



# Common Sense Initiative

Mike DeWine, Governor  
Jim Tressel, Lt. Governor

Joseph Baker, Director

## Business Impact Analysis

Agency, Board, or Commission Name: Department of Commerce – Division of Securities

Rule Contact Name and Contact Information: Roger L. Patrick, Jr., 614-644-4859,  
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Regulation/Package Title (a general description of the rules' substantive content):

1301:6-3-09 Registration by Qualification

Rule Number(s): 1301:6-3-09

Date of Submission for CSI Review: March 13, 2025

Public Comment Period End Date: March 21, 2025

Rule Type/Number of Rules:

New/\_\_\_ rules

No Change/\_\_\_ rules (FYR? \_\_)

Amended/ 1 rules (FYR? \_\_)

Rescinded/\_\_\_ rules (FYR? \_\_)

The Common Sense Initiative is established in R.C. 107.61 to eliminate excessive and duplicative rules and regulations that stand in the way of job creation. Under the Common Sense Initiative, agencies must balance the critical objectives of regulations that have an adverse impact on business with the costs of compliance by the regulated parties. Agencies should promote transparency, responsiveness, predictability, and flexibility while developing regulations that are fair and easy to follow. Agencies should prioritize compliance over punishment, and to that end, should utilize plain language in the development of regulations.

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### **Reason for Submission**

1. R.C. 106.03 and 106.031 require agencies, when reviewing a rule, to determine whether the rule has an adverse impact on businesses as defined by R.C. 107.52. If the agency determines that it does, it must complete a business impact analysis and submit the rule for CSI review.

**Which adverse impact(s) to businesses has the agency determined the rule(s) create?**

**The rule(s):**

- a. ☒ Requires a license, permit, or any other prior authorization to engage in or operate a line of business.
- b. ☒ Imposes a criminal penalty, a civil penalty, or another sanction, or creates a cause of action for failure to comply with its terms.
- c. ☒ Requires specific expenditures or the report of information as a condition of compliance.
- d. ☐ Is likely to directly reduce the revenue or increase the expenses of the lines of business to which it will apply or applies.

### **Regulatory Intent**

2. Please briefly describe the draft regulation in plain language.  
*Please include the key provisions of the regulation as well as any proposed amendments.*

The Division proposes to amend O.A.C. 1301:6-3-09 by adding two new subsections marked as (A)(4) and (A)(5). The rule governs registrations by qualification and registrations by coordination. Among other things, O.A.C. 1301:6-3-09 specifies the application requirements for registration; provides direction as to the materials to be filed; and sets offering periods. The Division proposes to amend O.A.C. 1301:6-3-09 by incorporating by reference national industry standards and by formally adopting guidelines that have been used by the industry and enforced by the Division for many years to facilitate state registration.

More specifically, the Division proposes (as directed by JCARR) to formally codify North American Securities Administrators Association (NASAA) Statements of Policy, Ohio merit guidelines, advertising guidelines, and a concentration limit policy. These policies and guidelines have been around for a long time but are being codified now to (1) make the policies more available to the public and impacted businesses and (2) further define various statutory terms. To maintain the flexible nature of these policies, the proposed amendment allows for a good cause waiver of all the foregoing policy guidelines by expressly prefacing the new subsections with the text “absent good cause shown” and

by providing an exemption from the concentration limit for sales to Ohio purchasers who meet the federal definition of an accredited investor.

**3. Please list the Ohio statute(s) that authorize the agency, board or commission to adopt the rule(s) and the statute(s) that amplify that authority.**

Ohio Revised Code Section 1707.20 gives the Division broad rulemaking authority. R.C. 1707.20 (A)(1) states: "The division of securities may adopt, amend, and rescind such rules, forms, and orders as are necessary to carry out sections 1707.01 to 1707.50 of the Revised Code, including rules and forms governing registration statements, applications, and reports, and defining any terms, whether or not used in sections 1707.01 to 1707.50 of the Revised Code, insofar as the definitions are not inconsistent with these sections."

Ohio Revised Code Section 1707.09 provides the statutory framework, standards, and fees for registrations by qualification and, therefore, amplifies the Division's existing rulemaking authority under R.C. 1707.20. As noted above, the statutory framework and standards for registration by qualification under R.C. 1707.09 apply also to registration by coordination, as defined in R.C. 1707.01 (Q)(1)(3). That definition states: "Reference in this chapter to registration by qualification also includes registration by coordination unless the context otherwise indicates." That statutory language is reinforced in O.A.C. 1301:6-3-091, which states: "The provisions of rule 1301:6-3-09 of the Administrative Code shall apply to registrations by coordination pursuant to section 1707.091 of the Revised Code."

**4. Does the regulation implement a federal requirement? Is the proposed regulation being adopted or amended to enable the state to obtain or maintain approval to administer and enforce a federal law or to participate in a federal program?**

***If yes, please briefly explain the source and substance of the federal requirement.***

No. The regulation does not implement a federal requirement. Registrations by coordination require separate registrations at both the federal and state level. Unlike federally covered securities (e.g., stock traded on the New York Stock Exchange and most private placements), offerings registered by coordination must meet all state registration requirements to be declared effective in the state of sale. The SEC applies federal law to the federal registration and the Division applies Ohio law to the state registration. The proposed regulation implements the state requirements only.

**5. If the regulation implements a federal requirement, but includes provisions not specifically required by the federal government, please explain the rationale for exceeding the federal requirement.**

Not applicable. As explained above in response to BIA Question 4, the proposed regulation implements state requirements that are set out in state statute, separate and apart from any requirements set forth in federal law. The lead stakeholder in this

rulemaking initiative acknowledged in its August 14, 2023 JCARR testimony that “technically speaking,” the regulation implements “state requirements, not a federal law or rule.”

**6. What is the public purpose for this regulation (i.e., why does the Agency feel that there needs to be any regulation in this area at all)?**

The regulation gives effect to the anti-fraud standard set forth in statute (R.C. 1707.09), which prohibits securities from being offered on “grossly unfair terms” or “in a manner that would tend to defraud or deceive investors.” The regulation helps filers by giving them guidance on how the Division interprets those statutory terms. The regulation helps Ohio investors by screening out fraud and other abusive terms and practices.

The investor safeguards embodied in this anti-fraud standard are important because most of the capital raised through this regulation is for complex, higher-risk investment offerings (non-traded REITs and BDCs) that are registered by coordination. Investor risks are noted in disclosures scattered throughout the product prospectuses.<sup>1</sup>

Risks that are disclosed and mitigated as the result of this regulation include illiquidity, hardships arising from unanticipated interruptions in income, and complete loss of investment. For example:

- The core set of products registered by coordination in Ohio (non-traded REITs and BDCs) are structured as perpetual life vehicles<sup>2</sup> that place no limits on how long the REIT or BDC sponsor can suspend monthly distributions (returns)<sup>3</sup> or pro-rate or suspend redemptions (exit).<sup>4</sup> Sponsors retain the unilateral right to suspend

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<sup>1</sup> Non-traded REITs and BDCs are frequently offered through affiliates of a common parent company and share many of the same structural risks. Upon request, the Division can produce a digital copy of the prospectuses for all non-traded REITs and BDCs registered in Ohio. Given the volume (aggregated page length of approximately 13,000 pages), the Division would recommend that Committee members review the prospectuses for [Blackstone Real Estate Income Trust](#) (BREIT) and [Blackstone Private Credit Fund](#) (BCRED) as typical samples. BREIT and BCRED are the largest non-traded REIT and non-traded BDC products in the country.

<sup>2</sup> BREIT (pdf of linked prospectus) at 325 (explaining “perpetual life” means “an investment vehicle of indefinite duration”); BCRED (pdf of linked prospectus) at 740 (same).

<sup>3</sup> BREIT at 315 (“Distributions are not guaranteed and may be funded from sources other than cash flow from operations, including, without limitation, borrowings, the sale of our assets, repayments of our real estate debt investments, return of capital or offering proceeds, and advances or the deferral of fees and expenses.”); BCRED at 712 (same).

<sup>4</sup> BREIT at 325 (“the investor may request that we repurchase their shares on a monthly basis, but we are not obligated to repurchase any shares and may choose to repurchase only some, or even none, of the shares that have been requested to be repurchased in any particular month in our discretion”); BCRED at 340 (same but only on a quarterly basis, rather than monthly).

distributions and withdrawals indefinitely at any time with little to no advance warning.<sup>5</sup>

- Sponsors allow investors to exit at redemption rates not to exceed 2% NAV per month, 5% NAV per quarter, and a max redemption of 20% NAV per year.<sup>6</sup> From 2017 when the first major NAV REIT hit the market through 2020, NAV product sponsors were generally able to satisfy investor redemption requests on a monthly basis. But during the pandemic, four smaller NAV REITs were forced to pro-rate or suspend their redemption programs. By late 2022, fundraising had slowed as redemption requests spiked, prompting pro-ration by the two largest NAV REIT sponsors.<sup>7</sup> The largest NAV sponsor denied 99.7% of investor redemption requests in December of 2022 and continued pro-ration for fifteen consecutive months.<sup>8</sup> The second largest NAV sponsor continues pro-ration today and currently caps investor redemption to 0.3% of NAV per month. Extended denials can create great stress for investors, especially retirees living on fixed incomes who need the distributions (or need to cash out) in order to pay living expenses.
- Product sponsors disclose that investors should not invest unless they can afford to lose the entire amount of their investment.<sup>9</sup> This is not a theoretical risk.<sup>10</sup>

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<sup>5</sup> BREIT at 329 (“our share repurchase plan may be modified or suspended”); BCRED at 732 (“our share repurchase program may be amended or suspended at the discretion of the Board of Trustees at any time”).

<sup>6</sup> BREIT at 65 (“The Repurchase Plan will be limited to no more than 2% of the Company’s aggregate NAV per month (measured using the aggregate NAV as of the end of the immediately preceding month) and no more than 5% of the Company’s aggregate NAV per calendar quarter (measured using the average aggregate NAV as of the end of the immediately preceding three months).”); BCRED at 739 (5% per quarter at the company’s discretion).

<sup>7</sup> In December of 2022, the two largest REIT sponsors in the country pro-rated redemptions and froze millions of shares held by Ohio investors, rejecting more than \$20 million in Ohio cash-out requests in that month alone. Jason Zweig, *You Bought a Hot Fund. Now It’s On Ice: Investors Who Piled Into an Unconventional Blackstone Real Estate Fund Now Can’t Get More Than a Sliver of Their Money Out*, Wall Street Journal (Dec. 9, 2022), <https://www.wsj.com/articles/breit-blackstone-redemption-real-estate-income-trust-11670609862>. The largest REIT sponsor continued pro-rations for fifteen consecutive months. Other REIT sponsors continue to gate redemptions.

<sup>8</sup> Blackstone, Starwood, KKR, and RREEF.

<sup>9</sup> BREIT at 382 (“potential investors should regard an investment in us as being speculative and having a high degree of risk”); BCRED at 716 (“risk that the investor may lose its entire investment”).

<sup>10</sup> Notable examples of REIT offerings involving significant investor losses include: United Development Funding REIT, Apple REIT (not affiliated with big tech company Apple), Wells Timber REIT, and Hartman REIT. In each case, federal regulators missed red flags and cleared the offerings, only to take enforcement action later after the offerings harmed investors in other states. The United Development Funding REIT case was a billion-dollar REIT that harmed 30,000 victims in other states; 4 executives were later convicted and sentenced to 20 years in federal prison. See, e.g., Bill Hethcock, *Government: 30,000 investors, banks*

- Firms selling these products emphasize illiquidity as a key risk, acknowledging that product sponsors can block investor exits through suspension or pro-ratio of redemption requests:
  - “Business Development Companies (BDCs). BDCs are types of closed-end investment companies, which are available to clients meeting certain qualification standards. Generally, BDCs invest primarily in the debt and equity of private and/or small U.S. companies and may offer distribution rates generated through potentially significant credit and liquidity risk exposures amplified through leverage. As with other high-yield investments, such as floating-rate/leveraged loan funds, private REITs and limited partnerships, investors are exposed to significant market, credit, interest rate and liquidity risks. In addition, BDCs run the risk of over-leveraging their relatively illiquid portfolios. Due to the illiquid nature of non-traded BDCs, investors’ exit opportunities may be limited only to periodic share repurchases by the BDC. A tender offer pursuant to a share redemption program may be oversubscribed so that the BDC accepts only a pro rata portion of the shares a client tenders during a redemption program. In such cases, a client may experience significant delays (including, potentially, indefinite delays) to exit from the investment. In addition, share redemption programs may be shut down at any time at the discretion of the issuer’s board. Also, BDCs may fund distributions from offering proceeds or

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*nationwide bamboozled by United Development Funding in Ponzi-like scheme*, Dallas Business Journal (Feb. 10, 2022), <https://www.bizjournals.com/dallas/news/2022/02/10/victims-united-development-funding.html>. The Apple REIT and its affiliated BDC’s captive broker-dealer were ordered to pay \$14 million in restitution to harmed customers. See, e.g., FINRA News Release, *FINRA Sanctions David Lerner Associates \$14 million for Unfair Practices in Sale of Apple REIT Ten and for Charging Excessive Markups on Municipal Bonds and CMOs* (Oct. 22, 2012), <http://www.finra.org/home/Newsroom/NewsReleases/2012/P191729>. The company was fined for 116 pieces of advertising containing misleading, unwarranted or exaggerated statements. See, e.g., Diana Britton, *Non-Traded REITs Raising Red Flags in the Industry*, Wealth Management Magazine (Nov. 22, 2011), <https://www.wealthmanagement.com/investment/non-traded-reits-raising-red-flags-industry>; FINRA News Release, *FINRA Fines Wells Investment Securities \$300,000 for Use of Misleading Marketing Materials for REIT Offering* (Nov. 22, 2011); <https://www.finra.org/media-center/news-releases/2011/finra-fines-wells-investment-securities-300000-use-misleading-marketing>. Allen Wells, the REIT CEO, had a history of securities laws violations. Dean Starkman, *NASD Suspends Wells President from Broker-Dealer Arm for Year*, Wall Street Journal (Oct. 13, 2003), <https://www.wsj.com/articles/SB106607847441279500>. The founder of the Hartman REIT was subsequently removed and sued by the company for misappropriation and mismanagement. The company is reportedly under investigation by the SEC. *Silver Star chairman accuses former CEO Allen Hartman of mismanagement, unauthorized borrowing*, Real Deal (Nov. 28, 2023), <https://therealdeal.com/texas/2023/11/28/silver-star-accuses-former-ceo-allen-hartman-of-misdeeds/>; Silver Star Properties REIT 8-K, Current Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 (Feb. 2, 2024), <https://www.sec.gov/ixviewer/ix.html?doc=/Archives/edgar/data/1446687/000144668724000052/fil-20240202.htm>.

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borrowings, which may constitute a return of capital and reduce the amount of capital available to make investments. In some cases, there may be an additional cost to investors who redeem before holding the shares for a specified number of years.”<sup>11</sup>

- “REITs. REITs invest in real estate, and there are special risks associated with investing in real estate, including, but not limited to, sensitivity to changes in real estate values, the risk of investment loss due to the use of leveraging and other speculative investment practices, interest rate risk, lack of liquidity and performance volatility. Non-Traded REITs are not required to provide annual valuations until two years and 150 days after reaching the minimum capital raise required to begin purchasing properties. This threshold is generally outlined in the product’s prospectus. Non-Traded REITs, which are available to clients meeting certain qualification standards, may fund distributions from offering proceeds or borrowings, which may constitute a return of capital and reduce the amount of capital available to invest in new assets. Clients should be aware that these securities may not be liquid as there is no secondary trading market available. At the absolute discretion of the issuer of the security, there may be certain repurchase offers made from time to time. However, there is no guarantee that client will be able to redeem the security during the repurchase offer. Issuers may repurchase shares at a price below net asset value. The repurchase program may also be suspended under certain circumstances.”<sup>12</sup>
- Federal regulators (the SEC and FINRA) have highlighted the foregoing product risks in investor alerts and have identified these products as examples of “complex” and “high-risk” products for which they apply heightened regulatory scrutiny. These federal notices continue to be released after the industry shift from lifecycle to NAV products.<sup>13</sup>

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<sup>11</sup> Sample from LPL Financial, [Risks Of Investing With LPL Investment Advisory Programs](#) (accessed February 27, 2025).

<sup>12</sup> *Id.*

<sup>13</sup> *E.g.*, FINRA, *FINRA Reminds Members of Their Sales Practice Obligations for Complex Products and Options and Solicits Comment on Effective Practices and Rule Enhancements*, FINRA Reg. Notice 22-08 (May 2022), <https://www.finra.org/rules-guidance/notices/22-08>. (listing non-traded REITs as example of “complex product” in section called “What is a complex product?” and separately referred to “business development companies as example of a “high-risk” complex product); See, e.g., FINRA Investor Insights, [Concentrate on Concentration Risk](#) (June 15, 2022) (“(Low-priced stocks, non-traded REITs and private placements might be hard to sell on short notice or at an efficient price.... If a large percentage of your portfolio is tied up in illiquid securities, consult an investment professional about potential remedies.”); SEC Office of Compliance, Inspections, and Examinations, [2021 Examination Priorities Report](#) at 21, (Mar. 3, 2021) (identifying REITs as example of a “complex product” that it would be reviewing as an exam priority).

- Collectively, non-traded REITs and BDCs represent a small fraction of market assets (far less than 0.1%) but consistently appear on FINRA's list of products generating the most investor complaints.

## **7. How will the Agency measure the success of this regulation in terms of outputs and/or outcomes?**

As part of the Ohio Department of Commerce, the Division's mission is to promote prosperity by protecting what matters most. The Division achieves this mission through regulations that (1) facilitate capital formation and (2) protect Ohio investors. To measure the success of this regulation, the Division will consider the following capital formation and investor protection outputs.

### **Capital Formation Outputs**

The Division does not routinely collect sales data from filers to know exactly how much capital is raised directly from Ohio investors in any single offering or in any industry, but the Division works very hard to approve all registration applications so that every filer has an opportunity to raise capital in this state. The Division's clearance rate is the primary output or metric that the Division uses to measure its success in facilitating capital formation. When it comes non-traded REITs and BDCs, the Division has a 97% clearance rate. The Division does not expect this output to change as the result of the regulation.

Stakeholders have reported various capital formation statistics in their comment letters and the Division has collected additional data through exam to analyze business impact that can also be monitored as outputs. For example, stakeholders report that non-traded REIT and BDC filers have raised nearly \$2 billion from Ohio investors in the past thirty years. In addition to marketing allowances and other forms of cash and non-cash compensation, selling firms have collected 8.75% to 15% of the gross offering proceeds in seller compensation, meaning they have collected \$175 million to \$300 million in Ohio compensation. No data has been produced to suggest that Ohio is lagging other states nationally on a per capita basis when it comes to capital raises or sales compensation.<sup>14</sup>

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<sup>14</sup> Ohio's securities industry has grown over 56% from around 160,000 firms and agents back in 2008 to more than 250,000 today. According to data compiled by the SEC's Office of the Small Business Advocate, Ohio contributed over \$23.7 billion of capital to registered offerings and over \$8 billion to private Reg D offerings in 2022. SEC, Office of the Advocate for Small Business Capital Formation, *Annual Report for Fiscal Year 2022* (2022), <https://www.sec.gov/files/2022-oasb-annual-report.pdf>. Ohio ranks #7 in the number of individual brokers and state-registered investment advisers based on home state residence, making it one of only two Midwestern states that rank in the top ten in these categories (other being Illinois). *SIFMA Capital Markets Report for 2022*, <https://www.sifma.org/wp-content/uploads/2022/07/CM-Fact-Book-2022-SIFMA.pdf>; *NASAA 2023 Investment Adviser Report*, <https://www.nasaa.org/wp-content/uploads/2023/09/2023-IA-Section-Report-FINAL.pdf>.



Moreover, the new accredited investor exemption proposed for the 10% concentration limit could increase capital raises and seller compensation moving forward.

### **Investor Protection Outputs**

While capital formation outputs are important metrics for the Division to consider in measuring the success of this regulation, investor protection outputs are important, too. As noted above, Ohio Administrative Code Rule 1301:6-3-09 is at its core an anti-fraud regulation designed to screen out grossly unfair terms and practices that would tend to defraud or deceive Ohio investors. Some of the most serious risks of harm include a sudden and unexpected reduction or suspension of distributions (returns), the pro-rata or suspension of redemptions (exit) for a significant or indefinite period of time, and a total loss of investment.

Relevant investor protection outputs include the number of regulatory actions, customer complaints, and other accounts of investor harm and hardship flowing from the products registered via this regulation. The Division has analyzed these outputs by collecting and reviewing the following data sources:

- (1) the Division's own complaint and exam data;
- (2) state and federal regulatory actions involving the products;
- (3) customer complaints disclosed in the CRD/IARD systems;
- (4) the products' appearance and ranking on FINRA's list of *Top 15 Security Types in Customer Arbitrations*;
- (5) academic and industry reports;
- (6) media reports; and
- (7) data provided by consumer advocacy groups.

The Division's key metric of investor protection success will be for Ohio to maintain a low incidence of investor complaints. In response to stakeholder and Ohio legislator requests, the Division has analyzed data comparing Ohio's complaint data involving these products with the complaint data observed in other states. The source is CRD/IARD data that were published online in the form of sortable Excel datasets to allow free, public access.<sup>15</sup> All investment professionals in the country are required to disclose customer complaints

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<sup>15</sup> Complete CRD/IARD datasets going back to year 2000 have been published through a direct download by the economic consulting firm SLCG. SLCG is the same firm that provided expert economic analysis on the behalf of Ohio and lead counties (Trumbull and Lake) in the opioid litigation and its analysis of non-traded REITs has been cited by the SEC in its rulemaking. See, e.g., SEC Adopting Release No. 34-86031, *Regulation Best Interest: The Broker-Dealer Standard of Conduct*, 17 CFR Part 240 (citing Craig McCann, [Fiduciary Duty and Non-traded REITs](#), INVESTMENTS & WEALTH MONITOR at 39 (July/Aug. 2015)). The CRD/IARD datasets are available online [here](#). The home state for each broker or investment adviser representative disclosing a complaint can be identified by searching for the broker's or investment adviser representative's full report on the online FINRA database [BrokerCheck](#), also free and publicly accessible.

through the CRD/IARD systems. The Division analyzed over a thousand complaints with state identifiers disclosed in the CRD/IARD systems over the past five years (2019 through 2023) that specifically referenced non-traded REITs, BDCs, and alternative products.<sup>16</sup>

To derive a complaint rate, the Division pulled data from [SIFMA Capital Markets Fact Book \(2023\)](#) and [FINRA Industry Snapshot Report \(2023\)](#), which report the number of investment professionals licensed in each U.S. jurisdiction. The Division also pulled [U.S. Census Data \(2023\)](#) to derive the incidence of complaints on a per capita basis for each U.S. jurisdiction. States had complaint rates ranging from a low of 0% to a high of 0.9% per home state FINRA rep, with instances as high as 1 complaint for every 98,000 residents to a low of 1 complaint for every 2 million residents. No matter how the data is sliced, Ohio has a lower rate of complaints than comparable states that lack the investor safeguard of a concentration limit that is being codified in this regulation.

For the full five-year period, there were a total of 21 Ohio customer complaints involving a non-traded REIT, BDC, or alternative product. Ohio is the home state of 19,812 registered FINRA representatives and home to 11.785 million Ohio residents. On a FINRA rep basis, Ohio has a 0.1% complaint rate. On a per capita basis, Ohio had 1 customer complaint disclosed for every 561,000 Ohio residents.

On a national basis, Ohio had the lowest incidence of complaints on a per capita basis of the ten largest states in the country. This was not an anomaly. Large states *with* some form of concentration limit consistently had fewer incidences on a per capita basis than states *without* any form as a registration condition.

1. Illinois (highest) – 1 complaint per every 151,000 residents – no concentration limit
2. Florida – 1 complaint per every 166,000 residents – no concentration limit
3. New York – 1 complaint per every 227,500 residents – no concentration limit
4. Michigan – 1 complaint per every 245,00 residents – no concentration limit
5. North Carolina – 1 complaint per every 285,000 residents – no concentration limit
6. California – 1 complaint per every 297,000 residents –concentration limit
7. Georgia – 1 complaint per every 315,000 residents – no concentration limit
8. Pennsylvania – 1 complaint per every 360,000 residents –concentration limit
9. Texas – 1 complaint per every 430,000 residents –concentration limit<sup>17</sup>

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<sup>16</sup> Brokers and investment adviser representatives are required to report the nature of customer disputes on the Form U-4 and are given an opportunity to respond to the complaints in a separate narrative field. The Division was able to identify complaints involving non-traded REITs, BDCs, and alternative products by filtering the data appearing in those two fields.

<sup>17</sup> A stakeholder objected to the Division's analysis based on its understanding that Texas does not impose concentration limits on non-traded REITs or BDCs. The Division is not an expert on Texas's registration practices but classified Texas as a state that applied a concentration limit in the Division's analysis because Texas had applied limits during the five-year period reviewed. Texas applied a limit as recently as November of 2021 in the \$7.5 billion Brookfield REIT. See e.g., [Brookfield Real Estate Income Trust Inc. Prospectus](#) (Nov. 2, 2021). In that REIT, Texas investors were limited to investing no "more than 10% of their liquid net worth in this offering and other similar direct participation investments," which is more restrictive than Ohio's limit.

10. Ohio (lowest) – 1 complaint per every 561,000 residents –concentration limit

Georgia was the only large non-concentration limit state with a per capita incidence of complaint lower than at least one of the states applying some form of concentration limit (California). But as shown in the chart below, on a FINRA rep basis, Georgia's complaint rate was higher than all four large states that have imposed some form of concentration limit during the five-year period (California, Pennsylvania, Texas, and Ohio).

Ohio's complaint rate fared equally well on a regional basis. Neighboring states that approximate Ohio's number of FINRA reps and residents include Illinois, Indiana, Michigan, and Pennsylvania. Complaint data for these neighboring states are as follows:

- Illinois is home to 31,877 FINRA reps and has 12.549 million residents. Illinois had 83 customer complaints, resulting in a complaint rate of 0.3% per FINRA rep and 1 customer complaint for every 151,000 Illinois residents.
- Indiana is home to 8,612 FINRA reps and has 6.862 million residents. Indiana had 35 customer complaints, resulting in a complaint rate of 0.4% per FINRA rep and 1 customer complaint for every 196,000 Indiana residents.
- Michigan is home to 12,500 FINRA reps and has 10.037 million residents. Michigan had 41 customer complaints, resulting in a complaint rate of 0.3% per FINRA rep and 1 customer complaint for every 245,000 Michigan residents.
- Pennsylvania is home to 25,696 FINRA reps and has 12.961 million residents. Pennsylvania had 36 customer complaints, resulting in a complaint rate of 0.1% per FINRA rep and 1 customer complaint for every 360,000 Pennsylvania residents.

Comparing Ohio with these four neighbor states, Ohio had the lowest complaint rate on both a FINRA rep and per capita basis. The next lowest was Pennsylvania with the same 0.1% rate, but a stronger incidence. Pennsylvania has also imposed a concentration limit. The complaint rates in the other three neighboring states (Illinois, Indiana, and Michigan) were 3 to 4 times higher than Ohio's and Pennsylvania's. All three of those states lack the investor safeguard of a concentration limit that is being codified by this regulation.

**8. Are any of the proposed rules contained in this rule package being submitted pursuant to R.C. 101.352, 101.353, 106.032, 121.93, or 121.931?**

Yes. The proposed rules in this rule package are being submitted pursuant to R.C. 101.352.

***If yes, please specify the rule number(s), the specific R.C. section requiring this submission, and a detailed explanation.***

O.A.C. 1301: 6-3-09 was initially submitted for amendment pursuant to R.C. 101.352. The Division was asked to appear before JCARR for a "policy into rule" discussion on October 12, 2021. Prior to the hearing, the Division agreed to undertake a rulemaking

effort to incorporate NASAA Statements of Policy into rule, eliminating the need for the Division's appearance at the hearing. The Division circulated a draft of the amended rule to stakeholders in April 2022. The complaining stakeholder was not satisfied with the Division's draft, leading to a second JCARR notice (dated November 10, 2022) requesting the Division's appearance at a December 12, 2022 hearing. At the conclusion of the hearing, JCARR voted to recommend that the Division commence the rule making process to incorporate NASAA Statements of Policy and other policy guidelines into rule, as described above. The Division submitted a final rule for JCARR approval in August of 2023, but JCARR remanded the rulemaking to CSI, stating the rule package was not ready for a JCARR vote. The Division revised the rule package, collected additional data as well as additional stakeholder comments and is re-submitting a final rule for CSI and JCARR approval.

### **Development of the Regulation**

#### **9. Please list the stakeholders included by the Agency in the development or initial review of the draft regulation.**

Financial Industry Regulatory Authority (FINRA)  
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**10. What input was provided by the stakeholders, and how did that input affect the draft regulation being proposed by the Agency?**

The Division solicited input from stakeholders on multiple occasions in the past three years. The Division is now circulating the ninth draft of the proposed rule to address

stakeholder comments and concerns. Key stakeholder input and Division responses involving the rule proposal can be summarized as follows:

| <b>Stakeholder Input</b>   | <b>Division Response</b>  |
|--|---|
| Division should codify NASAA Statements of Policy, comment letters, and newsletters into rule  | <b>DRAFT #1 (APRIL 25, 2022)</b><br>Division proposed codification of NASAA Statements of Policy into 1301:6-3-09; Division was advised by JCARR that it was not necessary to codify comment letters or newsletters into rule   |
| Division should submit every NASAA Statement of Policy as a separate rulemaking proposal (rather than list policy statements in serial fashion) and list each by version date  | <b>DRAFT #2 (MAY 27, 2022)</b><br>Division revised rule to list NASAA Statements of Policy by version date but declined request to create multiple rulemaking proposals for revisions to a single rule  |
| <b>JCARR Hearing (December 12, 2022)</b>   |   |
| Division should add the 10% concentration limit and other unspecified policies of general application into rule proposal   | <b>DRAFT #3 (JANUARY 20, 2023)</b><br>Division added 10% concentration limit and other policies of general application identified in comment process into rule proposal; circulated draft for public comment  |
| Division should eliminate or exempt accredited investors from 10% concentration limit policy; Division should revise term “extended” in reference to period of time in new section (5); Division should provide a detailed business impact analysis of the 10% limit                               | <b>DRAFT #4 (JUNE 13, 2023)</b><br>Division revised 10% concentration limit policy by creating new self-executing waiver process and form for all investors; Division replaced term “extended” with “significant” in new section (5), consistent with language used by stakeholder; Division provided a detailed memorandum analyzing business and investor impact of proposed rule |
| <b>JCARR HEARING (AUGUST 14, 2023) &amp; RE-REFERRAL TO CSI (AUGUST 15, 2023)</b>  |   |
| CSI directs Division to update its business impact analysis (BIA) form and complete additional round of stakeholder comment within 30 days   | <b>DRAFT #5 (AUGUST 22, 2023)</b><br>Division updated BIA and recirculated draft rule for additional round of comment   |
| <b>CSI RECOMMENDATION THAT RULE BE RE-FILED TO ALLOW FURTHER DIALOGUE (SEPTEMBER 14, 2023)</b>   |   |
| Competing views on 10% concentration limit with consumer groups supporting retention of limit while opposing an exemption on one hand with industry groups requesting elimination or accredited investor exemption on other hand   | <b>DRAFT #6 (OCTOBER 4, 2023)</b><br>Division made minor revision to rule language in section (5) clarifying that limit applies to security “type” and recirculated draft rule with 10% limit and waiver intact for additional round of comment   |
| Industry stakeholders reiterate view that 10% limit should be eliminated or revised to allow an accredited investor exemption; industry stakeholders and JCARR member requests additional state-level data on product complaints; no additional consumer stakeholder views submitted in this round | <b>DRAFT #7 (APRIL 3, 2024)</b><br>Division revised 10% concentration limit policy by adding an exemption for accredited investors who have significant tolerance for risk of loss and illiquidity; Division provided additional specific state data to justify its 10% state limit   |
| Only one industry stakeholder provided comment on last revision, applauding inclusion of an accredited investor exemption but questioning the qualifying language and also critiquing the BIA.   | <b>DRAFT #8 (DECEMBER 6, 2024)</b><br>Division removed the qualifying language used in the accredited investor exemption and removed  |

|  |   |
|--|---|
|  | the waiver form initially proposed. BIA also updated.   |
| The Division only received a handful of comments on the December 2024 revisions so the Division extended the comment period and convened a stakeholder meeting on February 27, 2025 to elicit further comment. During the stakeholder meeting, the Division agreed to revise the BIA to clarify that it is proposing a clean accredited investor exemption to its concentration limit policy. In an effort to reach a final compromise with key industry stakeholders, the Division also agreed to revise the rule proposal to eliminate the affiliate restriction currently enforced as part of the concentration limit policy. | <b>DRAFT #9 (MARCH 13, 2025)</b><br>Division removed the affiliate restriction from the concentration limit policy to be codified in the rule text. BIA also updated to reflect revisions requested during the stakeholder meeting. |

As highlighted in summation above, the key point of contention in this rulemaking initiative has revolved around the Division's 10% concentration limit. Consumer stakeholders support the safeguard, but industry stakeholders oppose it and have requested an accredited investor exemption and removal of the affiliate restriction as a compromise approach. To move this package forward, the Division is willing to proceed with the accredited investor exemption and remove the affiliate restriction.

#### **11. What scientific data was used to develop the rule or the measurable outcomes of the rule? How does this data support the regulation being proposed?**

The Division has expended considerable resources to research and develop the rule and to measure and assess likely outcomes on Ohio business and investors. The Division previously produced a comprehensive companion rulemaking memo citing numerous scientific and authoritative sources, which the Division incorporates by reference here. The data included links to over 13,000 pages of prospectus material; rules and guidance statements from peer regulators, including the SEC, FINRA, and state securities regulators; academic studies; industry reports (including multiple reports from stakeholders); media articles highlighting the real-people risks of these products; and comment letters that espouse both industry and consumer viewpoints. The Division is supplementing that discussion with the chart below, which organizes scientific data by category and explains (in parentheses) how each piece of data supports the proposed regulation.

| <b>Federal Rules, Guidance, Reports</b>   |
|---|
| <ul style="list-style-type: none"> <li>SEC Commissioner Hester Peirce, <i>Capital On-Ramps: Remarks at the SEC's 42nd Annual Small Business Forum – Exploring the Early-Stage Landscape: Trends and Strategies in Capital Raising</i> (Apr. 24, 2023) (SEC Commissioner recommended consideration of concentration limit as potential method of expanding investor access to private markets – aligns with Ohio policy approach in the regulation that expands investor access to alternative products);</li> </ul> |

- SEC Commissioner Mark Uyeda, *Remarks at the “Going Public in the 2020s” Conference: Columbia Law School/Business School Program in the Law and Economics of Capital Markets* (Mar. 3, 2023) (SEC Commissioner recommended consideration of concentration limit as potential method of expanding investor access to private markets – aligns with Ohio policy approach in regulation that expands investor access to alternative products);
- SEC Filing Review Process, <https://www.sec.gov/divisions/corpfin/cffilingreview> (disclosing up to 3-year gaps in federal review of registered entities, evidencing need for state level review);
- SEC Industry Guides, *Securities Act Industry Guide No. 5, Preparation of Registration Statements Relating to Interests in Real Estate Limited Partnerships*, SEC Publication 2056 (5-08) (1976) (federal advertising restrictions applicable to non-traded REITs – aligns with advertising component of proposed rule);
- SEC Investor Bulletin: *Non-Traded REITs* (Aug. 31, 2015) (warning investors about risks associated with lifecycle REITs);
- SEC Office of Compliance, Inspections, and Examinations, *2021 Examination Priorities Report* (Mar. 3, 2021) (identifying non-traded REITs and BDCs as complex, risky, illiquid product subject to heightened regulatory scrutiny, after shift to NAV products);
- *CF Disclosure Guidance: Topic No. 3, Staff Observations in the Review of Promotional and Sales Material Submitted to Securities Act Industry Guide 5* (Dec. 19, 2011) (describing advertising issues observed in the non-traded REIT industry);
- *CF Disclosure Guidance: Topic No. 6, Staff Observations Regarding Disclosures of Non-traded Real Estate Investment Trusts* (Jul. 16, 2013); (describing advertising issues observed in the non-traded REIT industry);
- *Compliance & Disclosure Interpretations: Non-GAAP Financial Measures*, (Dec. 13, 2022) (describing advertising issues observed in the non-traded REIT industry);
- *Study Regarding Financial Literacy Among Investors, as Required by Section 917 of the Dodd-Frank Wall Street Reform and Consumer Protection Act* (Aug. 2012) (documenting low levels of financial literacy and sophistication in retail investor market).

#### **FINRA Rules, Guidance, Reports**

- *2021 Report on FINRA’s Examination and Risk Monitoring Program* (Feb. 1, 2021) (identifying non-traded REITs as product requiring heightened regulatory scrutiny after NAV reforms);
- *2022 Report on FINRA’s Examination and Risk Monitoring Program* (Feb. 2022) (identifying non-traded REITs as product requiring heightened regulatory scrutiny after NAV reforms);

- *2023 Industry Snapshot (2023)* (providing state-by-state registration data used to analyze complaint data);
- [2025 FINRA Annual Regulatory Oversight Report](#) at 39 (January 2025) (finding breach of the best interest duty of care where firm recommends complex or risky products that result in concentrations “comprising a sizable portion of a retail customer’s liquid net worth or securities holdings in a manner that is inconsistent with the retail customer’s risk tolerance or investment objectives”) (having previously defined non-traded REITs and BDCs as examples of complex and risky products).
- *Dispute Resolution Statistics; FINRA Reminds Members of Their Sales Practice Obligations for Complex Products and Options and Solicits Comment on Effective Practices and Rule Enhancements*, FINRA Reg. Notice 22-08 (May 2022) (identifying non-traded REITs and BDCs as complex products requiring heightened regulatory scrutiny after NAV reforms);
- *Investor Insights: Concentrate on Concentration Risk* (June 15, 2022) (warning investors to avoid overconcentration of non-traded REITs after NAV reforms);
- *Report on 2018 Examination Findings* (December 2018) (identifying non-traded REITs as product requiring heightened regulatory scrutiny after NAV reforms).

#### **State Rules, Guidance, Reports**

- *NASAA Regulation Best Interest Implementation Committee: National Examination Initiative Phase I Report* (Sept. 20, 2020) (identifying non-traded REITs as product requiring heightened regulatory scrutiny after NAV reforms);
- *NASAA Request for Public Comment: Proposed Revisions to NASAA Statement of Policy Regarding Real Estate Investment Trusts* (Jul. 12, 2022) (proposing national 10% concentration limit for non-traded REITs – noting the existence of concentration limits in 20 U.S. jurisdictions and proposing limits nationally);
- *California Standards Relating to Advertisements*, California Corporate Code, Cal. Code Regs. Tit. 10, § 260.302 (current through Register 2023 Notice Reg. No. 18, May 5, 2023) (state advertising rule that has similar anti-fraud restrictions as proposed in regulation);
- *Idaho Rules Pursuant to the Uniform Securities Act*, Idaho Admin. Code § 12.01.08.047 (state advertising rule that has similar anti-fraud restrictions as proposed in regulation);
- *Kansas Administrative Regulations*, Office of the Securities Commissioner, Kansas Admin. Regs. § 81-10-1 (state advertising rule that has similar anti-fraud restrictions as proposed in regulation);
- *Nebraska Securities Act*, Neb. Title 48, Ch. 6, § 26 (state advertising rule that has similar anti-fraud restrictions as proposed in regulation);
- *North Carolina Securities Rules*, 18 N.C. 06A .1308 (state advertising rule that has similar anti-fraud restrictions as proposed in regulation);
- *Tennessee Securities Act rules*, Tenn. Comp. R. & Regs. 0780-04-02-.04 (state advertising rule that has similar anti-fraud restrictions as proposed in regulation);



- West Virginia Securities Act rules, West Virginia 32-1-01 through 32-4-403 (state advertising rule that has similar anti-fraud restrictions as proposed in regulation).

#### **Academic Publications, Research, Reports**

- Benjamin P. Edwards, *Conflicts and Capital Allocation*, Ohio State Law Journal (June 2017) (research indicating that non-traded REITs and other products with significant sales compensation (conflicts) steer capital to less productive uses, harming overall economy);
- Cerulli Report – *U.S. High-Net-Worth and Ultra-High-Net-Worth Markets 2022: Shifts in Alternative Allocations* (Jan. 17, 2023) (data indicating the increased targeting of retail investors in the sale of alternative products);
- Craig McCann and Regina Meng, *Blackstone’s Choice: Let BREIT Crash or Collapse It Slowly*, SLCG Blog (Dec. 2022) (critiquing valuation and performance of NAV REITs);
- Craig McCann and Regina Meng, *Blackstone fiddles as BREIT burns* (Apr. 17, 2023) (critiquing valuation and performance of NAV REITs);
- Fredric Dodard and Amy Le, *Total Global Market Portfolio*, State Street Global Advisors White Paper at 8 (Feb. 2022) (data pegging global market portfolio at \$179 trillion in 2021, illustrating the small market presence (<0.1%) of non-traded REIT and BDC products that collectively managed around \$150 billion in assets around that time – data puts economic impacts in proper context);
- Joshua Mallett and Craig McCann, *Further on the Returns to Non-Traded REITs*, The Journal of Wealth Management, 24 (3) 113-127 (Winter 2021) (research on performance of non-traded REITs, including NAV products);
- Lauren M. Cunningham and Jacob Leidner, *The SEC Filing Review Process: A Survey and Future Research Opportunities*, Contemporary Accounting Research, vol. 39 no. 3 (Fall 2022) (reviewing SEC comment letters to document decreased transparency and frequency – federal gap evidences need for state oversight);
- Neil Bhutta et al., Board of Governors of the Federal Reserve System, *Changes in U.S. Family Finances from 2016 to 2019: Evidence from the Survey of Consumer Finances*, Federal Reserve Bulletin, vol. 106, no. 5 (September 2020) (data indicating retail investor net worth is concentrated in retirement assets – justifies regulation as protection for older and retired Ohio investors);
- SLCG Economic Consulting, *Broker Disclosure Download*, <https://www.slcg.com/resources/brokerdisclosure/> (reproducing the raw dataset of all broker disclosures on CRD/IARD system from the year 2000 to the present in sortable Excel format).

#### **Industry Publications, Research, Reports**

- *Asset Allocation*, CFA Institute (2023 Curriculum) (recommending an investing time horizon of at least fifteen years for illiquid investments);

- Barry Ritholtz, *Your Co-Investors in BREIT*, The Big Picture (Dec. 12, 2022) (highlighting downside of increasing retail allocations in illiquid alternative products – evidences benefit of retail limit found in regulation);
- Chilton REIT Strategy, *Arbitrage Opportunity Available in Public REITs* (Apr. 2023) (noting issues with NAV REIT valuations – highlights product risk and rebuts claimed economic benefits of non-traded REITs);
- Christopher Stambaugh et al., *What are NAV REITs? Answers to Some Frequently Asked Questions*, DLA Piper (May 8, 2022) (explaining key differences between non-traded and listed REITs –informational background);
- Cohen & Steers, *What We Believe Investors Should Know About Non-traded REIT Redemptions* (Dec. 2022) (noting shift away from private real estate and price lagging);
- Connor Nechodom et al., *SEC Comment Letter Update: Highlights of Trends in the 2022 SEC Comment Letters to Real Estate Investment Trusts*, Troutman Pepper Hamilton Sanders LLP (Mar. 20, 2023) (noting SEC scrutiny of non-GAAP performance figures – aligns with proposed regulation);
- Dane Bowler, *Beware Blackstone Real Estate Funds – Public REITs Are Better*, Seeking Alpha (July 28, 2022) (questioning NAV valuations of non-traded REITs – highlights valuation risk that is mitigated by proposed regulation);
- Dane Bowler, *Blackstone’s Withdrawals Are a Symptom of Public/Private NAV Discrepancy*, Seeking Alpha (Dec. 9, 2022) (questioning NAV valuations of non-traded REITs);
- David Auerbach, *Analysis of BREIT*, Hedgeye TV (Dec. 12, 2022) (analyzing redemption data of large non-traded REIT – demonstrating illiquidity of NAV vehicles);
- David H. Roberts et al., *Goodwin Alerts: The Past, Present and Future of the Non-traded REIT Structure* (Jan. 23, 2020) (summary of product evolution in non-traded REIT product – informational background);
- David Kathman, *Real Estate Funds, Private REITs, and BREIT: What You Need to Know*, Morning Star (Jan. 18, 2023) (market research on cost differences between listed and non-traded REIT products – highlights cost risk (eroded returns) for retail investors that is mitigated by regulation);
- Guy Barnard et al., *Private v. listed property pricing disconnect signals opportunity: The global property equities team questions and examines the dispersion in returns between private and public real estate, which strengthens the case for listed property*, Janus Henderson Investors (Oct. 11, 2022) (questioning valuations of private real estate sponsors);
- Hamilton Lane, *Private Markets: A Guide for High-Net-Worth Investors* (Jul. 2021) (discussing illiquidity risk of various alternative products – evidences benefit of retail limit);
- Howard Marks, *What Really Matters?*, Oaktree Capital Management Memo to Clients (Nov. 22, 2022) (noting valuation questions circling NAV REITs);

- Institute for Portfolio Alternatives, *Practice Guide 2018-01, Per Share Investment Performance Measurement & Reporting for Publicly Registered Non-listed REITs* (Apr. 16, 2018) (affirming illiquidity risk of non-traded REITs, including NAV REITs as having “indeterminate holding periods”);
- Institute for Portfolio Alternatives, *Investing in Non-traded REITs* (2013) (calling out illiquidity as “primary risk” of non-traded REITs and recommending heightened suitability restrictions, including limiting “total allocation of illiquid investments to a reasonable percentage”);
- IPA /Stanger Monitor (Winter 2023) (touting NAV REIT performance based on lagged pricing);
- Jack Rodgers, *Blackstone REIT Keeps Bleeding Despite Infusion of Liquidity*, Globest.com (Mar. 2, 2023) (noting redemptions in large NAV REIT);
- John Henley et al., *An Analysis of 2021 and 2022 SEC Comments Issued to REITs*, Morrison Foerster (Mar. 9, 2023) (confirming SEC comments in only 13 non-traded REIT filings over course of two-year period of 2021-2022 – evidences federal gap in review of non-traded REITs);
- John O. Newell et al., *REITs Should Review Disclosure of Non-GAAP Financial Measures Based on New SEC Staff Guidance*, Goodwin Procter Alert (Dec. 22, 2022) (discussing heightened SEC interest in use of non-GAAP financial figures consistent with state interest in proposed regulation);
- John Quinn and Ryan Friel, *The Sale of High Commission Products Under Regulation Best Interest*, Aon Advisor Solutions Newsletter, Vol. 3 (Fall 2020) (predicting heightened regulatory scrutiny of non-traded REITs and other high commission products after Reg BI);
- Laurence B. Siegel, *Alternatives for the Masses?* AJO Vista (Feb. 6, 2023) (rejecting claim that retail investors should increase their allocations to alternative investments);
- Matt Krantz, *Chasing Right Stocks to Buy Is Critical with Fewer Choices but Big Winners*, Investors.com, (Nov. 27, 2020) (noting increase in complaints involving equity stocks – comparative data point for non-traded REIT and BDC complaints);
- McKinsey, *Private Markets Turn Down the Volume*, Global Private Markets Review at 37 (2023) (monitoring shift away from private markets due to illiquidity risk);
- Motley Fool, *Blackstone Inc. (BX) Q3 2022 Earnings call Transcript* (Oct. 20, 2022) (repeating sponsor’s stated success in avoiding redemption gates just a few weeks before the sponsor initiated largest REIT asset pro-rata in REIT history);
- Nareit, *REIT Industry Monthly Data* (April 2023) (data indicating the availability of \$3.6 trillion in listed real estate funds – rebuts claim that Ohio investors have limited investment options);

- Nareit, *REITs by the Numbers* (Q4 2022) (recommending total REIT portfolio allocations between 5-15% - evidencing workability of 10% concentration limit proposed in regulation);
- Or Skolnik et al., *Why Private Equity is Targeting Individual Investors*. Global Private Equity Report 2023, Bain & Co. (2023) (comprehensive report explaining why private equity is targeting retail investors);
- *Pathways to Raising Capital: Brokers, Finders, and Solicitors*, IPA Direct Insights Webinar Series (Mar. 25, 2021) (confirmation by industry leader that virtually all non-traded REIT recommendations are solicited – rebuts “investor choice” argument and related industry claim that investors desire higher concentrations);
- Phil Bak, *Liquidity Risk*, Substack (Jan. 11, 2023) (highlighting illiquidity risk of large NAV REIT);
- Sean Peche, *REIT Ruin*, Ranmore Global Equity Fund (Apr. 10, 2023) (highlighting valuation discrepancies in NAV REITs);
- SIFMA, *2023 Capital Markets Factbook* (July 2023) (comprehensive dataset highlighting key statistics in U.S. and global capital markets, confirming total global market size of \$231 trillion (\$101 trillion in equity markets, \$130 trillion in fixed income) as well as state-by-state registration statistics – puts industry’s claim of adverse economic impact into proper perspective as non-traded REITs and BDCs collectively represent less than 0.1% of investable assets available to Ohio investors);
- SIFMA, *US Corporate Bonds Statistics* (May 3, 2023) (data indicating there are \$10.3 trillion worth of corporate bonds in the U.S. market – provides market comparison for non-traded BDC market at \$45 billion (less than 1% of public bond market) – puts industry’s claim of adverse economic impact into proper context);
- Simon Lack, *Is BREIT Marked to Market?*, SL Advisors (Dec. 11, 2022) (questioning valuation of large NAV REIT – evidences ongoing valuation risk);
- Stephen Beck et al., *Alternative Investments and Their Roles in Multi-asset Class Portfolios*, Fidelity Institutional Insights (2022) (categorizing private real estate and private credit as the most illiquid products on the liquidity spectrum of the alternative asset class);
- *The Trouble in Conflating Illiquidity and Stability: If You Want Any Degree of Return, Volatility Is Inescapable*. Fisher Investments Editorial Board Staff, (Dec. 2, 2022) (explaining valuation risk of non-traded products and rebutting volatility claims of non-traded products as illusory);
- Travis Hoiom, *Why REITs Aren’t Immune to a Market Crash*, The Motley Fool (Apr. 1, 2020) (explaining how REITs can drive up commercial rent to the detriment of small businesses);
- UMB Fund Services and Fuse Research Network, *State of the Market: Non-traded REITs and BDCs* (July 2022) (comprehensive report with market data on non-traded REITs and BDCs – provides context for claimed economic impact of regulation).

## Media Articles

- Andrew Bary, *Blackstone Just Limited Withdrawals from Its Huge Retail Real Estate Fund*, Barron's (Dec. 1, 2022) (noting redemption outflows and illiquidity in large NAV REIT);
- Andrew Bary, *Blackstone's BREIT Lagged Public REITs in January. What to Know*, Barron's (Feb. 17, 2023) (noting performance challenges at large NAV REIT – evidences valuation and pricing risk of non-traded REITs);
- Andrew Bary, *Blackstone's Giant Real Estate Fund Boasts a Strong Run. But Can History Repeat?*, Barron's, (Aug. 5, 2022) (raising questions regarding valuation and performance of large NAV REIT);
- Andrew Bary, *The Lesson of Blackstone's Retail Real Estate Fund: Liquidity Matters*, Barron's (Dec. 10, 2022) (highlighting illiquidity risk of large NAV REIT);
- Alexander Graham, *BREIT's Blues*, St. Louis News (Dec. 2, 2022) (highlighting illiquidity risk of large NAV REIT);
- Alexander Graham, *BREITing Bad*, St. Louis News (Dec. 2, 2022) (highlighting illiquidity risk of large NAV REIT);
- Antoine Gara and Sujeet Indap, *How the Gates Closed on Blackstone's Runaway Real Estate Vehicle*, Financial Times (Dec. 5, 2022) (highlighting illiquidity risk of large NAV REIT);
- Arleen Jacobius & Arein Arvedlund, *Redemptions Curbed from Non-traded REITs: Blackstone, Other Alternatives Firms Pursued Retail Investors – and Now Are Rationing Exits*, Pension & Investments (Apr. 17, 2023) (highlighting illiquidity risk of alternative products);
- Ben Shepardson, *Commercial Real Estate Making Waves as Investors Look for Calmer Waters*, Realty Biz News (Dec. 19, 2022) (highlighting illiquidity risk of large NAV REIT);
- Beth Mattison-Teig, *Redemption Requests Raise Eyebrows for Non-Traded REITs*, Wealth Management (Jan. 30, 2023) (highlighting illiquidity risk of large NAV REIT);
- *Blackstone Marks Down Value of Investment Portfolio as Management Fees Increase*, Private Equity Wire (Oct. 10, 2022) (highlights valuation and conflict risks of non-traded REITs);
- *Blackstone REIT Redemptions Soar While Equity Raise Stumbles*, DI Wire (Nov. 28, 2022) (highlighting illiquidity risk of large NAV REIT);
- *Blackstone's Real Estate Shopping Spree Is Now a Mortgage Default Crisis*, Better Dwelling (Mar. 16, 2023) (highlighting systemic impacts of large NAV REIT investing in commercial real estate market);
- Brad Thomas, *This Could be Texas Toast for United Development Funding*, Forbes (Dec. 11, 2015) (real-time coverage of investor harm flowing from billion-dollar non-traded REIT);
- Brett Arends, *Why I Don't Have Blackstone BREIT Envy*, Market Watch (Jan. 5, 2023) (critiquing performance claims of non-traded REIT);



- Bruce Kelly, *Advisor Group Latest B-D Network to Halt Sales of Real Estate Products*, Investment News (Apr. 17, 2020) (real-time coverage of REIT pro-ration and suspension during pandemic);
- Bruce Kelly, *Cetera Cuts REIT Sales, Loses Senior Recruiter*, Investment News (Apr. 24, 2020) (real-time coverage of REIT pro-ration and suspension during pandemic);
- Bruce Kelly, *DOL Fiduciary Rule Could Hurt Nontraded REIT Sales: LPL's Cassidy*, Investment News (Apr. 30, 2015) (explaining potential impact of Reg BI on non-traded REIT sales);
- Bruce Kelly, *Is the New Generation of Nontraded REITs Really Any Better Than the Last?*, Investment News (Jan. 23, 2023) (questioning proclaimed benefits of NAV REIT reforms);
- Bruce Kelly, *Nontraded REIT Chickens Come Home to Roost at Wirehouses, RIAs*, Investment News (Dec. 9, 2022) (highlighting illiquidity risk of large NAV REIT);
- Bruce Kelly, *Nontraded REIT Math Is Still Bedeviling*, Investment News (Dec. 12, 2022) (highlighting illiquidity risk of large NAV REIT);
- Carol Ryan, *Blackstone's Property Bets Are Getting Shakier: Rent Growth Is Slowing for Residential Real Estate, Which Makes Up Over Half of the Private-Equity Giant's Portfolio*, Wall Street Journal (Dec. 5, 2022) (highlighting correlation between rent increases and REIT profitability);
- Chibuikwe Oguh, *Blackstone Limits REIT Investor Redemptions Again in April*, Reuters (May 1, 2023) (highlighting illiquidity risk of large NAV REIT);
- Chibuikwe Oguh, *Blackstone's Earnings Fall 16% On Sharp Drop in Asset Sales*, Reuters (Oct. 20, 2022) (real-time reporting of challenges in large NAV REIT);
- Chibuikwe Oguh, *Factbox: Redemption Wave Hits Private REITs Among Valuation Jitters*, Reuters (Jan. 24, 2023) (highlighting illiquidity and valuation risks of large NAV REIT);
- Chibuikwe Oguh and Herbert Lash, *Blackstone's \$69 Bln REIT Curbs Redemptions in Blow to Property Empire*, Reuters (Dec. 1, 2022) (highlighting illiquidity risk of large NAV REIT);
- Chris Farrell, *Yale Investment Legend's Advice for Ordinary Investors Is Good as Gold*, Star Tribune (May 15, 2021) (opinion article discouraging use of endowment model that promotes higher allocations of alts by retail investors);
- Chris Gasparino, *Private Equity Crackup Looming Amid Higher Interest Rates and Escalating Losses: Losses Mount in REITs Owned by Blackstone, the Carlyle Group, and Apollo*, Fox Business News (Apr. 21, 2023) (noting "Hotel California" dynamic and illiquidity risk of private equity investments);
- Dan DeFrancesco, *Blackstone Is Betting Big on Lending Out Money in the Private Markets, and the PE giant Has \$182 billion To Do It*, Business Insider (Oct. 21, 2022) (noting discrepancy in private credit versus listed credit valuations);



- David J. Lynch, *Financial Risks Grow in Shadowy Corner of Markets, Worrying Washington: This Time, the Big Banks Aren't the Problem*, Washington Post (Dec. 19, 2022) (explaining how NAV REIT pro-rata can cause industry bank run and larger systemic risk);
- Dawn Lim, *Blackstone's Profit Falters as Rising Rates Chill Deal making*, Bloomberg (Oct. 20, 2022) (highlighting diversification risk of real estate investments);
- Dawn Lim and John Gittelsohn, *Blackstone's \$70 Billion Real Estate Fund for Retail Investors is Losing Steam*, Bloomberg (Nov. 2, 2022) (noting how private equity performance is contingent on maintaining asset management fees);
- Eleanor Laise, *Retirees, Don't Get Stranded Hunting Returns*, Kiplinger, (Dec. 13, 2019) (reporting adverse experiences of retirees who invested in non-traded REITs);
- Evan Hudson, *In the Beginning Was the REIT*, Bloomberg Tax Insight (Dec. 10, 2019) (placing first public sales of non-traded REITs in 1990s – informational background);
- FINRA News Release, *FINRA Fines Wells Investment Securities \$300,000 for Use of Misleading Marketing Materials for REIT Offering* (Nov. 22, 2011) (reporting of sanction against broker-dealer for misleading advertising);
- FINRA News Release, *FINRA Sanctions David Lerner Associates \$14 million for Unfair Practices in Sale of Apple REIT Ten and for Charging Excessive Markups on Municipal Bonds and CMOs* (Oct. 22, 2012) (reporting of sanction against broker-deal firm for fraud in sale of non-traded REITs);
- Hannah Lang, *Analysis: Social-Media Driven Bank Runs Burden Regulators with a Bigger Problem*, Reuters (Mar. 22, 2023) (noting the increased potential for bank run financial panics as the result of social media);
- James Mackintosh, *Blackstone's BREIT Highlights Looming Dangers of Private Funds: In a World Increasingly Demanding Liquidity, Blackstone Is Selling Illiquidity*, Wall Street Journal (Dec. 13, 2022) (highlighting illiquidity risk of large NAV REIT);
- Janet Levaux, *Ex-CFO at Schorsch-Related REIT Arrested*, ThinkAdvisor (Sept. 8, 2016) (reporting on criminal investigation of CFO at large non-traded REIT);
- Jasmin Suknunan, *145 million Americans Own REITs: 12 Things to Know About These Stocks That Make Owning Real Estate Easy*, CNBC.COM, (Dec. 2, 2021) (highlighting illiquidity of products);
- Jason Zweig, *Yale Invests This Way. Should You? Yale University's Endowment Has Earned Spectacular Returns in Hedge Funds, Private Equity and Other "Alternative Assets." Investors Hoping to Mimic the School Need to Understand What Has Made It Successful*, Wall Street Journal: Intelligent Investor (Mar. 10, 2023) (warning retail investors of the risk of the endowment model of investing);
- Jason Zweig, *You Bought a Hot Fund. Now It's on Ice: Investors Who Piled into an Unconventional Blackstone Real Estate Fund Now Can't Get More Than a*

*Sliver of Their Money Out*, Wall Street Journal (Dec. 9, 2022) (highlighting illiquidity risk of large NAV REIT);

- John Stepek, *The Truth About Alternative Assets*, Bloomberg (Dec. 7, 2022) (critiquing valuation of illiquid alternative products);
- John Wilde, *On the Radar: Non-GAAP Financial Measures and Metrics*, Wall Street Journal (Dec. 7, 2021) (critiquing use of non-GAAP financial figures by non-traded REITs);
- Jonathon Guilford, *Blackstone Gets a Slap from Efficient Markets*, Reuters (Dec. 8, 2022) (highlighting illiquidity risk of large NAV REIT);
- Jonathan Kandell, *Ares Faces Its Biggest Decision Yet: Stick with Private Credit or Become an Alts Supermarket*, Institutional Investor (Mar. 16, 2023) (noting banks have been placed in a competitive disadvantage to private credit);
- Joy Wiltermuth, *It's a 'Safe Bet' to Expect Pain in Private Real Estate Funds*, MarketWatch (Jan. 23, 2023) (predicting that lagged valuations in private equity will result in product blowups);
- Kirsten Grind and Jean Eaglesham, *A \$2.5 Billion Business-Development-Corporation Fund Hits Redemption Limit: Volatile markets have prompted rush of investors to exit nontraded business development companies*, Wall Street Journal (Apr. 10, 2020) (real-time reporting of gating by non-traded BDCs during the pandemic);
- Konrad Putzier, *Rising Interest Rates Threaten to Expose Office Buildings' Inflated Values*, Wall Street Journal (Oct. 31, 2022) (highlighting valuation risk in commercial real estate market);
- Leah Nylen and Dawn Lim, *Private Equity Firms Probed by US on Overlapping Board Seats*, Bloomberg (Oct. 28, 2022) (reporting of DOJ investigation involving private equity firms' conflicts);
- Leslie Shaver, *Blackstone Says It Won't Force Asset Sales from BREIT: News That the Firm Was Limiting Withdrawals from Its \$69 Billion Real Estate Income Trust Has Led to Speculation Among Multifamily Watchers*, Multifamily Dive (Dec. 14, 2022) (reporting on potential systemic risk to residential real estate market arising from gating by large NAV REIT);
- Mark Maurer, *SEC Expected to Raise More Questions About How Firms Calculate Non-GAAP Measures*, Wall Street Journal (Feb. 28, 2023) (reporting heightened scrutiny of non-GAAP figures);
- Mark Niquette, *Wall Street Emerges as GOP's Villain Amid House Price Pinch*, Bloomberg News: Politics (Aug. 1, 2021) (highlighting potentially adverse impact of private equity investment in residential real estate market);
- Mark Schoeff, *Advisers Should Look to Alts to Attract High-Net-Worth Clients: But They Need to Be Aware of Stepped-Up Regulatory Scrutiny of Complex Products*, An Expert Tells Advisers at the Financial Planning Association Annual Conference, Investment News (Dec. 13, 2022) (reporting on heightened SEC scrutiny of alternative products);

- Michele Celarier *Short-seller Nate Koppikar Has Taken on Blackstone, Facebook, and the Tiger Cubs. He's Had an Amazing Year*, Institutional Investor (Feb. 27, 2023) (discussing valuation and performance issues in private markets);
- Molly Redden, *Private Equity May Be a Ticking Time Bomb for Public Pension Plans: It Won't Just Be People in the Private Equity Industry Who Suffer, Millions of Americans Who Hold a Public Pension Plan Could Be Squarely Within the Blast Radius*, Huffington Post (Apr. 4, 2023) (highlighting potentially adverse impact of private equity investment in real estate);
- *Non-traded REITs Limit Withdrawals Amid Investor Rush to Retrieve Cash: Smaller Investors Feeling the Financial Pressures from The Pandemic Are Finding It Increasingly Difficult to Redeem Shares*, The Real Deal (Apr. 15, 2020) (highlighting illiquidity risk of REITs during pandemic);
- *Non-traded REIT Redemptions Exceed 350% of Fundraising in February*, DI Wire (Mar. 28, 2023) (highlighting illiquidity risk of large NAV REIT);
- Peter Grant, *Commercial Property Funds for Small Investors Face Tougher Regulation*, Wall Street Journal (Aug 30, 2020) (highlighting illiquidity risk of non-traded REITs);
- Prarthana Prakash, *One of the World's Richest Men Knows Why Silicon Valley Bank Really Failed: 'People on iPhones,'* Forbes Finance (Mar. 30, 2023) (noting increased potential for bank run financial panics as the result of social media);
- Rich Hill, *Entry Points for Listed REITs Are Emerging*, Pension & Investments (Feb. 10, 2023) (explaining price lagging in private real estate investments);
- Robert Davis, *Blackstone Is Stepping Up Evictions of Hundreds of Tenants Across the US as a Top Exec Vows "Cash Flow Growth,"* Business Insider (Feb. 1, 2023) (highlighting potentially adverse impact of private equity investment in residential real estate market);
- Robin Wigglesworth, *Blackstone's Plan to Juice BREIT*, Financial Times (Dec. 7, 2022) (discussing valuation discrepancies between listed and non-traded real estate and reporting on sponsor's intention to increase rent and reinstitute evictions owned in portfolio);
- Robin Wigglesworth, *Inside Blackstone's 'Beloved' \$126bn Crown Jewel*, Financial Times (Oct. 21, 2022) (highlighting valuation issues at large non-traded REIT);
- Sam Chambers, *Blackstone's Rollercoaster Ride Goes Downhill as Markets Fall*, The Times, (Dec. 11, 2022) (highlighting illiquidity risk of large NAV REIT);
- SEC Litigation Release No. 24537, *Former REIT Manager and Executives to Settle SEC Charges for More Than \$60 Million* (Jul. 17, 2019) (reporting of sanctions against non-traded REIT executives at American Realty Capital for fraud);

- Shandel Menezes, *New Report Claims Blackstone Group Is Buying San Diego's Affordable Housing, Hiking Up Rent Prices*, (Mar. 25, 2023) (highlighting potentially adverse impact of private equity investment in residential real estate);
- Steven Kasovich, *The Red Flags at United Development Funding*, D Magazine, (Apr. 25, 2016) (noting concerns with large non-traded REIT);
- Tatyana Shumsky, *Accounting Choices Blur Profit Picture*, Wall Street Journal (June 28, 2016) (highlighting misleading use of non-GAAP financial figures);
- Tatyana Shumsky, *What Exactly are Non-GAAP Numbers? Well, That Depends*, Wall Street Journal (July 5, 2016) (explaining the misleading potential of non-GAAP financial figures);
- Telis Demos, *BREIT Flows Aren't the Be-All and End-All for Blackstone*, Wall Street Journal (Jan. 27, 2023) (highlighting conflicts arising from performance compensation and the importance of asset management fees to large private equity firms);
- *Three Questions: Blackstone's Investor Redemption Limits on REIT Explained*, Investment News (Dec. 2, 2022) (real-time Ohio advisor explanation of illiquidity risk in NAV REIT – evidences the direct Ohio benefits of concentration limits);
- U.S. Department of Justice, *Former Chief Financial Officer of American Realty Capital Partners Charged with Accounting Fraud*, (Sept. 8, 2016) (real-time reporting of criminal charges against executive at non-traded REIT);
- Wall Street Journal Editorial Board, *A Mistaken Reign on REITS: A Proposal Would Limit What Investors Can Put into Real Estate Trusts* (Oct. 10, 2022) (opinion piece claiming concentration limits are unnecessary due to NAV REIT reforms and improved liquidity shortly before NAV REITs trigger the largest lockup in REIT history).

### Prospectus Data

The Division also relied on Prospectus data that highlighted the need for regulation, as evidenced in these sample disclosures:

- “This investment involves a high degree of risk. You should purchase these securities only if you can afford the complete loss of your investment.”
- “There is no assurance we will pay distributions in any particular amount, if at all.”
- “The amount and source of distributions we may make to our stockholders is uncertain... As a result, we may not be able to make distributions to our stockholders at any time in the future, and the level of distributions we do make to our stockholders may not increase or even be maintained over time, any of which could materially and adversely affect the value of your investment.”
- “There is no public trading market for our common stock and repurchase of shares by us will likely be the only way to dispose of your shares.”

- “On a limited basis, you may be able to have your shares repurchased through our share repurchase plan, although we are not obligated to repurchase any shares and may choose to repurchase only some, or even none, of the shares that have been requested to be repurchased in any particular month in our discretion.”
- “An investment in our shares has limited or no liquidity and our share repurchase plan may be modified or suspended.”
- “We use the term ‘perpetual-life REIT’ to describe an investment vehicle of indefinite duration... In our perpetual-life structure, the investor may request that we repurchase their shares on a monthly basis, but we are not obligated to repurchase any shares and may choose to repurchase only some, or even none, of the shares that have been requested to be repurchased in any particular month in our discretion.”

#### **National (SEC and FINRA) Regulatory Actions Involving Non-traded REITs and BDCs**

- *Coastal Equities, Inc.*, [FINRA AWC No. 2019061213401](#) (Dec. 16, 2022) (imposing \$150,000 fine and partial restitution of \$268,800 for suitability and supervision violations arising from excessive concentrations in high-risk alternative investments);
- *Western International Securities, Inc.*, [FINRA AWC No. 2020067094001](#) (Oct. 31, 2022) (imposing \$400,000 fine and restitution of \$471,401.57, and undertaking for failing to report customer complaints and for suitability and supervision violations involving \$7.8 million in non-traded REIT sales to 59 customers, 19 of which were 60 or older) (REIT commissions accounted for 90% of broker pay);
- *National Securities Corporation*, [FINRA AWC No. 2019061652404](#) (June 23, 2022) (enforced state concentration limits and imposed \$3.6 million fine, \$4.7 million in disgorgements of commissions, and partial restitution of \$625,480 for suitability and supervision violations related to non-traded REITs and other alternative investments) (firm ended up paying \$17.7 million in restitution to 59 customers for the non-traded REIT violations) (see related complaint against broker Mark Sam Kolta, [FINRA Discip. Proc. No. 2018057297102](#));
- *Megurditch Patatian* (employed by Western International at time of violations), [FINRA Extended Hearing Panel Decision in FINRA No. 2018057235801](#), 2022 FINRA DISCIP. LEXIS 10 (June 10, 2022) (noting “[b]ecause non-traded REITs are complex and risky, several states limit how much a customer may invest in them;” ordering bar, restitution, and disgorgement totaling more than \$700,000 fine for suitability and supervision violations involving \$7.86 million in non-traded REIT sales to 59 customers. Customers included 20 elderly customers aged 65-91, many who retired from a California utility – California Water and Power);



- *Robert David, Jr.* (employed by Morgan Stanley at time of violation), [FINRA AWC No. 2019062180701](#) (April 7, 2022) (imposing \$15,000 fine and 20-month suspension for suitability/ concentration violations involving junk bonds – same risk profile as BDCs; also inflating customer financial figures to circumvent firm’s limit);
- *Dempsey Lord Smith, LLC*, [FINRA AWC No. 2019061213901](#) (March 21, 2022) (imposing \$70,000 fine and restitution of \$29,840 for suitability/ concentration and supervision violations involving alternative investment allocations exceeding 20% in accounts used for retirement purposes);
- *Christopher J. Passero* (employed by Money Concepts Capital Corp. at time of violation), [FINRA AWC No. 2020066345701](#) (April 11, 2022) (imposing \$10,000 fine and 3-month suspension for secretly paying \$249,560 in restitution and loans to customers to cover REIT losses suffered as the result of his recommendations);
- *StockCross Financial Services, Inc.*, [FINRA AWC No. 2018058595601](#) (July 14, 2021) (imposing \$250,000 fine and undertaking for independent consultant to remediate suitability/ concentration and supervision violations) (firm failed to detect abusive sales that caused almost \$800,000 in losses to two retired investors, 75 and 80 in age);
- *Kevin Marshall McCallum* (employed by LPL Financial at time of violation), [FINRA AWC No. 2019062569501](#) (June 17, 2021) (imposing \$25,000 fine, \$1.2 million in restitution, and disgorgement of \$14,231.61 in commissions for misleading advertising and projections regarding NAV and performance of non-traded BDCs as well as suitability/ concentration violations involving 12 customers, including four over the age of 60 and seven who invested with retirement funds) (\$1.2 million in realized investor losses with partial recovery provided by firm);
- *Mercer Hicks III* (employed with Southeast Investments N.C. at time of violations), [FINRA Extended Hearing Panel Decision in Discip. Proc. No. 2017052867301](#) (May 19, 2021) (touting state concentration limits as “useful guides to making a suitability determination” and imposing bar plus disgorgement of \$38,812.60 in commissions for suitability / concentration violations involving \$665,000 in sales of non-traded REITs and BDCs to six investors aged 73-88) (“issuers’ minimum suitability requirements put a ‘representative on notice that the issuer has flagged the product as, for example, risky, illiquid, or complex’ and a representative should take this into account”);
- *Independent Financial Group, LLC*, [FINRA AWC No. 2018059223401](#) (April 8, 2021) (enforcing state concentration limits and imposing \$200,000 fine and corrective supervisory measures for suitability and supervision violations involving hundreds of non-traded REIT transactions involving dozens of retired investors) (firm’s effort to monitor sales without formal concentration limits did



not work and firm ended up facing more than three dozen customer arbitrations between 2008 and 2016);

- *Gopi Krishna Vungarala* (employed with Purshe, Kaplan & Sterling Investments and Sutterfield Financial Group at the time of violation), [FINRA National Adjudicatory Council Decision in FINRA No. 2014042291901](#) (Oct. 2, 2018), (rep barred for suitability violations and ordered to disgorge over \$9.6 million in commissions from excessive REIT and BDC sales in sales to Native American tribe) (discipline sustained in [SEC Admin. Proc. File No. 3-18881](#) (November 20, 2020)) (over time, rep increased allocation from 5% to 10% and then to 22.8%; FINRA rejected assertion that tribe's status as an accredited investor inferred financial sophistication so as to justify sales);
- *Cynthia Diane Cowden* (employed with NPB Financial Group at time of violation), [FINRA AWC No. 2017055979301](#) (Oct. 21, 2020) (imposing bar for suitability/ concentration violations involving non-traded REIT allocations as high as 20% to three retired "senior customers"; accredited investor status did not justify sales in view of low annual income plus "high risk level far exceeded the couple's moderate risk tolerance");
- *Cabot Lodge Securities LLC*, [FINRA No. 2014041541401](#) (April 6, 2021) (enforcing state concentration limits and imposing \$270,000 fine for suitability violations as result of sales to 72 year-old security guard near retirement) ("A high concentration of investments in speculative securities is not suitable for investors with limited income, means, and investment experience. Non-traded REITs have particular risks, such as liquidity risk and cessation of distributions, that make them suitable for recommendation to only a very narrow band of investors capable of evaluating and being financially able to bear those risks.");
- *First Clearing, LLC* (now known as Wells Fargo Clearing), [FINRA AWC No. 2016051352401](#) (Nov. 4, 2020) (imposing \$300,000 fine for supervision and NASD Rule 2340 violations related to REIT valuations on account statements);
- *Kevin Barletta* (employed with LPL Financial at time of violation), [FINRA AWC No. 2017052828301](#) (Oct. 15, 2020) (enforcing firm's age-based concentration limit for REITs and imposing \$5,000 fine and 2-month suspension for suitability/ concentration violations) ("An unlisted REIT is a REIT where the trust's shares do not trade on a national securities exchange. For that reason, investments in unlisted REITs generally are illiquid and bear increased risk.");
- *Vereit, Inc.*, [SEC Cease and Desist Order in SEC File No. 3-19831](#), Order Pursuant to Section 8A of the Securities Act and Section 21C of the Securities Exchange Act (June 23, 2020) (imposing \$8 million civil penalty for financial reporting violations involving non-GAAP metrics whereby REIT overstated AFFO, an indicator of the ability to pay dividends) (related to *SEC v. AR Capital*, Case 1:19-cv-06603 (S.D.N.Y July 16, 2019));

- *Donald S. Woods* (employed with LPL Financial at time of violation), [FINRA AWC No. 2018058133301](#) (May 6, 2020) (imposing \$10,000 fine, 6-month suspension, and disgorgement of \$5,6000 in commissions for suitability/concentration violations involving three customers in late 60s to age 84 and for falsifying account documentation to circumvent firm's 10% limit on alternative investments);
- *Moloney Securities, Co., Inc.*, [FINRA AWC No. 2015046315102](#) (May 4, 2020) (imposing \$100,000 fine and restitution of \$15,574.13 for suitability and supervision violations involving sales of oil and gas partnerships – same risk profile - senior customers);
- *Craig M. Gould* (CEO of Cabot Lodge at time of violation), [FINRA AWC No. 2014041541402](#) (Jan. 2, 2020) (imposing \$20,000 fine and 90-day suspension for supervision violations whereby firm accepted organization and offering expense and underwriting compensation for REIT offering in excess of FINRA prescribed limits);
- *Howard Davis* (employed at Cabot Lodge at time of violation), [FINRA AWC No. 2014041541403](#) (Jan 23, 2020) (imposing \$10,000 fine for suitability and supervision violations whereby firm accepted organization and offering expense and underwriting compensation for REIT offering in excess of FINRA prescribed limits);
- *SEC v. Suneet Singal*, [No. 19-cv-11452 \(S.D.N.Y. Jul. 13, 2021\)](#) (broker employed at First Capital Real Estate Investments at time of violation) (ordering \$3.2 million in disgorgement and \$676,400 in interest and 10-year bar for fraudulent reporting of REIT and BDC financials);
- *NY LIFE Securities LLC*, [FINRA AWC No. 2016050685102](#) (Nov. 20, 2019) (imposing \$250,000 fine, restitution of \$76,643.47, rescission to 28 customers for suitability and supervision violations involving overconcentration in higher-risk mutual funds, leading to losses totaling \$1.4 million);
- *Alexander L. Martin*, [FINRA AWC No. 2016049789602](#) (June 8, 2018) (imposing \$10,000 fine and 20-day suspension for supervision violations involving unsuitable sales of illiquid alternative investments);

#### **State Regulatory Actions Involving Non-traded REITs and BDCs**

- *In re Ameriprise*, 2018 S. Car. LEXIS 16 (June 28, 2108) (broker-dealer fined \$650,000 for failure to supervise brokers who altered firm customer suitability forms to support non-traded REIT sales, mostly to retirees, and falsely marked sales as “unsolicited”);
- *In re Brady*, 2020 Mo. Sec. LEXIS 34, \*9 (April 24, 2020) (sanctioning dual agent for unsuitable non-traded REIT sales with elderly client, earning more than \$135,000 in commissions in one-year period);

- *In re David Lerner Associates, Inc.*, 2017 N.J. Sec. LEXIS 12 (May 22, 2017) (\$700,000 monetary penalty plus \$100,000 in costs against firm for systemic suitability and recordkeeping violations involving \$4 billion in sales of three Apple REITs, products that paid 7.5% in selling commissions and 2.5% in marketing expense allowance);
- *In re Hill*, 2012 Ark. Sec. LEXIS 14 (Jul. 18, 2018) (unsuitable recommendation and disclosure violations involving recommendation of \$100,000 investment in private REIT for a \$7,250 commission);
- *In re Infinex*, 2018 Mass. Sec. LEXIS 14 (Jul. 18, 2018) (ordering \$125,000 fine and restitution for investors sold unsuitable non-traded REITs and variable annuities based on agent incentives to earn substantial commissions);
- *In re Investment Professionals, Inc.*, 2017 Mass Sec. LEXIS 2 (Mar. 22, 2017) (ordering restitution and an independent consultant review of non-traded REIT sales to senior investors following unsuitable and excessive sales);
- *In re Jim Poe & Assocs.*, 2020 Tex. Sec. LEXIS 43 (June 15, 2020) (sanctioned for failure to supervise and allowing representative to overconcentrate clients in non-traded REITs, executing almost \$ 4,000,000 in non-traded REITs);
- *In re Johnson*, 2021 Maine Sec. LEXIS 7 (Apr. 21, 2021) (fined representative \$5,000 and issued a 30-day suspension for disregarding risks disclosed in prospectus; relying instead on information sponsors provided that misrepresented non-traded REITs as having “minimal risk”; also, overconcentrating investors in products);
- *In re Kulch*, 2020 Mass. Sec. LEXIS 1 (July 16, 2020) (representative sanctioned for over-concentrating his customers, including elderly, in illiquid, risky, and high commission products such as non-traded REITs and variable annuities, earning over a million in commissions on those two products during five-year period);
- *In re McCallum*, 2024 Ala. Sec. LEXIS 14 (May 17, 2024) (barring broker for recommending 17% to 60% concentrations in “high-risk and highly speculative publicly-traded BDC” to 12 customers that had low to moderate risk tolerances, 7 of which invested with retirement funds and 4 of which were over the age of 60, to generate commissions of \$37,492.78 to firm LPL and \$14,231.61 to broker; investors realized more than \$1 million in investment losses);
- *In re Mitra*, 2020 Fla. Sec. LEXIS 966 (February 6, 2020) (permanently barring broker for fraud and misrepresentations involving the illiquid nature of non-traded REITs);
- *In re Money Concepts*, 2017 Oh. Sec. LEXIS 22 (Jul. 27, 2017) (ordering restitution for unsuitable and excessive sales of non-traded REITs);
- *In re NEXT Fin.*, 2019 Mass. Sec. LEXIS 19 (Dec. 20, 2019) (sanctioning firm for failing to supervise rep who made hundreds of unsuitable non-traded REIT sales to collect large commissions; ordered rescission and fine);

- *In re Savage*, 2018 Oh. Sec. LEXIS 19 (June 29, 2018) (sanctioned for numerous incidents, including engaging in more than 50 unapproved transactions totaling approximately \$4 million in high-commission product, including oil and gas interests, private placements, and non-traded real estate investment trusts);
- *In re SII Investments*, 2018 Mass. Sec. LEXIS 20 (Sept. 7, 2018) (firm fined \$50,000 and ordered to pay restitution for overconcentrating clients in non-traded REITs);
- *In re Steadfast Income REIT*, 2013 Oh. Sec. LEXIS 26 (June 28, 2013) (cease and desist order against non-traded REIT sponsor for pricing manipulation);
- *In re Sutherland*, 2017 Oh. Sec. LEXIS 17 (Jul. 17, 2017) (suspension of agent and investment adviser representative license for suitability and excessive concentration violations involving sales of non-traded REITs to 18 different investors);
- *In re TFS Secs., Inc.*, 2021 N.J. Sec. LEXIS 22 (Oct. 19, 2021) (fined firm \$75,000 for books and records violations and supervisory lapses regarding sales of non-traded REITs and BDCs – missing, incomplete, and inaccurate suitability forms);

#### **Recent Customer Arbitrations and Settlements**

On the customer complaint front, the Division analyzed national-level customer complaint data in years 2019-2022. The data showed REITs and BDCs generating over 1,800 formal arbitration complaints in that period. The Division also re-produced analysis that it performed when it was first approached about rulemaking. That analysis showed REITs and BDCs producing a disproportionately large number of customer complaints, when compared to other product types in the market.

- *Centaurus Financial, Inc.*, [FINRA Arbitration Award No. 21-01782](#) (October 19, 2022) (awarding customer \$510,000 in damages for unsuitable sales of REITs and UITs);
- *Dinosaur Financial Group, LLC*, [FINRA Arbitration Award No. 21-02081](#) (October 04, 2022) (awarding customer \$314,564 in compensatory damages and \$103,807 in punitive damages for unsuitable REIT sales);
- *First Allied Securities, Inc.*, [FINRA Arbitration Award No. 18-01349](#) (March 11, 2022) (awarding \$1.9 million in compensatory damages and \$700,500 in costs and attorneys' fees for unsuitable REIT sales);
- *Chang v. Presidential Brokerage, Inc.*, FINRA No. 21-01528 (California) (72-year-old retiree) (invested \$3 million in non-traded REITs and BDCs, unsuitable concentrations and liquidity hardship);
- *Colvin v. National Securities Corp.*, FINRA No. 20-04187 (New York) (71-year-old retiree) (invested \$4.3 million in non-traded REITs, unsuitable concentrations and liquidity hardship);

- *Yang v. Cetera Investments Services*, FINRA No. 21-01611 (California) (lost entire 401k, unsuitable concentrations and liquidity hardship);
- *Lin v. Cetera Investments Services*, FINRA No. 21-01611 (California) (lost entire 401k, unsuitable concentrations and liquidity hardship);
- *Chang, v. Centaurus Financial Inc.*, FINRA No. 21-01846 (California) (retired 76 and 85-year olds, unsuitable concentrations and liquidity hardship)
- *Dickau v. VSR Financial Services, Inc.*, FINRA No. 21-00003 (Nebraska) (72-year-old retired ranchers) (\$7.5 million in sales of alternative investments, including multiple non-traded REITs, in retirement account, unsuitable concentrations and liquidity hardship).
- *Krings v. VSR Financial Services, Inc.*, FINRA No. 20-03783 (Nebraska) (retired couple aged 62 and 66, husband ran the family farm and wife worked as housewife and then special ed teacher) (more than \$1 million in sales of alternative investments, including multiple non-traded REITs, in retirement account, unsuitable concentrations and liquidity hardship);
- *Detert v. Concorde Investment Services, LLC*, FINRA No. 20-03895 (Arizona) (retired couple aged 76 and 77, worked as grocery store butcher and check processor) (approximately \$860,000 invested in alternative investments, unsuitable concentrations and liquidity hardship);
- *Rudes v. David Lerner Associates, Inc.*, FINRA No. 21-01087 (Florida) (retired couple aged 71 and 72) (more than \$1 million in sales of alternative investments, including non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Boesen v. Questar Capital Corporation*, FINRA No. 21-00865 (Nevada) (couple in late 50s who lost the proceeds from selling a business) (approximately \$1.5 million in sales of in alternative investments, including non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Dehler v. First Allied Securities, Inc.*, FINRA No. 21-01512 (California) (retired couple aged 62 and 66, worked in IT and healthcare) (approximately \$740,000 invested in non-traded REITs);
- *Yu v. Independent Financial Group, LLC and LPL Financial, LLC*, FINRA No. 21-01963 (California) (retired 95-year-old who invested in his 80s) (approximately \$1.5 million invested in non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Pankow v. Centaurus Financial Inc.*, FINRA No. 21-01791 (California) (divorced and retired in late 60s looking for “safe” investment) (approximately \$250,000 invested in non-traded REITs, unsuitable concentrations and liquidity hardship);



- *Blackwood v. Berthel, Fisher & Company Financial Services, Inc.* (Indiana) (settled prior to filing) (invested in 50s near retirement with conservative risk profile) (\$420,000 invested in alternative investments, including non-traded REITs, lost over \$100,000, unsuitable concentrations and liquidity hardship);
- *Pacis v. Uhlmann Price Securities, LLC*, FINRA No. 21-00760 (Illinois) (retired couple aged 84 and 88) (\$570,000 invested in non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Alvey v. Center Street Securities, Inc.*, FINRA No. 22-00118 (Kentucky) (retired, late 60s) (\$434,000 invested in non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Donigian v. Advisory Group Equity Services Ltd.*, FINRA No. 21-00881 (New Hampshire) (81-year-old who retired from construction business) (approximately \$2.5 million invested in private placements and Non-Traded REITs, unsuitable concentrations and liquidity hardship);
- *Hardy v. Cetera Advisor Networks LLC*, FINRA No. 21-01700 (California) (couple aged 59 and 62 near retirement) (approximately \$655,000 invested in non-Traded REIT and BDCs, unsuitable concentrations and liquidity hardship);
- *Turkeltaub v. National Securities Corp.*, FINRA No. 20-03844 (New York) (74-year-old who retired from career with City Department of Child Welfare) (\$819,037 invested in non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Bonesteel v. D.H. Hill Securities, LLP*, FINRA No. 20-03844 (Texas) (retired widower aged 73 with conservative risk tolerance) (\$285,000 in non-traded REITs, unsuitable concentrations and liquidity hardship);
- *Martinez v. Triad Advisors LLC*, FINRA No. 21-01652 (Nevada) (retired product manager from AT&T, aged 72) (approximately \$179,000 invested in non-traded REITs, unsuitable concentrations and liquidity hardship).

More recently, the Division supplemented the national-level complaint data with complaint data containing state identifiers, pulled from CRD/IARD as described more fully above. This data confirms that Ohio has a lower rate and incidence of complaint with the policy subject to codification than comparable states that lack the policy.

The Division produced Ohio-specific examples of investor hardship. In relation to REIT lockups that started in December of 2022, the Division shared that two REIT sponsors froze millions of shares held by Ohio investors and rejected more than \$20 million in Ohio cash-out requests. The Division also highlighted exam data indicating the most Ohioans who invest in these products are of advanced age (80% are 55+; 45% are 65+).



Other salient scientific or authoritative facts that the Division has produced include:

- The proposed regulation gives effect to code provisions that gave the Division merit authority over a century ago. The Division's merit authority been upheld by both the Ohio Supreme Court and the United States Supreme Court as a lawful exercise of state police power. *In re Columbus Skyline Secs.*, 74 Ohio St. 3d 495, 499 (1996); *Hall v. Geiger-Jones*, 242 U. S. 539 (1917).
- The Division is not an outlier in regulating these products. Most if not all states apply NASAA REIT guidelines and all merit states apply merit guidelines. The advertising guidelines included in this proposal are modeled directly after other federal and state rules.
- Close to half of the states (20) have enforced concentration limits in some form for these products. Those states are Alabama, California, Idaho, Iowa, Kansas, Kentucky, Maine, Massachusetts, Missouri, Nebraska, New Jersey, New Mexico, North Dakota, Ohio, Oregon, Pennsylvania, Puerto Rico, Tennessee, Texas, and Vermont.
- The Division is not the most restrictive regulator of these products. Even without the proposed accredited investor exemption, Ohio purchasers were able invest up to 20% of their liquid net worth in these products (10% in a non-traded REIT and another 10% in a non-affiliated BDC). 85% of selling firms have internal limits that are equally or more restrictive than Ohio's limit. There are other states that are more restrictive than Ohio and cap investments in both products to 10%.
- The 10% limit was originally adopted as a pro-capital formation policy to create a registration path for alternative products in Ohio. Stakeholders have used the policy to raise billions of dollars of capital from tens of thousands of Ohio investors.
- The 10% limit is consistent with a 2013 industry "white paper" that actively promoted liquid net worth and income limits as tools that "broker-dealers and financial advisors should consider in analyzing these products as investment opportunities." In that paper, the stakeholder recommended that non-traded REITs only be sold to investors with:
  - "Sufficient liquid net worth to more than cover foreseeable and some unforeseeable liquidity needs for the holding period of the REIT after making the allocation to this and other direct investments;"
  - "A level of income high enough that the investor is not likely to need the investment principal during the holding period of the non-traded REIT;"

- “A total portfolio that is well diversified across asset types and sectors to decrease overall liquidity risk if part of the portfolio does need to be liquidated to fulfill an extraordinary cash need;”
  - “Sufficient cash reserves so that, if the investor sustains loss of income from employment or other unexpected liquidity needs, he or she can cover the shortfall without needing to sell any investment assets for a short period of time.”
- To help mitigate illiquidity risk, the stakeholder specifically urged its members to “limit total allocation to illiquid investments to a reasonable percentage that does not render the portfolio largely illiquid, prevent the investor from making reallocation decisions, or limit him or her from taking advantage of unique market opportunities in other sectors...”
  - The data indicates compliance costs are minimal in relation to the amount of capital raised. Non-traded REIT and BDC issuers report spending less than 0.1% of their offering proceeds on Blue Sky registration – which is the aggregated cost for all U.S. jurisdictions.
  - The data illustrates how the policies have helped the Division screen out fraudulent deals that other regulators, including the SEC, have failed to either review or intercept. Example: United Development Funding case – billion-dollar REIT program that harmed investors in other states; four executives currently sentenced to 20 years in federal prison last year for their misconduct.
  - Academic and industry research strongly support investor safeguards.
  - Recent comment letters from AARP, PIABA, Consumer Federation, Better Markets, arbitration clinics, and other consumer protection groups support strengthening, not removing or relaxing, state regulation.

**12. What alternative regulations (or specific provisions within the regulation) did the Agency consider, and why did it determine that these alternatives were not appropriate? If none, why didn't the Agency consider regulatory alternatives? *Alternative regulations may include performance-based regulations, which define the required outcome, but do not dictate the process the regulated stakeholders must use to comply.***

The Division has considered the rules and policy approaches of other state and federal securities regulators. The Division's rule and policy approaches are similar to those of other merit states (i.e., states that incorporate anti-fraud merit guidelines in their statutory codes and rules). Indeed, this rulemaking effort was initiated to formalize the Division's adherence to the NASAA Statement of Policy involving Real Estate

Investment Trusts, a 2007 policy statement developed by a coalition of states securities administrators and applied by most if not all states.

Most commenters did not take issue with the revisions proposed in the regulation, save the Division's 10% concentration limit policy. The Division considered a variety of alternative approaches to codify the 10% concentration limit, as well as codifying an exemption process applicable to that limit. Those options and the Division's reasons for determining they are not appropriate are discussed below.

### **Alternative Option A – Eliminate 10% Limit**

The Division considered eliminating the concentration limit entirely, as recommended by a few industry stakeholders, but did not do so for several reasons. First, the Division reviewed regulatory actions and customer complaints involving these products and observed, time and time again, investors being harmed when they invested more than 10% of their liquid net worth in illiquid products.

Second, at least 19 other states have imposed the 10% limit as a safeguard to protect their investors. The Division did not want to roll back common-sense safeguards that most merit states offer.

Third, consumer protection groups across the country, including AARP, have urged states to strengthen, not relax, state regulation over these products because of investor harm.

Fourth and finally, the Division believes it is fundamentally unfair for any product sponsor to give itself the unilateral right to hold onto Ohio investor assets perpetually without any investor right to returns or ability to exit the investment. The only way for the Division to register a product with those lop-sided terms is to mitigate the potential for investor harm. That potential was mitigated long ago by including a 10% limit in the prospectus. Investors have never complained about the limit. The arrangement has worked well for thirty years and the Division has no data that would justify tossing out that time-tested policy entirely.

### **Alternative Option B – Modified or Qualified Accredited Investor Exemptions**

The Division considered adopting modified and qualified accredited investor exemptions. The modification first proposed in 2023 was to adjust the net worth standards – to either the qualified client standard (a \$5 million standard) or a compromise version of an accredited investor exemption whereby financial thresholds are adjusted for inflation (recommending a \$3 million standard). According to the recent SEC Accredited Investor Report: "If the natural person accredited investor thresholds were adjusted to reflect inflation since their initial adoption through 2022 using CPI-U, the net worth threshold would increase from \$1 million to \$3,037,840, the individual income threshold would increase from \$200,000 to \$607,568, and the joint income threshold would increase from \$300,000 to \$911,352." The Division discussed this

approach with stakeholders at an in-person meeting but did not adopt them. The Division accepted stakeholder feedback that \$5 million was too “high” and \$3 million would be too “new.”

A second qualified exemption was proposed last year that would exempt accredited investors that have “significant tolerance for illiquidity and risk of loss” from the concentration limit restriction. The Division only received feedback from one stakeholder on this approach, with the stakeholder questioning the language and expressing a preference for a clean accredited investor exemption without qualifying language. The current draft of the rule adopts the clean exemption approach.

### **Alternative Option C – 10% Aggregate Limit for All Non-traded REITs and BDCs**

The Division considered adopting a more restrictive 10% policy, as recommended by a large group of national consumer advocacy organizations. At least two merit states restrict non-traded REIT and BDC purchases to no more than 10% in the aggregate, whereas the Division allows a max 20% in the aggregate (10% in REITs and 10% in BDCs). See “Suitability” Section of Prospectuses. The Division did not adopt a more restrictive policy because there is a low incidence of Ohio investor complaint at the current level.

### **Alternative Option D – Principles-Based Limit**

The Division considered adopting a 5-pronged, principles-based limit, using the language recommended in a whitepaper published by the stakeholder leading this rulemaking effort:

Ohio purchasers may not invest in this product unless they: (a) have a sufficient liquid net worth to more than cover foreseeable and some unforeseeable liquidity needs after making the allocation to this and other direct investments; (b) have a level of income high enough that they are unlikely to need the investment principal during the anticipated holding period of 7-10 years; (c) have a total portfolio that is well diversified across asset types and sectors to decrease overall liquidity risk if part of their portfolios needs to be liquidated to fulfill an extraordinary cash need; (d) have sufficient cash reserves so that they can cover shortfalls occasioned by loss of income from employment or other unexpected liquidity needs without having to liquidate this investment; and (e) limit total allocation to illiquid investments to a reasonable percentage that does not render their portfolios largely illiquid, prevent them from making reallocation decisions, or limit them from taking advantage of unique market opportunities in other sectors.

Although the Division agrees with those recommendations, the Division did not incorporate them into its approach because the text is lengthy, complex, and unlikely to curb investor complaint.

### **Alternative Option E – Eliminate 10% Limit and State Review in Deference to SEC**

Lastly, one stakeholder suggested that the Division eliminate state review entirely and simply “rely on federal regulators.” As explained above, the Division cannot abdicate its statutory authority to conduct a merit review of offerings registered by qualification or coordination. It would not be prudent for the Division to do so in any event where, due to resource constraints or simply different rigors of review, federal regulators have cleared harmful REITs that the Division has screened out. The SEC discloses it can go as long as three years without reviewing a company’s filings and industry reports indicate that the SEC only issued comments on 13 non-traded REITs in all of 2021 and 2022.

#### **13. What measures did the Agency take to ensure that this regulation does not duplicate an existing Ohio regulation?**

JCARR directed the Division to codify registration policies that are not already spelled out in the Ohio Securities Act or associated securities rules and regulations. The Division reviewed those state securities laws and regulations to confirm that the proposed regulation gives effect to and aligns with those code provisions, without specifically duplicating them. The Division also conducted a digital word-search of the Ohio Revised Code and the Ohio Administrative Code through the Lexis-Nexis legal database to verify there was no duplication.

#### **14. Please describe the Agency’s plan for implementation of the regulation, including any measures to ensure that the regulation is applied consistently and predictably for the regulated community.**

With the exception of the new accredited investor exemption and removal of the affiliate restriction from the Division’s concentration limit policy, the policies presented for codification in this rule proposal are currently enforced by the Division and have been in effect for many years. Unless and until these policies are revised in a future rulemaking overseen by JCARR, the Division commits that it will apply the policies and statements and guidelines that are codified in rule. On a filing-by-filing basis, the Division will continue to assist filers and counsel with compliance as it has always done.

The only changes that the Division proposes to existing registration policies are the addition of the accredited investor exemption that Ohio purchasers may use to exceed the 10% limit and removal of the affiliate restriction. An issuer can demonstrate compliance by striking the text “, our affiliates,” that previously appeared after the word “us” below and by adding the bolded text to its existing prospectus disclosure:

*Purchasers residing in Ohio may not invest more than 10% of their liquid net worth in us and other non-traded real estate investment programs.<sup>18</sup> For purposes of Ohio's suitability standard, "liquid net worth" is defined as that portion of net worth (total assets exclusive of home, home furnishings, and automobiles minus total liabilities) that is comprised of cash, cash equivalents, and readily marketable securities. The condition does not apply, directly or indirectly, to federally covered securities. **The condition also does not apply to purchasers who meet the definition of an accredited investor as defined in rule 501(a) of Regulation D under the Securities Act of 1933, 15 U.S.C.A. 77a, as amended.***

Industry stakeholders assert that this accredited investor exemption will reduce and streamline the regulatory requirement.

Pursuant to industry stakeholder request, the Division will permit product sponsors to remove the Ohio affiliate restriction from product prospectuses now and will also make the accredited investor exemption available to Ohio purchasers immediately with the intention of formally codifying these accommodations into rule (as proposed) if they are approved by CSI and JCARR. As with all other product terms, Ohio purchasers can find the exemption in the product prospectuses. It is important to note that selling firms remain subject to suitability, best interest, and fiduciary obligations. FINRA and the SEC have made it clear that suitability, best interest, and fiduciary obligations are *not* waivable.<sup>19</sup> This is true no matter what kind of exemption Ohio adopts for accredited investors.

### **Adverse Impact to Business**

- 15. Provide a summary of the estimated cost of compliance with the rule(s). Specifically, please do the following:**
- a. Identify the scope of the impacted business community, and**

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<sup>18</sup> For non-traded BDCs, the Division would state "non-traded business development companies" in the place of "non-traded real estate investment programs."

<sup>19</sup> See, e.g., *In re Vungarala*, FINRA No. 2014042291901, 2017 FINRA Discip. LEXIS 44 (Oct. 25, 2017) (discipline sustained in SEC Admin. Proc. File No. 3-18881) (Nov. 20, 2020) (rejecting assertion that the Tribe's status as an "accredited investor" inferred financial sophistication); *In re Escarcega*, FINRA NAC, Complaint No. 2012034936005 (Jul. 20, 2017) ("Merely disclosing to a customer the risks of a particular investment, however, does not satisfy a registered representative's requirements under FINRA's suitability rules."); *In re Stonegate Partners LLC*, 2008 FINRA Discip. 26 (May 15, 2008) ("a determination that a customer is an accredited investor ... is not equivalent to a determination that the particular investment is suitable for that customer"); *In re Stein*, 56 S.E.C. 108,117 (2003) ("Even in cases in which a customer affirmatively seeks to engage in highly speculative or otherwise aggressive trading, a representative is under a duty to refrain from making recommendations that are incompatible with the customer's financial profile"); *In re Chase*, 56 S.E.C. 149, 156-57 (2003) ("We have repeatedly found that high concentration of investments in one or a limited number of securities is not suitable for investors," and that the suitability obligation cannot be satisfied through disclosure of risk, investor "must be able to understand and take the risk"); *In re Pinchas*, 54 S.E.C. 331, 342 (1999) (stating that "even if the customer wanted to 'double her money,' a registered representative is not relieved of his suitability obligations"); *In re Venters*, 51 S.E.C. 292, 294-95 (1993) (notwithstanding client's interest in investing in speculative securities, broker had duty to refrain from recommending such investments when he learned about his customer's age and financial situation); *In re Reynolds*, 50 S.E.C. 805, 809 (1992) (representative was obligated to abstain from making recommendations that were inconsistent with the customer's financial situation" even if the customer agreed with the recommendation).



The rule is directed to companies (issuers) seeking to raise capital from Ohio investors through a registration by qualification or registration by coordination. Companies selling securities that are registered by qualification or coordination (selling firms) are secondarily impacted by this rule as are Ohio purchasers, some of whom are natural persons while others are business entities. There may also be incidental business impacts to people and business entities that have business dealings with issuers that register their securities through this rule.

**b. Quantify and identify the nature of all adverse impact (e.g., fees, fines, employer time for compliance, etc.).**

***The adverse impact can be quantified in terms of dollars, hours to comply, or other factors; and may be estimated for the entire regulated population or for a representative business. Please include the source for your information/estimated impact.***

The proposed regulation should have no material adverse impact on issuers – the policies were adopted by the Division and implemented by regulated entities long ago. The business impact should be positive from the industry perspective because the accredited investor exemption for the 10% concentration limit policy has the potential to increase the sales that regulated entities can generate in Ohio.

The proposed regulation does not impose criminal or civil penalties. The Division does not have statutory authority to independently impose criminal fines or assess civil penalties against regulated persons or entities for paperwork or other violations of the Ohio Securities Act. The Division may refuse to register an offering under R.C. 1707.09 and R.C. 1707.091 (or suspend an offering under R.C. 1707.13) where an offering is grossly unfair or would tend to deceive and defraud Ohio investors. The proposed regulation does not (and cannot) change the statutory standard. The policies being presented for codification have resulted in a very low rate of registration refusals (less than 3%).

The only adverse impact that regulated persons or entities will encounter as the result of this regulation are minor compliance costs. Because non-traded REIT and BDC issuers raise funds nationally through a coordinated registration statement and common offering documents filed in all states, they can defray their expenses and raise substantial amounts of capital with minimal cost. As noted in the both the initial and supplemental BIA accompanying the initial proposal, issuers devote far less than 0.1% of their offering proceeds to Blue Sky expenses, which is the cost to comply with the registration requirements of all states. This data is sourced directly from the issuers themselves, as they are required to state their regulatory compliance costs and all material operating expenses in SEC financial reports. Ohio is just one of the 53 states and jurisdictions contributing to that expense, so Ohio expense is less.

The only modification that the Division is proposing to existing policy that will create a new issuer expense is the codification of the 10% concentration limit policy and associated exemption. See Division's Response to BIA Question 14. The Division is

recommending changes in the language used in the product prospectuses. Issuers typically make an initial filing in Ohio and then apply for renewals. As a result, subsequent offering documents would need to adjust a few sentences to a document that would have already been prepared. For issuers, this would require word-processing changes that issuer counsel can complete in less than five minutes. If stakeholders are correct and there is significant unmet Ohio investor demand to increase allocations to these products, the benefits to this 10% policy change will far exceed the cost of implementation.

The revisions that are proposed in this rule package should not have a harmful impact on selling firms because any requirements that might impact them were implemented long ago and are now relaxed with the proposed exemption for accredited investors and removal of the affiliate restriction. Most firms operate in all states and have already factored NASAA Statements of Policy, state merit guidelines, and advertising restrictions into their compliance systems. In examining whether these policies have a material adverse impact on selling firms, the Division reviewed financial statements for a representative sample of publicly held selling firms, which are also reported to the SEC. As was the case with issuers, the Division found no selling firms reporting compliance with or implementation of state Blue Sky requirements as a material operating expense. The Division likewise found no selling firms reporting or mentioning any expenses related to Ohio's registration laws or policies in their financial statements, annual reports, or websites.

The Division did not find compliance with existing Ohio registration requirements and policy statements (the crux of this rule proposal) mentioned or separately disclosed as a material expense on a standalone basis by any issuer or selling firm. If the Division has overlooked any issuers or selling firms reporting Ohio requirements as a material expense, they are requested to produce a copy of the relevant reports in responsive comments.

The Division also examined the compliance policies of a representative sample of 50 selling firms that hold almost \$1 billion of these products for Ohio investors. The policies were produced in response to confidential exam requests. None of those firms built their policies, procedures, or compliance systems around Ohio's existing rules (or the rules of any individual state). The Division did not see any firms cite to specific Ohio laws or rules in their policy manuals. Rather, selling firms built their policies, procedures, and compliance systems around federal laws and rules, which are cited, and broadly referred to state laws and rules more broadly in the collective sense. The Division did not identify any selling firm policies that would require updating as the result of this Ohio regulation (and no stakeholders identified any examples in their comment letters either). While selling firms will likely share the new exemption with their accredited Ohio clients, which would likely involve some communication and agent training costs, those actions and costs are discretionary as they are not required by the regulation.

**16. Are there any proposed changes to the rules that will reduce a regulatory burden imposed on the business community? Please identify. (*Reductions in regulatory burden may include streamlining reporting processes, simplifying rules to improve readability, eliminating requirements, reducing compliance time or fees, or other related factors*).**

Yes. The proposed accredited investor exemption will eliminate the 10% concentration limit as a registration condition for eligible Ohio purchasers. Industry stakeholders were unified in their request for this accommodation. If adopted, the exemption would eliminate the regulatory restriction that currently exists for those clients. The Division has also proposed removal of the affiliate restriction from the concentration limit policy, which was also requested by industry stakeholders to reduce the potential for adverse business impact.

**17. Why did the Agency determine that the regulatory intent justifies the adverse impact to the regulated business community?**

The Division has balanced the critical objectives of the regulation with the costs of compliance by the regulated parties and determined those costs are justified. The regulation's objectives are to give effect to the merit standard found in 1707.09, which extends to 1707.091. The statutory provisions were enacted and are currently enforced to allow companies to raise capital through registrations by qualification and coordination on fair terms that do not tend to defraud or deceive Ohio investors. To achieve compliance, the Division must consider competing capital formation and investor protection interests.

The proposed regulation facilitates capital formation by letting companies know how the Division interprets statutory terms so they avoid compliance pitfalls that would frustrate their ability to sell their securities in this state. Most of the policies being codified in this regulation are facilitating guidelines, meaning they facilitate the registration process. With these guidelines in place, 97% of filings have been registered for sale in Ohio. This has allowed non-traded REIT and BDC sponsors to raise \$2 billion in capital from more than 30,000 Ohio investors.

The only restriction on capital formation that the Division currently has that has garnered significant stakeholder opposition in this rulemaking initiative was the Division's 10% concentration limit policy, used to mitigate distribution and redemptions restrictions in certain offerings. As explained above, the Division is proposing an exemption for accredited investors and removing the affiliate restriction, as requested by industry stakeholders. There is no filing fee or other cost associated with the exemption. The only thing that issuers need to do is adjust a few sentences of disclosure in their prospectus, alerting Ohioans that an exemption is available for accredited investors. The Division previously offered a waiver option that would have eliminated the concentration limit for all Ohio investors, but only a minority of stakeholders support that approach.

To facilitate investor protection, the regulation codifies longstanding investor safeguards to screen out grossly unfair and fraudulent terms before they are sold to Ohio investors. The federal regulator does not conduct a substantive review of all filings and, even when it does, it only reviews disclosures. Through merit review, Ohio has screened out REITs that the federal regulator approved that harmed investors in other states.

For issuers, the costs to comply with state registration requirements are low as explained in response to BIA Question 15. The Division has produced the specific Blue Sky expenses for all major programs and can re-produce upon request, confirming that compliance costs are not a material expense. Although the proposed rule only imposes registration conditions on issuers, the Division reviewed disclosures and financial statements of selling firms and found no firms attributing any material operational expense related to compliance with this rule or compliance with Ohio registration conditions imposed on issuers. Moreover, no stakeholder produced any data to support the claim that rule compliance is a material expense.

The Division believes the proposal is well-supported by the data and a reasonable way of balancing competing capital formation and investor protection interests in Ohio-registered offerings. The Division believes the regulation is a beneficial codification of Ohio merit guidelines and policy, as directed in JCARR's R.C. 101.352 recommendation.

### **Regulatory Flexibility**

#### **18. Does the regulation provide any exemptions or alternative means of compliance for small businesses? Please explain.**

The Ohio Securities Act and associated rules provide numerous registration exemptions that allow issuers to raise capital in the manner that works best for their company given the intended investor base. To provide an example, R.C. 1707.03(O) is widely utilized by small businesses and provides an exemption from registration if the "total number of [equity] purchasers in this state of all securities issued or sold by the issuer ... during the period of one year ... does not exceed ten." It also provides a non-self-executing exemption for private placements under R.C. 1707.03(Q). Non-traded REITs and BDCs are increasingly using these small business exemptions to raise capital as alternatives to a registration by coordination.

In addition, the proposed amendments explicitly formalize a mechanism for a good cause waiver, which is the mechanism currently used informally by the Division and filer counsel to negotiate terms and sales conditions that demonstrate compliance with Ohio's statutory registration standard. In practice, the Division has modified or waived the application of these provisions for certain small businesses over the years. Lastly, the Division is proposing an accredited investor exemption to its concentration limit policy, further relaxing the compliance obligation.

#### **19. How will the agency apply Ohio Revised Code section 119.14 (waiver of fines and penalties for paperwork violations and first-time offenders) into implementation of the regulation?**

The Division does not have statutory authority to impose fines or civil penalties for violating the relevant rule so there will be no fines or civil penalties for paperwork violations of these rules, as defined.

**20. What resources are available to assist small businesses with compliance of the regulation?**

The Division regularly responds to public inquiries from investors and/or issuers of all sizes and their counsel. Division forms provide instructions for filers. Generally, counsel is retained because of the inherent liabilities in securities offerings. In addition to the rules being readily available, the Division publishes a quarterly newsletter to discuss relevant issues.