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ARIZONA ATTORNEY GENERAL

August 18, 1959

Mr. Joe Sotelo, Acting Director
Securities Division
Arizona Corporation Commission
Capitol Annex Building
Phoenix, Arizona

MAGGIORE
VANLANDINGHAM
CHURCH

Dear Mr. Sotelo:

In answer to your letter of July 30th, we have prepared the following for your consideration.

Reference is made to the letter from attorney Thomas B. Hargis addressed to your office and dated July 23rd. We believe the statement of law contained therein is essentially correct, to-wit, 1. The transfer of a naked leasehold interest does not constitute the sale of a security; 2. However, to determine whether or not sale of a certain interest is a security, we must go behind the form of the document used and consider the substance of the transaction. People v. Syde, 235 P.(2d) 601; Securities and Exchange Comm. v. C. W. Joiner Leasing Corp., 320 U.S. 344, 163 A.L.R. 1061; Moore v. Stella (1942), 52 Cal. App.(2d) 766, 127 P.(2d) 300; Domestic & F. Petroleum Co. v. Long (1935), 4 Cal.(2d) 547, 51 P.(2d) 73.

The statute in question A.R.S. §44-1801, reads in part as follows:

"13. 'Security' or 'securities' include *** any fractional interest in an oil, gas or mineral lease, claim, permit or right, any assignment of subdivided portions of any oil, gas or mineral lease, permit, claim or right which is subdivided for the purpose of a public offering, any certificate of interest in title to property, earnings or profits, or, in general, any instrument commonly known as a security, including any guarantee of, temporary or interim receipt for, certificate for, or warrant or right to subscribe to any of the foregoing."

Similar statutes have been construed in other states along two general lines: (1) the more liberal

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view holds that a transfer of an interest in an oil lease is not a security unless the purchaser depends upon further action of the seller to reap a profit, and (2) the more strict rule that the sale of any subdivided portion of an oil and gas lease, interest, right or claim constitutes the sale of a security. Our court has not ruled directly on this point, and we therefore have only the statute to guide us. In considering the intent of the legislature it would appear that the statute itself is clear and unambiguous, and we must therefore conclude that the legislature intended to say exactly what the statute says and such conclusion leads us to believe that we should adhere to the more strict rule.

As a practical matter, the only real way to determine whether a particular transaction constitutes the sale of a security is to look beyond the form of the instrument of conveyance to the substance of the transaction. In the particular instance we have only the attorney's well meaning and I am sure competent and conscientious advice of the intentions of the parties, when in fact the real nature of the transactions proposed may not be evident until such transactions are made. We caution that no matter what the best guess might be as to whether this transaction would be a security at the present time, the actual facts of the transaction later might make it a security and by reason of this fact the entire transaction be subject to rescission.

With these matters in mind we turn to the question further presented upon the request for exemption under A.R.S. §44-1846. Assuming the proposed transaction to be one involving securities, the Commission would then have to determine whether the qualifications of the above statute are met, namely, that the petitioner agrees to limit the number of offerees, agrees to limit the time of offering, and shows that the transaction in question is of sufficient special character not essential to public interest. The finding on these matters is of course administrative with the Commission, but if these elements are not found to the satisfaction of the Commission, then the exemption should be denied.

In summary, it is the opinion of the office of the Attorney General that the sale of a subdivided portion of an oil and gas lease as outlined in the letter from Mr. Hargis would constitute the sale of a security under A.R.S. §44-1801, and whether or not the exemption applied for should be granted, is an administrative decision of the Commission but can only

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be granted if the requirements of A.R.S. §44-1846 are met
to the satisfaction of the Commission.

Respectfully submitted,

WADE CHURCH
The Attorney General

V. D. MAGGIORE
Assistant Attorney General

VDM:JV:lmh