ADMINISTRATIVE PROCEEDING
FILE NO. 3-4117

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	
SPENCE & GREEN CHEMICAL COMPANY	INITIAL DECISION
(24FW-1555)	

APPEARANCES: Robert F. Watson and James E. Sims of the Dallas Regional Office of the Commission for the Division of Enforcement.

Andrew Spence, President, Spence & Green Chemical Company for the Company.

BEFORE: Ralph Hunter Tracy, Administrative Law Judge

Spence & Green Chemical Company (Spence & Green), incorporated in Texas on March 6, 1956, filed with the Commission on September 14, 1972, a Notification and Offering Circular for the purpose of obtaining an exemption from the registration requirements of the Securities Act of 1933 (Securities Act) pursuant to Section 3(b) thereof and Regulation A thereunder, with respect to a public offering of 104,250 shares of its $.50 par value common stock at $2.50 per share.

The Commission, on January 11, 1973, issued an order (Order) pursuant to Rule 261 of Regulation A temporarily suspending the exemption. The Order alleges, in substance, that the $500,000 ceiling available under Regulation A would be exceeded because of Spence & Green's refusal to escrow stock held by directors, officers and promoters as required by Rule 253 of Regulation A; that the Notification and Offering Circular were deficient in that they contained untrue statements of material facts and omitted to state material facts necessary to make the statements made, in the light of the circumstances under which they were made, not misleading; that the terms and conditions of Regulation A have not been complied with; and that the offering, if made, would have been in violation of Section 17 of the Securities Act.

The issuer filed an answer denying the allegations generally and requesting a hearing to determine whether to vacate the Order or to enter an order permanently suspending the exemption.

Spence and Green was represented by its president, Andrew Spence, who is not an attorney. Proposed findings of fact and conclusions of law and briefs in support were filed by the parties.

The findings and conclusions herein are based upon the preponderance of the evidence as determined from the record and upon observation of the witnesses.

ISSUER

According to the Offering Circular the issuer is the successor to S & G Laboratories, a partnership, whose assets were acquired by issuer in exchange for 348,780 shares of its common stock. The appraised fair market value of S & G. Laboratories was $264,000. The company states that it is engaged in the research, development and construction of a chemical process of improved design for the conversion of certain low grade industrial by-products into readily market(sic) products of higher grades and that it has three patents issued on this process.

On July 21, 1972, Spence & Green filed a Notification and Offering Circular pursuant to Regulation A under the Securities Act for the purpose of obtaining an exemption from the registration requirements of the Act for a proposed offering of 104,250 shares of its $.50 par value common stock at $2.50 per share. By letter of July 31, 1972, the Fort Worth Regional Office rejected this filing and returned it with a letter stating that it was so deficient as not to be reviewable. However, some 14 areas of obvious deficiency were cited.

On September 14, 1972, Spence refiled the Notification and Offering Circular with a covering letter stating that "there is very little change in the offering circular. The valid deficiencies have been corrected. I have the following comments for the deficiencies you outlined in your letter of July 31, 1972:". Spence then goes on to dispute each of the 14 items cited but without making any corrections.

On October 31, 1972, Spence addressed a letter to stockholders of Spence & Green which was strongly critical of the Commission's handling

of his Regulation A filing and which stated that the offering was now being made to Texas stockholders only. Enclosed with the letter was the offering circular filed on September 14, 1972, together with all copies of correspondence between Spence and the S.E.C., including the deficiency letter of July 31st with comments written in by Spence.

DEFICIENCIES IN REGULATION A FILING

Failure to Escrow Securities Pursuant to Rule 253.

The Offering Circular discloses that Spence & Green has 1,542,738 shares outstanding; that Andrew Spence is the record and beneficial owner of 411,274 shares; that other directors and officers as a group own 282,292 shares; and that 95,750 unregistered shares were issued to officers, directors and existing shareholders within the 12 months preceding the date of the Offering Circular.

Rule 253 of Regulation A provides that where, as here, an issuer was incorporated more that one year prior to the date of a Regulation A offering and has not had a net income from operations, of the character in which the issuer intends to engage, for at least one of the last 2 fiscal years, then in computing the amount of securities to be offered it must include all securities issued prior to the filing of the Notification to any director, officer or promotor of the issuer. However, such securities need not be included in the computation if, as provided in the Rule, they are escrowed or otherwised immoblized to assure against there being offered to the public for at least one year after the commencement of the Regulation A offering.

Spence & Green has never had a net income from operations since its incorporation in 1956. A Statement of Expenses and Operating Deficit

included in the Financial Statement filed with the Offering Circular shows net loss or deficit for each year from 1967 to June 30, 1972, totaling $939,892.

Spence has refused to comply with the escrow provisions of Rule 253. He argues that Rule 253 does not apply as Spence and Green has had a net income from operations of the character in which it was engaged. He arrives at this conclusion by redefining income as gain and then asserting that research and development was the character of the business and having completed its research Spence & Green's gain is almost unmeasurable.

The argument advanced by Spence concerning issuer's failure to comply with Rule 253 is rejected. The record supports a finding that the provisions of Rule 253 were applicable under the circumstances herein and that no effort was made to comply with them. Accordingly, such refusal to comply renders the Regulation A exemption unavailable pursuant to Rule 261.[1/]

It is axiomatic that the burden of establishing the availability of an exemption from registration rests upon the one who claims it.[2/]

1/ Rule 261 promulgated under the Securities Act of 1933 provides that the exemption shall be suspended if --

> "(1) . . . any of the terms or conditions of this regulation have not been complied with . . .
> (2) The notification, the offering circular or any other sales literature contains any untrue statement of material fact or omits to state a material fact necessary to make the statements made, in the light of the circumstances under which they were made, not misleading;
> (3) The offering is being made or would be made in violation of Section 17 of the Act . . ."

2/ S.E.C. v. Ralston Purina, Inc., 346 U.S. 119 (1953).

The exemption under Regulation A is conditional and it is available only as to securities "offered in accordance with the terms and conditions . . . of (the) Regulation."[3/]

False and Misleading Statements in Offering Circular

Spence & Green is controlled and operated by Andrew Spence who has been its dominating force since its inception in 1956. From that time until September 14, 1972, he had issued for services and cash a total of 1,542,738 shares of the company's common stock without a registration statement being in effect, or an exemption from registration being available. During this time he has extracted from the public over $1,500,000 which he has used to support himself and the company. Although Spence claims that there are only 58 stockholders the record discloses at least 873, which includes 314 Texas residents, 484 out of state residents and 75 accounts in Street name with brokerage firms. The price at which the stock has been sold ranges from $.50 to $5.00 per share and it has been traded over the counter and listed in the pink sheets and 82 broker-dealers have submitted stock to the company for transfer.

Spence has pursued a self regulatory theory of his own which allows him to issue and sell stock whenever he chooses and to anyone he wishes. He testified that he would allow the sale of restricted stock "If I considered it a proper transaction." What he was describing was the resale by others of stock purchased from him. His method of operation

---

3/ S.E.C. v. Sunbeam Gold Mines, Inc., 95 F.2d 699 (9th Cir. 1938); In the Matter of Taxas-Augello Petroleum Co., 39 S.E.C. 292 (1959).

was to sell shares subject to a 13 month holding period after which they were free to be sold. Sometimes a legend would be placed on the shares and sometimes not, but in any event it would be removed by Spence upon request. He testified that "Over the period from March 6, 1956 to January 30, 1973, there have been transactions with fifty-eight persons and suppliers of equipment." However, this does not tell the whole story. What actually took place was that the shares for ten subscribers would be placed in the name of one person and then at the end of the 13 month period would be transferred to each subscriber who was then free to sell under Spence's interpretation. Spence has been the only salesman and the company has been its own transfer agent and registrar.

Sometime in late 1970 or early 1971 Spence employed a certified public accounting firm to prepare financial statements for Spence & Green. At that time he was contemplating filing a Notification and Offering Circular with the Commission, and, also, becoming registered under Texas securities law so that he could sell the shares publicly. While certified financials are not required for a Regulation A filing they are a requirement to becoming registered in Texas for the sale of securities.

After considerable effort the auditors informed Spence in writing that they could not make an audit as the books and records of Spence & Green were not auditable. Among other things the auditors found that there was no basis for the valuation of the assets conveyed to Spence & Green, the issuer, from the partnership at the time of incorporation; that no records and documents supporting cash receipts and disbursements could be found; that the basis for the inventory valuation carried on the books was indeterminable; and that the collectability of advances to Spence

personally could not be ascertained.

At the request of the auditors for a legal interpretation of the issuance of stock by Spence & Green a letter was prepared at the request of Spence by a securities lawyer under date of January 31, 1972, which stated that there had been a number of transactions involving shares of the company's common stock which may have been in violation of Section 5 of the Securities Act of 1933, and that such transactions may have created a liability against the company at least equal to the consideration which the company received for such shares. The letter then proceeds to set forth five pages of stock transactions involving 17 individuals and 186,210 shares. This letter was delivered to Spence by the attorney but Spence did not deliver it to the auditors. Instead he addressed a letter to the auditors, dated February 2, 1972, in which he stated, "In my opinion, there have been no security violations made by the company."

After the auditors withdrew Spence had the financial statement contained in the offering circular prepared by James I. Farmer, CPA, a director of Spence & Green. Although the Offering Circular filed on September 14, 1972, states that no outside accounting firm has been involved in the financial statements, it does not disclose who prepared it. Mr. Farmer testified that at the time he prepared the financial statement he had available the report of the auditor and the letter from the securities lawyer advising as to the possible Section 5 violations and the contingent liabilities. Farmer was aware that the financial statement he prepared was to be used in an Offering Circular in connection with a proposed public offering of Spence & Green securities but he

did not examine Regulation S-X promulgated by the SEC with respect to accounting requirements for financial statements used in offerings of securities.

None of the foregoing information concerning the sale of unregistered securities by the company and others, the warning by an attorney of possible Securities Act violations and contingent liability arising therefrom, the inability of auditors to ascertain the company's financial condition and the role of a director of the company in preparing a financial statement at Spence's direction was disclosed in the Notification or Offering Circular.

Accordingly, it is found that the Notification and Offering Circular of Spence & Green contains untrue statements of material facts and omits to state material facts necessary to make the statements made, in the light of the circumstances under which they were, not misleading.

The Order for Proceeding alleges, further, that the terms and conditions of Regulation A have not been complied with in that there is no disclosure in the Offering Circular concerning: the nature of the company's proposed products; how the company's research and development and patents are to be applied commercially; transactions between management and the company; and a description of the equipment and processes purportedly developed by the company.

Spence has refused to supply any of this information on the ground that it is all of a proprietary nature and cannot be disclosed even on a confidential basis to the staff of the Commission. He stated in the cover letter to the September 14, 1972 filing: "The Company's patents are listed by number and give adequate description of the patents and

their application. Know how in application, commercial refinement, becomes proprietary knowledge."

In view of the issuer's refusal to furnish any meaningful information as to the company's business and related matters it is found that the terms and conditions of Regulation A have not been complied with as alleged in the Order.

SECTION 17(a) OF THE SECURITIES ACT

As found above, the Offering Circular filed on September 14, 1972, intended for use in Spence & Green's proposed offering contains materially false and misleading statements concerning the company and its past, present and proposed activities. The use of the offering circular in connection with the offer or sale of Spence & Green's common stock, therefore,would operate as a fraud and deceit upon purchasers in violation of Section 17(a) of the Securities Act.

CONCLUSION

Each one of the violations found is sufficient to suspend the exemption. As previously stated, the obligation to comply with the terms and conditions of Regulation A rests with the one seeking to take advantage of it, in this case Spence & Green. It is clear that Spence & Green failed to comply with the terms and conditions of Regulation A. Therefore, it is concluded that the exemption of Regulation A should be permanently suspended, accordingly,

IT IS ORDERED, pursuant to Rule 261 of Regulation A under the Securities Act of 1933, that the exemption of Spence & Green Chemical Company under Regulation A is permanently suspended.

This order shall become effective in accordance with and subject to Rule 17(f) of the Commission's Rules of Practice.

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party who has not within fifteen days after service of this initial decision upon him, filed a petition for review of this initial decision pursuant to Rule 17(b), unless 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 for review, or the Commission takes action to review as to a party, the initial decision shall not become final with respect to that party.[4/]

Ralph Hunter Tracy
Administrative Law Judge

Washington, D.C.
July 18, 1973

4/ To the extent that the proposed findings and conclusions submitted by the parties, and the arguments made by them, are in accordance with the views herein they are accepted, and to the extent they are inconsistent therewith they are rejected.