

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of
The Registration Statement of
CROYLE COMPUTER SERVICES, INC.
2 West Northern Avenue
Phoenix, Arizona 85021
File No. 2-46544

FILED
MAY 31 1974
SECURITIES & EXCHANGE COMMISSION

INITIAL DECISION

May 31, 1974
Washington, D.C.

Sidney L. Feiler
Administrative Law Judge

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APPEARANCES: John C. Hughes, Esq., 750 Arizona Public Service
Building, 411 North Central Avenue, Phoenix,
Arizona 85004, for Croyle Computer Services, Inc.

David H. Belkin, Jonathan A. Pace and Merton B. Goldman, Esqs.,
for the Division of Enforcement.

BEFORE: Sidney L. Feiler, Administrative Law Judge

I. THE PROCEEDING

This proceeding was instituted by order of the Commission pursuant to Section 8(d) of the Securities Act of 1933, as amended, ("Securities Act"), to determine whether, as alleged by the Division of Enforcement, a registration statement filed with the Commission by Croyle Computer Services, Inc. ("Registrant"), includes untrue statements of material facts and omits to state material facts required to be stated therein or necessary to make the statements therein not misleading, as more specifically set forth in the Division's Statement of Matters annexed to the order. An additional issue to be determined is whether a stop order should be issued suspending the effectiveness of the aforementioned registration statement.^{1 /} The Registrant filed an answer denying the allegations set forth in the Statement of Matters and setting forth certain affirmative defenses.

Pursuant to notice a hearing was held in Washington, D.C. The parties were represented by counsel and full opportunity was afforded them to present evidence and to examine and cross-examine witnesses. Proposed Findings of Fact, Conclusions of Law and Supporting Briefs were filed on behalf of the parties.

On the basis of the entire record, including evaluation of the testimonial evidence presented,^{2 /} the undersigned makes the following:

^{1 /} Section 8(d) of the Securities Act provides, in pertinent part, that if it appears to the Commission at any time that a registration statement includes any untrue statement of a material fact or omits to state any material fact required to be stated therein or necessary to make the statement therein not misleading the Commission may, after notice and opportunity for hearing, issue a stop order suspending the effectiveness of the registration statement. When such statement has been amended in accordance with such stop order the Commission shall so declare and thereupon the stop order shall cease to be effective.

^{2 /} John C. Croyle, President of the Registrant, was the sole witness.

II. FINDINGS OF FACT AND LAW

A. The Registrant - Background of this Proceeding

On December 11, 1972 Croyle Computer Services, Inc., filed a Registration Statement on Form S-2 to the Securities Act covering an offering of 500,000 shares of its no-par value common stock at \$10.00 per share. The Registration Statement was amended on January 15, February 20 and April 26, 1973 and became effective by operation of law on May 15, 1973.^{3/}

After each filing a letter was sent by the Division of Corporation Finance to counsel for the Registrant stating that the filing was so materially deficient in preparation and content that no further examination would be undertaken.^{4/} In a letter dated January 11, 1973, after the statement was made that the filing was found to be materially deficient, it was further noted that a member of the staff had apprised counsel of certain deficiencies in the filing and had recommended that the registration statement be withdrawn. The letter reiterated that consideration be given to withdrawing or amending the filing (Div. Ex. 1).

After the amendment of January 15, 1973 was filed, a letter dated January 31, 1973 was sent to counsel for the Registrant stating that

^{3/} The Registration statement filed on April 26, 1973 invoked the language of Rule 473(b) under the Securities Act to begin the twenty day period at the end of which the registration statement would become effective pursuant to Section 8(a) of the Securities Act. Consequently, on May 15, 1973, the registration statement became effective by operation of law.

^{4/} When a supervisory staff official decides, after initial analysis, that the registration statement is so poorly prepared or otherwise presents serious problems, review will be deferred since no further staff time would be justified in view of other staff responsibilities. (Securities Act Release No. 5231, Page 1, February 3, 1972).

after review the Division took the position that the filing was still materially deficient and requesting that consideration be given to the making of an application for withdrawal of the registration statement (Div. Ex. 2). A letter to the same effect was sent by the Division counsel to the Registrant on April 6, 1973 after the amendment of February 20, 1973 was filed (Div. Ex. 3).

After the amendment of April 26, 1973 was filed, a further letter was sent to counsel for the Registrant by the Division of Corporation Finance in which it was stated ". . . except for certain minor revisions and updating of financial statements the information contained therein (in the registration statement) is approximately the same as that contained in the amendment filed on February 20, 1973." The Division adhered to its position that the registration, as amended, was still materially deficient even though certain changes had been made after certain comments had been given by telephone on December 20, 1972 and January 30, 1973 (Div. Ex. 4).

After the conclusion of the hearing herein and the filing of the Division's Proposed Findings of Fact and Conclusions of Law and Brief In Support Thereof, the Registrant filed a post-effective amendment which it designated "Amendment No. 4."

B. Mootness of the Proceeding

Registrant contends that this proceeding should be dismissed on the ground that the issues are moot and that the issuance of a stop order under these circumstances could serve no purpose.

In support of this contention it is pointed out that the registration statement became effective by operation of law on May 15, 1973. The prospectus provided that if the Company was unable to raise a minimum of \$836,000 from the proceeds of the offering within six months

from the time the shares were first offered to the public, it would not commence business and the monies received would be refunded to the subscribers in accordance with the number of shares purchased, less 5% sales commission. Registrant states that all subscription payments less the 5% sales expense have all been returned to investors during the pendency of this proceeding.^{5 /}

It is further argued that this proceeding, instituted on September 18, 1973, had the effect of suspending the effective operation of the registration statement and that the Registrant's "license to sell" was suspended during the pendency of the proceeding. It is also contended that the post-effective amendment indicated that Registrant intended to engage in a different type of business operation requiring far less capital investment than was specified in the original registration statement. Whereas the Registrant originally intended to offer 500,000 shares at \$10 per share, the new prospectus describes a different type of business operation in the computer maintenance field with an offering of 250,000 shares of common stock at \$1 per share. Registrant, therefore, contends that since prior sales have all been rescinded, the effective operation of the registration statement having been suspended in law and in fact and the post-effective amendment having no effective date until the Commission determines that date, Registrant accordingly has no "license" to sell securities and a stop order has nothing to prohibit and nothing to suspend. Concluding the argument, Registrant states that the post-effective amendment relating to a different sale at a different price of fewer securities, the proceeds of which are to be used in a different business operation, is

^{5 /} 'No data has been submitted in support of this statement, but it is accepted as correct for consideration of the contention made. Approximately \$127,000 of stock covered by the registration statement has been sold (Tr. 18).

not the subject of this or any proceeding and the present proceeding should be dismissed as moot.

The registration statement filed by the Registrant became effective by operation of law on May 15, 1973. Registrant then was free to sell the securities covered by the registration statement and did so. Four months later, this proceeding was instituted. The commencement of the proceeding, contrary to the contention made, did not suspend the effective operation of the registration statement. Registrant, pursuant to the provisions of Section 8(d) of the Securities Act, could continue to sell its stock unless and until a stop order were issued suspending the effectiveness of the registration.

Registrant argues that once a stop order proceeding is instituted, a registration statement is no longer "effective" in the sense of "completeness of operative force and freedom to act."^{6/} However, while the order put the Registrant on notice that challenges were being raised to material in the registration statement and omissions from it, Registrant could make its own determination to continue selling stock, since the statement had become effective and remained so.

The Jones case, supra, on which the Registrant relies, dealt with the issue whether a registrant had an absolute right to withdraw a registration statement before its effective date. No such issue has been raised here. Moreover, the filing of an amendment seeking to substantially alter the nature of the original offering cannot moot a stop order proceeding. Once a proceeding has been instituted there is no absolute right to render it moot by filing an amendment. Conversely, it is within the discretion of the Commission whether to consider any post-effective amendment filed during the proceeding.^{7/} Where, as here, stock has been sold to the public

^{6/} Jones v. S.E.C., 298 U.S. 1, 18 (1936).

^{7/} Kiwago Gold Mines Ltd., 27 S.E.C. 934, 940 (1948).

the Commission must consider the rights of those who invested money in the enterprise (although most of their investment was offered to be returned) and also the general public interest in preventing the use of incomplete, false, and misleading material in registration statements (Sec. Act, Sec. 8(c)). After a stop order has been issued, an amendment may be filed to make the necessary changes. Only when an amendment has been made, in accordance with the stop order, the Commission shall so declare and the stop order shall cease to be effective (Sec. 8(d)). It is therefore concluded that this proceeding was not rendered moot by the actions of the Registrant or by operation of law.

C. Deficiencies in the Registration Statement

The Division alleges that the registration statement was deficient in a number of respects by reason of inclusion of misleading statements of material facts and/or omissions of material facts.

1. Plan of Distribution

It is stated in the registration statement (p. 4) ^{8 /} that it is anticipated that securities will be sold by duly licensed salesmen employed by the Company and paid 5% of monies collected or \$.50 per share and that sales will be made by personal contact and advertising in trade journals.

It is alleged that this material is deficient in failing to disclose adequately the extent and type of advertising which Registrant proposed to make and that the federal securities laws only permit notice of the offering in the form of "tombstone advertisements". An additional

8 / Unless otherwise noted, references to the registration statement and prospectus refer to the registration statement and prospectus as amended by pre-effective amendment no. 3, filed April 26, 1973 which became effective on May 15, 1973.

deficiency, it is contended, is the failure to disclose with whom the securities salesmen are licensed and, specifically, whether such salesmen are registered with the Commission as broker-dealers.

Registrant advertised by means of notices of the offering in the form of "tombstone advertisements" which referred readers to the Company for copies of the prospectus. These notices were placed in 3 Arizona newspapers. No advertisements were placed in trade journals. As far as Registrant knew, the threesecurities salesmen it employed were licensed to sell securities in the State of Arizona only, and confined their activities within that State.

The Division contends that in an offering such as this, with no underwriter, it was important for the potential investor to be able to judge the chances for the offering to succeed; that the tombstone advertisements were not selling literature, but merely notices of the offering; and that the registration statement is misleading in failing to disclose the extent and scope of the "advertising" the Registrant intended to make.

There are definite restrictions in the Securities Act and applicable rules on the nature of "advertising" which may be used to sell securities.^{9/} The statement that advertising in trade journals would be used was basically a half-truth without explanation of the nature of the advertising which could be employed, and was materially misleading inasmuch as it related significantly to the success of the offering.

Croyle testified that sales of the Registrant's stock were made only in Arizona by salesmen authorized to sell in Arizona or by Company officials. According to Croyle, Registrant's plan was to commence selling in Arizona and eventually branch out into other states. The undersigned

is not persuaded that there was any material deficiency in the registration statement with regard to the use of salesmen.^{10/}

2. Organization and Business

The Division contends that material in the registration statement relating to the Organization and Business of the Registrant is materially deficient in a number of respects.

Plan of Operation and Anticipated Budget

In a section headed "Plan of Operation and Anticipated Budget" (p.9), the Company's plan and minimum budget is set forth for the first thirty days, then by quarter-year periods, and, finally, personnel projections are made through the fifth year of operations for planned increases in field engineers to 530.

This section is alleged to be deficient in that it fails to disclose adequately the assumptions upon which the "anticipated budget" of Registrant was prepared and fails to disclose the assumptions used for estimating the number and type of employees Registrant will have in the future. In its answer, the Registrant contends that staffing assumptions were spelled out as the best judgment of management.

The Commission, on February 2, 1973, issued its Statement On The Disclosure Of Projections Of Future Economic Performance (Sec. Act Rel. No. 5362). In it, it pointed out that it has been a long-standing policy generally not to permit projections to be included in prospectuses and reports filed with the Commission. It stated that after rule-making hearings, it had determined to permit issuers who meet certain standards to include

^{10/} The post-effective amendment refers to the use of salesmen, but has eliminated any reference to the use of advertising in trade journals (p. 5). Changes made in the post-effective amendment in some material charged as misleading by the Division will be noted in this decision and commented on later.

projections in filings with the Commission. The standards would include a requirement that the issuer had been a reporting company for a reasonable period of time and that it had a history of earnings and of internal budgeting. Underlying assumptions would have to be set forth and projections would have to be for a reasonable period, such as a fiscal year. Specific releases and rule and form changes to implement the Commission's conclusions were to be prepared. These have not yet been issued nor would Registrant fit the standards envisioned by the Commission.

While there are no sales and earnings projections, as such in the section of the registration statement referred to, it is evident that the personnel figures presented constituted a projection of sharp increases in sales and profits. The projection of field engineer staff who would perform the maintenance work for customers was 118 in the first year, 225 in second year, 314 in the third year, 453 in the fourth year, and 530 in the fifth year. Croyle testified that the Company projected \$26,000,000 in gross revenues would be generated by the staff of 530 field engineers and other personnel in the fifth year. (Tr. 57-59). Profits were estimated at \$3,135,000 at the end of the fifth year. While the projected earnings figures were not placed in the registration statement, the employment figures which were directly related to them were inserted. The figures used lend an appearance of predictability of future profits and operations which the Commission has criticised as improper for a corporation which has yet to start business, even though stated as an estimate. ^{11/} It is ^{12/} concluded that the projections in the registration were materially misleading. in failing to adequately disclose the underlying assumptions on which they ^{12/} were based, including the limitations on those assumptions.

^{11/} Thomas Bond, Inc., 5 S.E.C. 61, 71 (1939). See also, Petroleum Investors Participating Assn., 8 S.E.C. 238, 241, 242 (1940); Breeze Corporation, Inc. 3 S.E.C. 709, 720-, 21 (1938).

^{12/} These projections are not present in the post-effective amendment.

Marketing Efforts to Obtain Business

The section of the registration statement headed "The Company" (p. 11) states that the Registrant has made extensive contacts in the industry and has had many requests for service contract proposals, and that while responses have been made, no contracts will be executed until capitalization is sufficiently achieved. The Statement of Matters alleges that the registration statement is incomplete and misleading in that it fails to disclose the nature of the "extensive contacts" made by the Registrant and the extent and nature of the "many requests for service contract proposals."

The Division contends that the language used carries the implication that only the actual execution of the contracts remains to be accomplished inasmuch as Croyle testified that Registrant has responded to inquiries by stating that Registrant is not ready to give service contract proposals. While the undersigned does not agree that the language used goes so far as to indicate that only the actual execution of contracts remains it does carry the clear implication that negotiations have been entered into for service contracts. Conversely, no statement reflects that no proposals have been discussed or even proposed. To that extent the language is misleading. The extent and nature of these requests relate to the success of the enterprise and the failure to give details of these requests renders the statement incomplete and misleading.^{13/}

Computer Maintenance Market

The registration statement notes that the Registrant, as a newly organized business based in Phoenix, Arizona, proposes to engage in the highly competitive computer maintenance business nationwide (p. 1). It is further

^{13/} This language has been substantially modified in the post-effective amendment (p. 14).

stated that the market for maintenance service is estimated at \$530,000,000 in 1972, with projected gross market in 1976 estimated at \$1.948 billion. It is then asserted, "The Company plans to service this market on a nationwide basis, servicing both privately owned computers and leased computers regardless of the manufacture" (p. 12). In the Statement of Matters, it is asserted that the registration statement is deceptive and misleading in juxtaposing the information concerning the size of the estimated computer service market with the statement that the Registrant intends to service such market, since the Registrant is newly organized and has no history of operations, has no existing contracts for this market, and does not have nationwide facilities to service the nationwide market.

The Division contends that by the language used, the investor is led to believe that Registrant has the capacity to immediately service this vast market and that Registrant can compete for a significant portion of it.

Croyle testified that it would be possible for the Company to service equipment on a nationwide basis, but on a selective basis so that there would be "islands of density" as opposed to nationwide density (Tr. 111). An "island of density", according to Croyle, would be a group of Company employees assigned to a contract at a particular location which would be of sufficient size to give the Company economy of scale by having a large enough crew at the location to fulfill contract needs and to return a profit to the Company. There would have to be a significant contract at each separate location (Tr. 109-111).

In its answer, the Company contends that information throughout the prospectus relating to the size of the Company and "Speculative and Risk Factors" furnish details of the condition of the Company so that a

reader could not be misled. However, while it listed a number of large companies in the field and stated that they all had far greater resources than the Company, there was no indication, other than difference in size, that the Company could not compete with the other companies in all parts of the United States. The failure to make clear the "island of density" concept that the Company intended to pursue in nation-wide operations rendered the aforementioned statements incomplete and misleading.^{14/}

Pricing Reductions

The registration statement, in the section headed "Business" contains statements that the Company's business plan involves three major marketing efforts to obtain business (p. 13). One of these is listed as the Federal Government, where the Company proposes to offer maintenance to selected large systems at maintenance prices lower than the published manufacturers' G.S.A. pricing list. Another marketing area is given as Leasing Companies, where the Company plans to seek business on a selective location basis with pricing reduction from the present manufacturers' agreements. These statements are claimed in the Statement of Matters to be deficient in failing to disclose the basis for Registrant's belief that it can furnish maintenance services at lower rates and in failing to disclose whether offering these services at reduced prices will be economically feasible.

Registrant, in its answer, states that other portions of the registration statement clearly set forth the competitive position of the Company with respect to solicitation efforts so that no member of the public could be deceived or misled, and that in order to avoid the misleading of investors, no statement as to the economic feasibility of the Company's

^{14/} The post-effective amendment still retains the concept of operations on a nation-wide basis without any limiting language (p. 10).

plan was included. Croyle testified that the Company could offer pricing reductions lower than prices offered by service companies affiliated with large manufacturing companies because the latter companies had higher overhead costs than the Company would have. He admitted that there would be no such advantage over independent maintenance service organizations (Tr. 72-76).

Registrant claimed substantial competitive advantages in the offer of its maintenance services to important customers but no facts were given to substantiate the claimed advantages. The failure to furnish this information rendered the statements made incomplete and misleading, since investors would have no way to evaluate the asserted competitive advantages.^{15/} It further appeared from Croyle's testimony that the claimed advantages were, at least to a certain extent, illusory.^{16/}

3. Description of Property

In the section of the registration statement headed "Use of Proceeds" (p. 7), it is stated that the Company intends to use \$91,000 to acquire adequate leasehold improvements for warehouses, shops and offices in Phoenix, Arizona. Lease improvements, other than actual leased property, are listed.

This statement is alleged to be incomplete and misleading in that it fails to disclose what leases Registrant has entered into or proposes to enter into in connection with the leasehold improvements and the terms of such leases. The Division contends that the figure of \$91,000 is misleading in omitting to disclose the basis for the figure. Furthermore, it is asserted, the use of the exact figure implies that the Registrant may already have leases and it implies a certainty for which there is no basis.

^{15/} Laser Nucleonics, Inc., Sec. Act Rel. No. 5041, p. 3 (Feb. 2, 1970).

^{16/} The post-effective amendment does not contain any change in the Company's claim of being able to offer price advantages without furnishing any basis for the claim (P. 11).

Croyle testified that the figure of \$91,000 was arrived at after a survey of local leasehold rents to arrive at a square footage rate. This was multiplied by the estimated space required. To this was added the estimated cost of office and other equipment (Tr. 69-72). Registrant, in its answer, states that sufficient detail was furnished, in view of other material making clear that the company was still in the formative stages.

The undersigned concludes that it has not been established that this section was deficient. It was evident that Registrant was referring to leaseholds to be negotiated and other property to be acquired. It is clear that the figure given was an estimate and was not presented as an exact figure.

4. Other Expenses of Registration

It is stated in the registration statement that securities of the Registrant were given for "legal services and the preparation of the registration of these securities" (p. 3). It is later set forth that John C. Hughes, in his capacity as Secretary and Counsel, has received 100,000 shares of common stock (p. 18). It is footnoted at that page that "The services rendered by Mr. Hughes have been those usually performed by an attorney in the formation of a new company, and as corporate counsel, comprising the drafting of legal documents, the securing of the corporate charter, the preparation and filing of this Prospectus, conferences, consultations and the rendering of legal opinions to the corporate officers which were necessary over the two-year period preceding the filing of this registration. By necessity, the determination of the amount of stock to be issued to these three individuals [Hughes, the President, and the Vice-President] has been an arbitrary decision predicated upon the expertise

and contribution of each of said individuals to the formation of the Company and the anticipated guidance to be furnished to the Company hereafter, although no employment contracts have been executed by the Company."

It is further stated on Page I of Part II of the Registration Statement under Item 14 "Other Expenses of Registration and Distribution" that it is not expected that any legal fees will be payable in connection with the distribution of the common stock.

It is alleged that the foregoing material is deficient in failing to set forth at the above section a reasonably itemized statement of all legal expenses incurred or to be incurred by Registrant in connection with the registration and distribution of these securities.

According to Croyle and counsel for the Company, shares of stock were given to counsel for his legal services including the preparation and filing of the registration statement. This has been characterized by Registrant as a loose arrangement (Tr. 113-116).

Registrants, under item 14 of Form S-2 are required to furnish a reasonably itemized statement of all expenses in connection with the distribution of the securities being registered. Registrant contends that it set out in reasonable detail at page 18 what the legal services were and that Item 14 refers to other expenses of registration to be incurred and no additional legal fees have been incurred. However, there is a further statement on page 18 that the stock issued to officers, including Hughes, was issued in consideration of services rendered and expenses paid until April 12, 1973, the date when Amendment No. 3 was signed. There is no mention in the registration statement of any arrangement for the payment of legal fees and expenses after the cut-off date. In addition, the response that no legal fees will be paid in connection with the distribution

of the common stock does not deal with additional expense only, as Registrant contends, but with all legal expense. The response to this item is incomplete and misleading and contradictory to earlier material appearing at page 18, and no clarification is furnished.^{17/}

5. Distribution Spread and Risk Factors

The cover page of the prospectus sets forth that 500,000 shares of common stock are being offered with the price to the public of the shares being \$10.00 per share and commissions of .50 per share or 50 cents.

In the registration statement in a paragraph headed "Impounds" (p. 4) it is stated that "The net proceeds derived from the subscription for the first 88,000 shares of the common stock being offered at \$10.00 per share, less 5% sales expense, shall be deposited as received by the Company with the Company's bank depository, until such time as the whole 88,000 shares have been subscribed for. In the event the net proceeds from the subscription for shares of common stock deposited in the impound account do not exceed the sum of \$836,000 within six months from the time the shares are first offered to the public, then and in that event, the monies deposited shall be refunded to the subscribers in accordance with the number of shares to be purchased, less the 5% sales commission."

It is alleged that the registration statement fails to disclose adequately in a prominent place therein that potential investors stand to lose automatically 5% of their investment should 88,000 shares of the offering not be sold within six months, that the only place in the registration statement where this information is disclosed is in the last line on page 4, and that in a speculative offering, such as this, this important fact should be put on the cover of the prospectus

^{17/} The defects found have not been corrected in the post-effective amendment.

or at least in the "Risk Factors" section of the prospectus.

The first page of the prospectus sets forth clearly that the commission on each share is .50, thus apprising an investor of the cost and commission basis of his purchase. At that point the investor would understand that his entire investment would be at full risk. In the "Summary of Contents" section (P. 1) reference is made to three contingencies, one of which is the failure to realize the appropriate amount necessary to fund the Company's operations, and the reader is referred to the "Impounds" section. In the "Introduction" section (p. 2-3), the statement is made that if the Company does not raise a minimum of \$880,000 it will not commence business and reference is again made to the "Impounds" section.

The "Impounds" section itself clearly states that in the event of refunds, sales commissions will not be refunded. Since reference to the "Impounds" section is made in several important places in the prospectus and the subject itself would attract the interest of investors to that section, the undersigned concludes that sufficient notice of the potential loss of 5% of the cost of each share, designated as sales commission, was given, and the failure to make further reference to it in other places was not misleading.

6. Introductory Statement

On page five of the registration statement there is a graphic illustration entitled, "Illustration of Differential Between Public Offering Price and Price Paid by Promoters." The Division contends that the material furnished is incomplete and misleading since the illustration does not accurately reflect the mathematical relationship between the amount paid by public investors (\$10.00 per share) and the average amount paid by

promoters (\$.0157 per share). These figures appear at the illustration and the differential of \$9.9843 is also noted.

The graphic illustration was furnished in response to the requirement: "There shall also be set forth a chart in the following form to illustrate the difference between the public offering price and the price paid by promoters and others, including private investors who have previously purchased shares of the registrant (appropriate presentations also are acceptable)" (Sec. Act Rel. No. 5278, July 26, 1972).

The Division contends that the registration statement is materially misleading in the inclusion of a mathematically inaccurate graph to illustrate the difference between the price paid by the public and that paid by the promoters, thereby grossly overstating the price paid for Registrant's stock by the promoters when comparison is made of the size of the block labeled "Average Amount Paid by Promoters" with that labeled ". . . Amount Paid by Public Investors".

The Registrant contends that the illustrative chart shown in Sec. Act Rel. No. 5278 contains an 80% error and that if the differential on page 5 of the registration statement were to be shown in absolute accuracy the graph would have to be reproduced on paper 41" tall, with the block representing price paid by promoters being 1/16" high (too small to include the printed amount) and the block representing the amount paid by the public being 41" in height. It is further pointed out that the figures given are stated accurately and that the same information is set out more fully in the printed paragraph on "Dilution".

Sec. Act Rel. No. 5278 was enacted for the announced purpose of making prospectuses more readable and understandable. In addition to

furnishing written information on the extent of dilution, registrants, in appropriate cases, are required to set forth in graphic form an illustration of the dilution of the investor's equity in the enterprise. The Commission emphasized that "Any graphic presentation presented in accordance with this Guide should accurately reflect the mathematical relationship of information presented." Judged by this standard, the graphic illustration on Page 5 was incomplete and misleading. At the very least, if the Registrant had encountered problems in graphic presentation, it should have pointed that out and given the exact dimensions of the required chart.^{18/}

III. CONCLUDING FINDINGS, PUBLIC INTEREST

The Registrant contends that adequate disclosure of material facts has been made in the registration statement, the significant parts of the prospectus have not been challenged, and the only risk which the Division contended was not adequately disclosed was the risk of loss of 5% of a subscription payment in the event the offering does not succeed.^{19/} It is further urged that where relevant and appropriate, the language used in the post-effective amendment has been drafted with due regard to the allegations contained in the Statement of Matters and describes a different type of business operation with a different stock offering from that originally proposed.

The Division has taken the position that the numerous deficiencies in the registration statement render it materially misleading and that a stop order should issue suspending the effectiveness of the registration statement.

^{18/} The post-effective amendment (p. 6) contains an accurate graphic presentation.

^{19/} It also pointed out that it made an offer of settlement in which it offered to refund the 5% payment. The offer was rejected.

It has been found that the registration statement was materially deficient in that it included untrue statements of material facts or omitted to state material facts required to be stated therein, or necessary to make the statements therein not misleading. Contrary to the contentions of the Registrant, the deficiencies were serious and substantial and rendered the registration statement inaccurate and misleading.

The Registrant attempted to meet at least some of the allegations in the Statement of Matters in the post-effective amendment. The amendment was filed after the hearing herein and the Registrant, in preparing the amendment, had the benefit of the evidence developed at the hearing and a conference which the undersigned directed the parties to have during the hearing so that there could be an interchange of views which might be mutually helpful.

It is a matter of discretion to consider a post-effective amendment during a stop order proceeding. The undersigned has decided to do so in view of the fact that in the opinion of the undersigned the Registrant has made efforts in good faith to meet applicable requirements. It has been pointed out by footnote references in this decision that the Registrant has made certain changes designed to meet the deficiencies.^{20/} Yet serious deficiencies do remain, including the failure to mention this current litigation.

20/ The Division has taken the position that the post-effective amendment not only does not dispose of the issues raised in the administrative proceeding, it does not mention them and, therefore, does not give any notice to investors of the deficiencies existing in the effective registration statement which is the subject of this proceeding (Reply Brief).

The Registrant maintains that it attempted in good faith to meet all applicable requirements in preparing and amending the registration statement. However, the Commission has stated,

"The Securities Act of 1933 requires more than good faith; it requires, as well, that those who seek trusteeship of the public's money on the basis of information in the registration statement and the prospectus, must live up to certain minimum standards of ability and due care in their preparation. It will not suffice that a registrant has attempted to prepare a registration statement to the best of its ability. It is necessary that it meet the standards imposed by the law." 21/

This principle, first enunciated in early Commission cases, has never been changed or modified. 22/ The registration statement, as amended, fails to meet this standard.

Registrant, in its post-effective amendment, substantially changed its financing plans by decreasing the dollar value of securities offered from \$5,000,000 to \$250,000. Its plan of operations was altered to include consultation and maintenance management in addition to computer maintenance services. These changes do not warrant any withholding of a stop order since the offering of securities would still be made under a deficient registration statement.

It is concluded that a stop order should issue. Registrant can then proceed to remedy the deficiencies found, if it wishes to,

21/ Herman Hanson Oil Syndicate, 2 S.E.C. 743, 746 (1937); Accord, Unity Gold Corporation, 1 S.E.C. 25, 29 (1934); Emporia Gold Mines, Inc., 2 S.E.C. 209, 221 (1937); U.S. Molybdenum Corporation, 10 S.E.C. 796, 804 (1941).

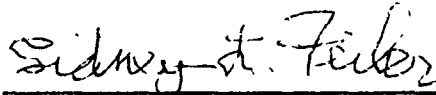
22/ Franchard Corporation, 42 S.E.C. 163, 174 (1964); Clinton Engines Corporation, 42 S.E.C. 353, 358 (1964).

in accordance with statutory requirements and procedures.

Accordingly,

IT IS ORDERED that the effectiveness of the registration statement filed by Croyle Computer Services, Inc. is suspended.

Pursuant to Rule 17(b) of the Commission's Rules of Practice a party may file a petition for Commission review of this initial decision within fifteen days after service thereof on him. This initial decision pursuant to Rule 17(f) shall become the final decision of the Commission as to each party unless he files a petition for review pursuant to Rule 17(b) or the Commission, pursuant to Rule 17(c), determines on its own initiative to review this initial decision as to him. If a party timely files a petition to review or the Commission takes action to review as to a party, this initial decision shall not become final as to that party.^{23/}



Sidney L. Feiler
Administrative Law Judge

Washington, D.C.
May 31, 1974

23/ All contentions and proposed findings and conclusions have been carefully considered. This initial decision incorporates those which have been accepted and found necessary for incorporation therein.