorize the "agent" to use such funds in such trading as may suit its discretion and for its compensation to retain one-half

of all net profits. It further contains a general power of attorney as to such moneys and investments representing the same.

Exhibit 5 purports to be a general power of attorney authorizing the "agent" to use as he may deem proper moneys delivered to him by the contractee in the operation of one or more stock exchange accounts on margin or otherwise, or to deal in securities therewith. From such agreement the plan of operation is to commingle the funds of numerous parties into a common pool, each party having an interest in the common mass, the agent for his compensation receiving 3% of the original deposit plus one-fourth of the appreciation of the mass.

Exhibit 6 purports to be a receipt for certain "cash, securities, etc.," for deposit in a "trading account" to be used for dealing in "listed stocks". All losses from transactions in which such accounts are invested are to be borne by the "depositor". In the event there is a profit, 25% thereof is to be retained by G. C. B.

Exhibit 7 purports to be a transcript of testimony concerning the method of operation of the H. T. K. & Co. and S. & Co. From such testimony it would appear that the H. T. K. & Co. organizes a pool of \$100,000.00 having units of \$500.00, and invests such pool in listed securities under the management of H. T. K. & Co. For its services in the management and control it receives 1½% of the original deposit and 25% of all profits realized. The interest of the members is represented by a "receipt".

You first inquire whether the paper evidencing such moneys so left with the "agent" for investment, speculation or management is "securities" within the meaning of Section 8624-2, General Code. That part of Section 8624-2, General Code, applicable to your first inquiry, reads:

"The term 'security' shall mean any certificate or instrument which represents title to or interest in, or is secured by any lien or charge upon, the capital, assets, profits, property or credit of any person (as that term is defined by subsection (4) of this section (2) * * and shall include * * warrants and options to purchase securities, subscription rights, * * all forms of commercial paper and evidences of indebtedness, * * syndicate certificates * * certificates in or under profit sharing or participation agreements, * * or * * certificates evidencing an interest in any trust or pretended trust * *."

It would appear from Exhibits 1 to 7, both inclusive, that it was within the contemplation of the parties that the deposit, of the moneys or securities recited therein, was either at the time of the delivery of the instruments represented by such exhibits or that the delivery of such moneys was to be evidenced by a receipt or other writing. In fact, such is the testimony set forth in exhibit 7. I do not believe that it will be contended that such receipt would be "a certificate or instrument." The question is more particularly, whether such certificate or instrument is of the type which subparagraph (2) of Section 8624-2, General Code, defines as a "security." Strictly speaking, a receipt is not evidence of title to property delivered, but is rather evidence of the delivery of the property mentioned therein. Such receipt would be evidence that some money or property was delivered to the "agent"; the title to which would be evidenced by the instruments which you have referred to as Exhibits 1, 2, 3, 4, 5, and 6 and that described in Exhibit 7. Such instruments on their face, purport not only to represent that the con-

tractee is the owner of the moneys or property deposited or rather that proportion reserved to him but also of a portion of the earnings hoped to be derived from the investment of the same.

It might be urged that the rights of the agent, as set forth in such instruments are so broad as to vest the title of the funds or securities deposited in the "agent." If such contention be conceded, it would then appear that such instrument or the performance thereof, was secured by a "lien or charge upon, the capital, assets, profits, property or credit of" the "agent." Such "agent" is clearly a "person" as that term is defined in subsection (4) of Section 8624-2, General Code, which reads:

"'Person,' shall mean and include a natural person, firm, co-partnership, limited partnership, partnership association, syndicate, joint stock company, unincorporated organization or association, trust, trustee of a trust (excepting a trust created or a trustee designated by law or by a will or by judicial authority), and a corporation organized under the laws of any state or of any foreign government, or political subdivision thereof."

I am not unmindful of that rule of statutory construction to the effect that where general words are followed by an enumeration of particular words that, under certain circumstances, such particular words are to be construed as limiting the general words, and only those particular classes enumerated are to be included within the meaning of the statute. Without deciding whether such rule is or is not applicable in the case under consideration, let us examine some of the particular types of securities mentioned after the general classification above referred to.

"Syndicate certificates" are written instruments evidencing the proportionate ownership of the syndicate members in the undivided syndicate assets. A "syndicate," as that term is commonly used, is a group of persons who pool together their assets, or a portion thereof, to be used in a common enterprise for a single transaction or several transactions usually under a common agreement that their liability in such venture is limited to the capital so invested but not for an unlimited period as in a partnership. See 25 R. C. L., 46; *Hambleton vs. Rhind*, 84 Md. 456; *Jackson vs. Clemson*, (Pa.) 156 Atl. 540, 542.

In each of the exhibits submitted it is at least intimated, where not expressly so stated, that the moneys deposited are to be pooled together for a common enterprise, and that the liability of the contractee is not to be greater than the sum deposited.

For the purposes of this opinion it is unnecessary to decide that the exhibits submitted and the complementary receipts when necessary to further the purpose of the parties, are or are not in fact syndicate certificates. In the same definition the legislature has stated that "certificates in or under profit sharing or participation agreements" are also securities within the meaning of the Ohio Securities Act. As stated by McCormick, District Judge, in *Duke vs. Welsh*, 49 Fed. 2d, 339, 341:

"Profit sharing ordinarily signifies the participation of employees with their employer in a given share of the profits of an enterprise by reason of their labor and not by reason of their capital investment

therein. Moreover, the term 'profit sharing' does not imply the idea that the employe is to share any part of the losses. * * The general understanding of a profit-sharing arrangement between the employers and workers is that the worker shall share in earnings and profits of his employer, but is not accountable or liable for losses or deficits in the business, and there is also generally present in profit-sharing transactions the element of contribution by the employer to the project."

Viewing each of the exhibits as a single and isolated transaction, it would appear that all the elements of a profit sharing certificate are present. The certificates or written indentures purport to be an employment agreement. The following elements of a profit-sharing agreement are present:

- (1) An agreement between an employer and an employee to share a portion of the profits of the transaction with the employee.
- (2) The employee contributes only his services but no capital to the venture.
- (3) The employee is not liable for any portion of the losses of the venture, if any.
- (4) The employer makes a contribution of the capital and of earnings when, as and if accrued.

It would thus appear that as between the employer and the "agent" the transaction is a profit-sharing venture and certificates or instruments representing the interests of the parties are profit-sharing certificates and that as between the different members of the pool or group the transaction is a syndicate.

If I am in error as to my conclusions as to the nature of such exhibits as being syndicate certificates or profit-sharing certificates, it would nevertheless appear that such certificates are at least "certificates evidencing an interest in any trust or pretended trust." From the tenor of such exhibits it would appear that at least the equitable ownership of the moneys deposited is not intended to pass to the "agent." The moneys delivered to him for investment are evidently intended to be and remain the property of the contractee except as to that portion which is set aside to the agent as his fee or commission. The agent has the right to use such funds only in the manner authorized by the agreement. Such funds in the hands of the agent or depository are trust funds; they are funds deposited for a particular purpose, and it has been repeatedly held that such funds are trust funds. *McDonald vs. Fulton*, 125 O. S. 507; *Stepfield vs. Fulton*, 126 O. S., 351; *Blakley, Rec'r., vs. Brinson*, 286 U. S. 254; *Northwestern Lumber Co. vs. Bank*, 130 Washington, 33.

It therefore appears that the certificates or other writings evidencing ownership of a portion of such commingled property would at least be "certificates evidencing an interest in any trust or pretended trust" and therefore "certificates" within the meaning of Section 8624-2, sub-paragraph 2. For such reasons, I am of the opinion that the writings evidencing such transactions as described in the exhibits submitted to me are "securities" within the meaning of the Ohio Securities Act.

Since my answer to your first inquiry is in the affirmative, a consideration of your second inquiry becomes necessary.

Your second inquiry is, "whether the solicitation of persons in Ohio to

enter into such contracts constitutes a 'sale' within the meaning of that term as defined by Section 8624-2, sub-section 3, of the General Code of Ohio." Sub-paragraph 3 of Section 8624-2, General Code, in so far as is material to your inquiry, reads:

"'Sale' shall have the full meaning of the term 'sale' as applied by or accepted in courts of law or equity, and shall include every disposition, assignment, subscription, offer to sell, option to sell, solicitation or agreement to sell or exchange any security or an interest therein, directly or indirectly by agent, circular, pamphlet, advertisement or otherwise."

The ordinary meaning of the term "sale," as such term is used in commercial usage, is that a sale is a transaction by which, for a monetary consideration, a person transfers to another property or an interest therein. *Clark vs. Gault*, 77 O. S. 497; *State vs. Bank*, 16 O. S. 236; *Brock vs. Jewell*, 52 O. S. 187; Section 8381, General Code.

If a literal interpretation of the exhibits submitted is given to the language of such exhibits the question would arise as to what property was the subject matter of the sale and to whom the transfer of the title passed. Such instruments purport on their face to retain the title to the money or securities deposited by the contractee in the contractee except as to that portion which is set aside to the "agent" as his commission or retainer fee.

However, in determining the nature of such securities and the nature of the transaction, it is highly probable that the court would look beyond the form, and to the intention of the parties as evidenced by such instrument, in determining the exact nature of the transaction. In the case of *State vs. Robinson*, 185 Minn. 202, the court had before it the question as to whether the solicitation of "purchasers" of muskrats was the sale of securities within the meaning of the Securities Act of Minnesota. From the facts as recited in the reported opinion it would indicate that the parties to such transaction entered into two contracts, the first of which purported to be for the sale of muskrats. The second purported to be an agreement between the purchaser and the seller, to the effect that the muskrats were to be left at the seller's muskrat farm and that the purchaser was to receive his proportionate share of the profits arising from the increase by multiplication thereof, whether such muskrats were sold alive or their pelts were dressed, tanned and sold. Under such agreement, the seller was to receive one-half of the purchaser's proportionate share of the profits arising from such agreement as compensation for supervising, managing and operating the farm. The court held that such plan of operation was a profit-sharing scheme or venture and that the solicitation and entering into such agreements amounted to a sale of an interest in a profit-sharing scheme or venture and was, therefore, a sale of securities within the meaning of the Minnesota Securities Act.

In the case of *People vs. Oliver*, 102 Cal. App., 29, the court held that the making and execution of a contract entered into between a promoter of a syndicate being organized and a person who thereby became a member of such syndicate when organized, was a "sale" within the meaning of the California Securities Act.

In *Kerst vs. Nelson*, 171 Minn. 191, the court had before it the question of whether or not contracts for the sale of portions of a tract of land to be

used as a vineyard, with an agreement on the part of the seller to cultivate, harvest and market the crops and divide the net profits with the buyer, are a contract for investments in a profit sharing scheme, and therefore, securities within the meaning of the Minnesota Securities Act.

The court held that the solicitation and execution of such contracts was a sale of securities, within the meaning of the Minnesota Securities Act.

In the case of *Groby vs. State*, 109 O. S. 543, the Supreme Court of Ohio had before it the question as to whether or not the solicitation or sale of shares in a syndicate constituted a "sale" within the meaning of the former securities Act of Ohio, and held, as stated in the third paragraph of the syllabus:

"Solicitation of subscriptions for shares or interest in a 'syndicate,' or an association, for which a so-called 'membership receipt' is issued to the subscriber stating that he is entitled to a 'pro rata interest in all earnings and profits of the said syndicate,' is a 'sale of securities' of such association, and falls within the regulatory provisions of the statute, whether or not such transaction is preliminary to the organization and incorporation of a company and the issuance of the stock thereof."

It would therefore appear that the method of conducting the transactions in question constitutes a sale of securities within the meaning of Section 8624-2, of the General Code.

Respectfully,
JOHN W. BRICKER,
Attorney General.

2566.

APPROVAL, TWO RESERVOIR LAND LEASES EXECUTED TO W. A. COCHRAN OF CELINA, OHIO—MERCER COUNTY, OHIO.

COLUMBUS, OHIO, April 25, 1934.

HON. EARL H. HANEFELD, *Director, Department of Agriculture, Columbus, Ohio.*

DEAR SIR:—The Chief of the Bureau of Inland Lakes and Parks of the Division of Conservation in your department has submitted, for my examination and approval, two certain reservoir land leases in triplicate, executed by the conservation commissioner to one W. A. Cochran of Celina, Ohio.

Each of these leases is for a stated term of fifteen years and each calls for an annual rental of \$15.00, payable semi-annually. The tract of land covered in one of these leases is 10.4 acres, one-half of which lies below waste-weir line of the reservoir, while two tracts of land of 4.89 and .30 acres are covered by the other lease. All three of these tracts of land are in the northeast quarter of Section 20, Township 6 South, Range 3 East, Mercer County, Ohio, and all are leased as Lake St. Marys Reservoir Lands.

On examination of these leases, I find that the same have been properly executed by the conservation commissioner and by W. A. Cochran, the lessee named in each of these leases.