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Blue Sky Law

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Introduction

Compliance with registration requirements of each state is time-consuming and expensive, enough so that in some instances it deters capital-raising efforts entirely. The legal avenues by which firms can raise capital but avoid state registration are thus critical to capital-raising efforts.

From their inception, states' blue sky laws attempted to clear the way for secondary trading and help facilitate certain small-business capital-raising efforts. But variations among state laws persisted, which resulted in recurrent, loud calls for preemption of these state regimes entirely. Beginning in 1996, the federal government and the U.S. Securities and Exchange Commission further and further displaced and preempted those state registration requirements. Today, if an offering qualifies for an exemption from federal registration efforts, it likely qualifies for an exemption under state law as well.

While the state securities registration requirements have been largely displaced by a patchwork of federal law, state blue sky laws are continuing to evolve special protections for society's most vulnerable members. For instance, as covered in prior updates to this treatise, the states like Indiana and Utah have begun to develop a system of rewards and protections for those who report potential securities law violations to state securities regulators. And the North American Securities Administrators Association proposed model legislation for additional states to follow suit. This update covers two new efforts by states to broaden the protective reach of the blue sky laws: a system of special incentives and protections under the securities laws for vulnerable investors, and special administrative funds to assist victims of securities fraud in obtaining restitution. As Chapter 8 of this update explains, the blue sky laws pay special attention to seniors and persons under states' protective services, and states are increasingly adopting "report and hold" legislation to protect these persons. Similarly, as Chapter 11 discusses, a handful of states, like Indiana, Kansas, and Vermont, have adopted legislation implementing special assistance funds for victims of securities fraud. Recently, the North American Securities Administrators Association put forth a legislative template other states can use to craft their own special assistance funds. These developments, and more, are discussed in this updated version of Blue Sky Law.

This update contains new and revised sections on federal and state treatment of M&A brokers (§ 8:35), special state regulation of proxy advisors (new § 8:170), special state regulation of the use of emerging technologies (new § 8:171), civil penalties (§ 11:78), manner and method of reporting for the purposes of whistleblower award eligibility (§ 11:88), the issue of retaliatory intent whistleblower protections (§ 11:94), and right to jury trial (new § 11:98).

In Memoriam

Joseph C. Long, the original author of the *Blue Sky Law* treatise, and co-author of *Securities Arbitration Desk Reference*, passed away on November 22, 2017 at the age of 78. He had a long and distinguished career as a professor, a state regulator, and a practitioner in the field of securities regulation. He earned his J.D. from the University of Missouri-Columbia in 1963 and his LLM from the University of Virginia in 1972. Professor Long was on the faculty of the University of Oklahoma Law School from 1970 to 2001. During his tenure in Oklahoma, Professor Long served as Assistant General Counsel and consultant to the Oklahoma Securities Commission. From 1980–1994, he also served as Special Counsel for the North American Securities Administrators Association, Inc., advising its committees, filing amicus briefs on its behalf, and providing its members with expert testimony on securities issues. Professor Long served as counsel or as a consultant in a number of private securities cases, and appeared as an expert witness on securities matters.

Professor Long was also a past president of the Public Investors Arbitration Bar Association (PIABA) and he regularly presented seminars and wrote articles about securities law. His friend, co-author, and fellow past president of PIABA, Seth Lipner, described “the Professor” as he was known within PIABA in the following way in the *PIABA Bar Journal* in 2014:

[Joe Long was] the Encyclopedia Britannica of securities law, but it is not just the knowledge he imparts when he talks. In any conversation you have with him, the exuberance, the love of the subject, and the need to make the world safer for investors bursts out. And every paragraph he utters ends with that big smile, his deep laugh, and a good moral to the story.

21 *PIABA Law Journal* 173 (2014).

We recognize and honor the Professor’s contributions to this treatise and to the legal profession.

Publisher’s Editorial Staff

About the Author

Joseph C. Long received his B.A. and J.D. degrees from the University of Missouri at Columbia. He also holds an L.L.M. from the University of Virginia. He spent his early teaching career at the University of South Dakota and Stetson College of Law. Since 1970 to 2001, he was a member of the law faculty at the University of Oklahoma. Since July 1, 2001, he has been a professor emeritus. He continues an active securities practice and serves as an expert witness in administrative, civil, and criminal cases, and arbitrations.

During his tenure in Oklahoma, Professor Long has served as Assistant General Counsel of and consultant to the Oklahoma Securities Commission. Since 1980 to 1994, he also served as Special Counsel for the North American Securities Administrators Association, Inc., advising its committees, filing amicus briefs on its behalf, and providing its members with expert testimony on securities issues.

He was the co-reporter for the early drafts of the Revised Uniform Securities Act (1985). He is also the author of numerous articles on blue sky and other securities topics in various legal journals. He has co-authored with Seth Lipner the West treatise, *Securities Arbitration Desk Reference* (SABREF database on Westlaw).

Michael J. Kaufman is one of the nation's leading experts in the areas of securities litigation and civil procedure. He is the Dean and Professor of Law at Santa Clara University School of Law. Prior to joining Santa Clara University, Dean Kaufman served as Dean and Professor of Law of Loyola University Chicago School of Law, where he teaches courses on securities litigation and civil procedure. He also served as Loyola University Chicago's Acting Provost and Chief Academic Officer, leading the University's academic vision and inclusive strategic planning process. While at Loyola, Dean Kaufman also founded the Loyola University of Chicago School of Law's Institute for Investor Protection. He has practiced securities litigation at Sachnoff & Weaver Ltd., and Reed Smith LLP, and is often called upon by state and federal regulators and private law firms to serve as a consulting or testifying expert. Dean Kaufman has published more than 50 books and countless articles in his areas of expertise. He also serves as a public arbitrator for securities matters and has acted as an expert consultant for the U.S. Securities & Exchange Commission, the Consumer Financial Protection Bureau, and the Illinois Attorney General's Office.

John M. Wunderlich is currently in-house litigation counsel with a U.S. Fortune-500 company. He was formerly a litigator in the Chicago office of Kirkland & Ellis LLP, where he worked on securities and shareholder litigation, antitrust matters, and qui tam lawsuits. John has coauthored Rule 10b-5 Private Securities-Fraud Litigation

(Thomson Reuters), a comprehensive practice guide for navigating securities-fraud litigation from the filing of the complaint to trial. He has also authored and coauthored many articles in the area of securities litigation, which have appeared in scholarly and peer-reviewed journals and that have been favorably cited by numerous federal courts. In addition, he has contributed to books on securities litigation and coauthored chapters on securities arbitration. He is a former adjunct professor of law for Loyola University Chicago School of Law and staff law clerk for the U.S. Court of Appeals for the Seventh Circuit.

Special Acknowledgment

The authors are extremely grateful to **A. Michael Hainsfurther** of the Dallas law firm of Munsch Hardt, for allowing them to incorporate Mr. Hainsfurther's excellent state-by-state summary of the Regulation D coordinating exemptions as Appendix F to this Treatise. This summary was originally a freestanding article published in the Southwestern Law Journal. Mr. Hainsfurther very graciously agreed to update the piece previously and allow its inclusion here. It has been an extremely welcome addition to the work, giving it an important dimension it would not otherwise have. This state-by-state summary should be of great practical significance to those readers attempting to cope with the ever-changing securities regulations of the various states in attempting to make a national private offering under Regulation D.

This volume evolved over a period of years. When Professor Joseph C. Long joined the Oklahoma faculty and first became interested in state securities (blue sky) law, he found that there was an appalling lack of scholarly work dealing with these laws. The only real treatise in the area, Loss and Cowett, *Blue Sky Law*, published in 1958, was out of print and could only be found in the rare book room of most libraries. At the same time, there was a definite renaissance in the interest in state securities laws. This developed in part as the result of an increased concern with securities regulation in general by the plaintiff's bar as an easy avenue for recovery. It was also due, in part, to the reemergence of state securities agencies through the efforts and financing of the North American Securities Administrators Association, Inc. that created a strong cohesive force that could share with the Securities and Exchange Commission the burden of regulating and policing the greatly expanding securities industry. In writing this treatise, the author faced a number of major problems, some of which are inherent in the nature of the subject matter. Since these problems dictate the scope and coverage of the book, brief mention of them here is appropriate. First, there is the breadth of the field. While authors writing about federal securities law have a manageable universe of federal securities acts to contend with, the blue sky law author has to deal with fifty-four different statutes. Each state, plus the District of Columbia, Puerto Rico, Guam and the U.S. Virgin Islands, has some form of state securities act. With the important exception of Appendix F, previously prepared by A. Michael Hainsfurther, dealing with the coordinating exemptions with Regulation D, this book does not attempt to show the variations between these statutes or to deal in depth with the law of any one state or jurisdiction. Instead, this book uses as its base the Uniform Securities Act, as adopted by the National Conference of Commissioners on Uniform State Laws in 1957. This Act is as close to a lingua franca as one will find in the state securities area. The Uniform Act has been adopted, in part or whole, in virtually

every U.S. jurisdiction. And even where not expressly adopted, the Uniform Act's influence is still felt in the remaining states like California and New York, have provisions similar to those found in the Uniform Act. As a result, cases, administrative decisions, and administrative opinion letters from one jurisdiction can often be of some help in predicting how the courts or securities agencies of other states will react. There should also be added a word of caution. Many states that have enacted the Uniform Act have made substantial changes in the Act. This is especially true in the last several decades as the Uniform Act ages and fails to cope with new emerging regulatory attitudes and problems. As a result, the reader should never assume that the law of a particular jurisdiction follows the Uniform Act. Cases decided under the law of one state cannot be applied to the statute of another state until the reader checks to see that the language of the two statutes is identical. The second major problem is how to approach the subject matter. There are two ways to deal with this: One is to deal largely with state-by-state variations among their respective securities acts, with limited analysis of the statutory language, in an attempt to answer questions of interpretation arising from that language. The author has chosen the second approach: Their interest has been focused on examining authorities that have interpreted the statutes, and has attempted to provide tentative answers to statutory interpretative problems that they know exist. Of course, they have not identified all the problems of interpretation that exist in the Uniform Act, and many of the tentative solutions will no doubt be rejected when the courts and administrative agencies have cause to deal with the issues. As this book is still in a period of evolution, the authors would greatly appreciate input and feedback from its users. They would like to hear about other interpretative problems, that have arisen and other possible solutions. In this way, future editions can be made more useful to those who deal with state securities regulation on both a regular and an irregular basis. The final problem deals with the mass of interpretative material which exists. At first glance, there appears to be little authority construing state Securities Acts. This is deceptive. It is true that there are few reported appellate decisions interpreting the Acts. As a result, greater emphasis must be placed on trial court and administrative decisions and opinions. A vast number of these decisions and opinions are presently rendered, and an even greater number have been decided in the past decades after the Securities have come into existence. The problem is that new opinions are not being adequately and completely reported. Many older opinions that are known to exist are not in readily accessible form and are not digested. The authors have a great deal of this material; some is cited in the present edition, and more will be cited in future editions. The authors, however, would solicit the user's help in two specific regards. First, they know that there are many appellate, trial, and administrative decisions that go completely unreported. The California and New York courts, as well as the federal courts, frequently do not publish their securities opinions or trial orders. The

SPECIAL ACKNOWLEDGMENT

authors would greatly appreciate copies of these decisions and rulings from lawyers involved and law firms that are familiar with them. Second, the authors have been looking for years for certain copies of the Stocks and Bonds Law Service. This publication by Commerce Clearing House was the forerunner of the present Blue Sky Law Reports. It began in 1928 and ran until 1946. From 1928 through 1936, a new edition was published every two years. One author of this treatise has located the 1928, 1930, and 1936 through 1946 versions of this reporter. The Library of Congress, Commerce Clearing House, and none of the major law libraries in the United States admit to having the 1932 or 1934 versions. These versions are known to have existed because materials from them are presently digested in the Blue Sky Law Reports. The authors believe that these volumes surely must still exist, probably in a forgotten corner of a major law firm office gathering dust. If a user discovers a copy of these services the authors would greatly appreciate a call or a letter.

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Table of Abbreviations

ADR	American Depositary Receipt
Board	Federal Reserve Board
CBOE	Chicago Board Options Exchange
CEA	Commodity Exchange Act
CFTC	Commodity Futures Trading Commission
COD	cash on delivery
Commission	Securities and Exchange Commission
DK	don't know
DTC	Depository Trust Company
DVP	delivery versus payment
ESOP	employee stock ownership plan
FINRA	Financial Industry Regulatory Authority
FRB	Federal Reserve Board
FRRS	Federal Reserve Regulatory Service
MSRB	Municipal Securities Rulemaking Board
NASD	National Association of Securities Dealers, Inc.
NCM	Nasdaq Capital Market (formerly Nasdaq SmallCap Market)
NMS	National Market System
NNM	Nasdaq National Market
NSMIA	National Securities Markets Improvement Act
NRSRO	nationally recognized statistical rating orga- nization
NSRO	nationally recognized statistical rating orga- nization
NYSE	New York Stock Exchange
OCC	Options Clearing Corporation
OTC	over the counter
SEC	Securities and Exchange Commission
SMA	special memorandum account
SRO	self-regulatory organization



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