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APPLICABILITY OF THE REGISTRATION REQUIREMENTS OF THE UTAH UNIFORM SECURITIES ACT TO THE OFFER AND SALE OF OIL AND GAS ~~INTEREST~~ Leasehold

Utah Securities Commission Release No._____

Dated

It has come to the attention of the Utah Securities Commission that clarification is required as to when the provisions of the Utah Uniform Securities Act, Section 61-1-1, et seq., are applicable to the offer and sale of various oil and gas leasehold interests.

Offerings of oil and gas leasehold interests will be required to be registered as a security under the Utah Uniform Securities Act when such offerings have characteristics similar to those described herein. In addition, persons engaged in the business of buying or selling investment contracts or participating in profit-sharing agreements of this type may be brokers or dealers within the meaning of the Utah Uniform Securities Act and, therefore, may be required to be registered as such with the Department of Business Regulation, under the provisions of Section 61-1-3 of the Act.

The offer of mineral interest, as such, without any collateral arrangements with the seller or others as an economic inducement to invest, is the offer of real estate and does not involve the offer of a security. Chase v. Morgan, 9 Utah 2d 125, 339 P.2d 1019 (1959).

Under certain circumstances and in the presence of various kinds of collateral arrangements, the offering of oil and gas leaseholds may involve the offering of an investment contract or participation in a profit-sharing agreement under the definition of Section 61-1-13(12) of the Utah Securities Act, which would be required to

be registered with the Securities Commission. Domestic and Foreign Petroleum Co. v. Long, 51 P.2d 73 (1935). It is when the presence of such arrangements indicates that the offeror is offering an opportunity through which the prospective purchaser may earn a return on his investment in the oil and gas interest, which will depend upon the efforts of the promoter or other third persons to obtain the benefits of the transaction for him, that the offer will be deemed to be a security under the Act. The manner of the offering, including the advertising, sales literature, promotional schemes, the sophistication of the purchaser, and the oral representations that emphasize the economic benefits to the purchaser, will be considered by the Commission in making such a determination.

Neighboring jurisdictions have held that a security interest may still be involved in situations where the oil promotion schemes are tailored to meet the tests laid down in the Joiner case, 320 U.S. 344, 64 S. Ct. 120 (1943). Oil Lease Service, Inc., v. Stephenson, 162 Cal. App. 2d 100, 327 P.2d 628, (1958). The Joiner case suggests that the sale of a security interest would not be involved if the neighboring test wells to be drilled by third parties were not controlled by the seller. However, the court in the Oil Lease Service case, supra, held that the appellant's business went far beyond merely acting as an agent to secure oil and gas leases. The appellant had offered, through advertisements, to procure United States Government oil and gas leases in Emery County, Utah, for interested purchasers ahead of "the big drilling campaign" to be conducted by one or more of the major oil companies. The court held that these certificates of interest in oil and gas leases were investment contracts and thus securities.

> The purchaser did nothing but pay the "fee" and appellant, as represented by it, did all of the work. Obviously the purchaser gave his money to appellant in the hope and upon its representation that by the use of its superior knowledge,

> experience, information and skill it would select for his lease areas "that appear favorable for future (oil) development" which he would be able to sell or assign later at a profit when oil was discovered and drilled by oil companies. Both purchaser and appellant knew that the areas involved were unproved land and that the purchaser had neither the knowledge nor experience to choose a potential oil area, nor the ability nor money to prospect or drill for oil. His profits, if any, depended not on his own efforts, or on the lease itself, but entirely on the efforts of others--first, on whether appellant, through its skill, chose for him an oil bearing area and, second, on whether an oil company would discover and drill for oil on that land. * * * 327 P.2d at 633.

The court in the Oil Lease Service case went on to point out that the name of the instrument making the conveyance is of little consequence in determining the type of interest that is actually being conveyed.[1] The determining factors are the facts and circumstances surrounding the transaction. The following constitute the type of factors that the Commission will deem to be relevant in making such a determination:

1. Where the seller represents (whether truthfully or falsely) that the land is oil bearing and that the purchaser can expect profits from the operations of the seller or some third party oil company or driller to whom the purchaser might lease the land at the present or in the future;

2. Where numerous purchasers of the mineral interest in the land execute community leases to the seller or to some third person as a part of the same transaction, or if it becomes apparent from the manner of the sale that the parties contemplate a community lease to a presently unidentified lessee-developer at some indefinite future time;

3. The size of the parcel of land conveyed, where the parcel may be so small that it would be economically unfeasible for the purchaser individually to exploit the oil on his own parcel;

4. The sophistication of the purchaser in previously having the means, knowledge and experience to develop oil and gas productions.

These factors and any others that tend to establish that the purchaser was not relying on his own efforts or the lease itself to earn his profits from the investment will be deemed relevant in determining if the sale of a security interest is involved.

Other cases which support the Commission's determination that the sale of oil and gas leasehold interests in this manner constitutes the offering of a security are: Roe v. United States, 287 F.2d 435 (5th Cir. 1961), cert. denied, 368 U.S. 824, 82 S. Ct. 43 (1961); Moses v. Michael, 292 F.2d 614 (5th Cir. 1961); SEC v. Addison, 194 F. Supp. 709 (N.D. Texas 1961).

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1. "Appellant contends that any assignment of a part of a 640-acre lease becomes a distinct and separate lease under federal law and constitutes a lease under California law, not a security. * * * In presenting such an argument, appellant overlooks the very feature of its operations that clearly brings most of its transactions within the purview of the corporations code--the use of the assignment form which could not possibly constitute a lease until the assignment of lease was approved by the government. * * * Until this assignment form was submitted to the government for its approval of the assignment by appellant from its master lease to the purchaser, the document did not become a lease with the government. This document so employed clearly brings it within the operation of section 25008 of the Corporations Code.