



450 E. 96th Street
Suite 185
Indianapolis, IN 46240

317-663-4180 main
www.adisa.org

October 31, 2023 VIA EMAIL TO: csipubliccomments@governor.ohio.gov

Ohio Common Sense Initiative
77 S. High St., 30th Floor
Columbus, OH 43215-6117

Re: Ohio Division of Securities Rule 1301:6-3-09 Registration by Qualification

Dear Sir or Madam:

The Alternative & Direct Investment Securities Association (ADISA)¹ appreciates the opportunity to comment on the proposal of the Ohio Division of Securities Division (the Division) to amend Rule 1301:6-3-09 (the Proposal). ADISA's members include firms that sponsor and distribute non-exchange listed real estate investment trusts (REITs) and business development companies (BDCs), both of which are subject to the Proposal.

There is no practical benefit to recounting or otherwise discussing the procedural history of the Proposal here. While ADISA did not engage directly with the Division in regard to prior iterations of the Proposal, the Association has frequently participated in discussions with industry regulators at the state and federal level on issues of import to its members; in fact, ADISA submitted comments addressing some of the issues set forth in the Proposal when they were put forth in the context of proposed amendments to REIT guidelines being considered by the North American Securities Administrators Association (NASAA). ADISA appreciates the Division's continuing openness to hearing from industry members impacted by the Proposal and submits the following thoughts on the Proposal for the Division's consideration.

1. The Proposed Limitation on Illiquid or Restricted Securities

a. Scope and Reach

The Proposal would establish, in practical terms, a ten percent (10%) limitation on the ability of Ohio residents to purchase a security issued by a REIT or a BDC where the security restricts a purchaser's ability to exit from the investment (in whole or in part) for an "indefinite or significant period of time..." This 10% limitation would apply to the purchaser's "liquid net worth;" perhaps more importantly, the Proposal would include in the calculation of the limit "all holdings of the purchaser in the issuer, its affiliates, and other issuers of the same security" to the

¹ ADISA is the largest association of the retail direct investment industry in the United States. ADISA has approximately 5,000 members who employ over 220,000 investment professionals, together serving the interests of more than 2 million investors throughout the country. Direct and alternative investment programs serve a critical need in the creation and ongoing management of diversified investment portfolios.

extent that (i) the securities are subject to registration in accordance with the Ohio Revised Code,² and (ii) likewise restrict a purchaser's ability to exit in whole or part for an indefinite or significant period of time..." The Proposal also includes a provision that would permit an Ohio purchaser of such a security to avoid application of the 10% limit by submitting to the Division a completed waiver request prior to purchase.

The Division has a lengthy history of imposing limitations on purchases by Ohio investors of illiquid investments. ADISA is not proposing to challenge the thinking behind having some kind of limitation on the purchase by state residents of programs that limit or restrict liquidity. Similar provisions are imposed by other states in their merit review process. Moreover, as part of a framework to assess and manage the liquidity needs of investors, a limit of some kind can play a constructive role.³

In ADISA's view, the critical issue is the reach or scope of any such limit, particularly where it would be placed directly into the Division's merit review regulations. In simplest terms, we believe that the language of the proposed limitation is somewhat broad and potentially imprecise in its application, therefore making it more likely that the process of monitoring and enforcing the limitation would be fraught with errors, confusion and administrative difficulties. As proposed, the limitation would subject more than just a purchase of REIT or BDC shares to the limit. Rather, in applying the limit, any purchase of the program under review would have to be aggregated with purchases or holdings of the investor in securities that are subject to exit conditions or restrictions and that are (i) issued by affiliates of the program under review; and (ii) "the same security" and issued and sold in Ohio pursuant to the State's registration by coordination and registration by qualification rules.

In ADISA's view, based on the experience of its members, limitations that require a purchaser or his or her or its adviser to measure and include other programs that are sponsored by both related and potentially unrelated issuers in the calculus present a high likelihood of error or confusion. One adviser does not necessarily know which programs his or her or its clients already own, particularly where the client has spread his or her or its investments across multiple advisers and multiple firms and custodians. While use of the proposed waiver might obviate any concerns the investor and his or her adviser might have with regard to the purchase under consideration, the practice of placing restrictions (including limitations) on programs that in turn are enforced at the client/adviser level is a recipe for non-compliance in the best of circumstances.⁴

For these reasons, ADISA believes that the language of any limitation should reach only the security or program under consideration and leave out affiliated and other "similar" programs. Any such limitation would still support the Division's goals while guarding against confusion and worse in the application of the restriction.

² The language in the Proposal would pick up both offerings that are registered by coordination and those that are registered by qualification.

³ As discussed below, ADISA's comments on the language of the limitation are accompanied by thoughts on the role of a waiver in relieving investors and their advisers from compliance with any such limit.

⁴ For example, determining when something is the "same security" cannot be done with confidence without more – significantly more – guidance from the Division.

b. Waiver

As noted above, the Proposal provides that the effect of any limitation can be avoided by means of filing a pre-purchase waiver form with the Division. According to the Division, this form will be self-executing and not intended or designed to inhibit Ohio investors from investing in illiquid programs offered by REITs and BDCs. As the Division itself noted, it opted for a “self-executing waiver” that “purposefully flags key risks in simple and clear language that investors should be able to understand.” Furthermore, filing the waiver form “will allow all Ohio purchasers at all income levels to exceed the limit once key risks are acknowledged (assuming other federal and state conduct standards are met).” There is no filing fee or other cost associated with the waiver and firms relying on the waiver will not be required to keep copies of the form. Finally, according to the Division, “[t]here is no review or ruling on the waiver by the Commissioner or Division staff. The waiver is fully self-executing, meaning it will be automatically granted once the form is submitted.”

ADISA is pleased that the Division is considering an approach that would be applicable to any Ohio-based investor, whether or not accredited. As the Division itself stated, the definition of “accredited investor” found in Regulation D under the Securities Act of 1933, as amended, may undergo amendment in the near future, and qualifying as accredited under the definition does not necessarily provide assurance that the investor is willing to do without the protections of all otherwise-applicable laws and regulations.

Before going down the path of placing the waiver concept in its regulations, however, ADISA believes that the Division should give consideration to some of the ancillary but still important issues that use of such a document would raise. For example, the Division should discuss whether it can commit to not contacting those investors who file waivers to make further inquiries as to the circumstance of the execution and submission of the waiver document. And it should consider whether the regulation should, as put in place, contain an express provision stating that the proffer by a broker-dealer to its client of a waiver form in connection with an investment in a REIT, BDC or other non-fully liquid investment is not by itself evidence that the broker-dealer acted improperly or labored under an impermissible conflict of interest, except where the investor or the State can prove that the waiver was in fact procured via fraud or material misrepresentation.

ADISA appreciates the creative approach taken by the Division to the issues discussed immediately above and stands ready to work with the Division and others to frame the relevant issues and potentially bring about appropriate change(s) or amendment(s).

2. Proposed Advertising Guidelines

The Division is also proposing to add several advertising principles intended to limit or at least cut down on advertisements for securities programs that do not meet certain standards of care, accuracy and transparency. Prohibited materials would include those that:

- (i) inflate or distort the value or performance of securities purchased or held;

(ii) include misleading or incomplete financial metrics, such as using non-generally accepted accounting principles (GAAP) figures without presenting the most comparable GAAP figures;

(iii) conflict with the express terms of the prospectus or that downplay the risk disclosures set forth in the prospectus; or

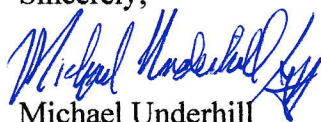
(iv) fail to provide a balanced presentation of risks and benefits of the investment or otherwise present risk in a manner that makes it difficult for prospective purchasers to read or understand.

ADISA supports efforts to ensure that investment programs of all kinds, and especially those pertaining to non-exchange listed REITs and BDCs, employ sales materials that are clear, comprehensive, and helpful to investors. Toward that end, the principles that the Division is proposing to put into its regulations aim to achieve similar if not the same goals. Having worked with dedicated advertising materials teams at FINRA, ADISA can say on behalf of its members that it is important to provide as much guidance and color around these requirements as is possible. Firms typically want to know how to comply with applicable rules, and if there are practices or approaches that Ohio has found to be problematic, it would be helpful for it to publish its thoughts along those lines, for the benefit of firms that want to comply and not get into a situation where they stand accused or worse of violating applicable guidelines.

For that reason, ADISA recommends that the Division publish FAQs that reflects its views on the issues presented by these guidelines, and to get and incorporate feedback from the industry on them. In the alternatives, the Division could provide additional clarity by creating and adding definitional terms to the guidelines, thereby providing additional information that can be used by issuers and the distributor partners in avoiding any intended missteps.

ADISA appreciates the opportunity to submit comments on the Division's Proposal and stand ready to meet with the Division or to otherwise work to increase regulatory understanding of these issues as they apply to these important investment products and programs.

Sincerely,



Michael Underhill
President

cc: ADISA Drafting Committee—John H. Grady, Catherine Bowman