ADMINISTRATIVE PROCEEDING
FILE NO. 3-2451

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

PAUL L. RICE
1307 Andover Court
Oklahoma City, Oklahoma

INITIAL DECISION

David J. Markun
Administrative Law Judge

April 30, 1973
Washington, D. C.

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APPEARANCES: Joan H. Saxer, Robert Yeager, Thomas W. McIlheran, with Cecil S. Mathis on the reply brief, for the Division of Enforcement ("Division") (formerly called Division of Trading and Markets).

A. Bob Jordan, Gerald E. Durbin II, of Rogers, Travis & Jordan, Oklahoma City, Oklahoma, for Respondent.

BEFORE: David J. Markun, Administrative Law Judge

THE PROCEEDING

This public proceeding was instituted by an order of the Commission dated May 13, 1970 ("Order") against Respondent Paul L. Rice ("Rice", or "Respondent") and four other respondents[1] pursuant to Sections 15(b), 15A, and 19(a)(3) of the Securities Exchange Act of 1934 ("Exchange Act") to determine whether the respondents committed various charged violations of the Securities Act of 1933 ("Securities Act") and of the Exchange Act and the remedial action, if any, that might be appropriate in the public interest.

The proceeding has been resolved as to all respondents other than Respondent Rice in the Commission's Findings, Opinion and Order of Suspension dated November 3, 1972.[2] The Opinion and Order of the Commission did not consider the charges against Respondent Rice inasmuch as the Commission had earlier issued a default order against Rice barring him from association with any broker or dealer, based upon a finding that he had failed to appear at the hearings held after having been duly notified of them.[3]

In connection with a petition for review of the default bar order filed with the United States Court of Appeals for the Tenth

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1 / The other respondents were Stone Summers & Company ("Registrant" or "Stone Summers"), a broker-dealer firm in Oklahoma City that has been registered with the Commission since March 29, 1968, and three officers and owners of the firm: Alexander J. Stone ("Stone"); Thomas E. Summers ("Tom Summers"); and Bobby Layne Summers ("Bob Summers"). The latter two are brothers.

2 / Securities Exchange Act Release No. 9839, November 3, 1972.

3 / Securities Exchange Act Release No. 9206, June 14, 1971, reconsideration denied July 28, 1971.

Circuit, the Commission stayed its bar order against Rice and ordered that a public hearing be held with respect to the issues regarding Respondent Rice, subject to stated conditions set forth in the "Order For Hearing", dated March 29, 1972, [4/] which conditions reflected agreements that the Commission and Rice had arrived at in connection with Rice's review petition in the Court of Appeals.

In accordance with the Order For Hearing of March 29, 1972, public hearings respecting the charges against Respondent Rice were held in Oklahoma City, Oklahoma, on May 22, 23, 24 and 25, 1972. [5/]

4/ The Order For Hearing was issued subject to conditions that:

1. The petition for review filed with the Court of Appeals on September 13, 1971, be dismissed with prejudice and without costs.

2. All of the testimony and exhibits which were before the hearing examiner when he made his initial decision with respect to other respondents will be admissible in the hearing on the allegations against Rice, and Rice will be accorded an opportunity to cross-examine any of the witnesses who testified at the prior hearings upon whose testimony reliance is placed by the Commission's staff and to introduce any relevant evidence.

3. A date certain, agreeable to all parties and the hearing examiner, shall be set for the hearing, and no postponements of the scheduled hearing date will be granted.

4. Rice will appear and take the stand at the scheduled hearing.

5. The hearing examiner who presided at the hearings with respect to the other respondents herein may be assigned to preside at the hearing because of his familiarity with the proceedings.

5/ These hearings respecting Respondent Rice are reported in pages 634 through 1274 of the transcript of hearings in this proceeding.

(CONTINUED)

This initial decision has application only to Respondent Rice, even though the decision will necessarily, in view of the nature of the charges and of the factual circumstances, also involve findings respecting some of the other respondents. 6/

The Division of Enforcement ("Division") and Respondent Rice filed proposed findings of fact, conclusions of law, and supporting briefs pursuant to Rule 16 of the Commission's Rules of Practice, 17 CFR 201.16. The findings and conclusions herein are based upon the record 7/ and upon observation of the demeanor of the various

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5/ Continued.
At the hearings respecting Respondent Rice the Division introduced Exhibits 1 through 6 and Respondent Rice introduced Exhibits A through L. In accordance with the Order For Hearing and procedures established at the close of the hearings respecting Rice, the Division designated for inclusion in the record respecting Rice pages 53, 132, 142-144, 174-175, 207-254, and 366-400 of the transcript of the hearings involving the respondents other than Rice and also designated for such inclusion Exhibits 1, 5, 11, 22, 26-40, and 131 introduced by the Division at the earlier hearings at which Rice had not appeared. (The exhibits so designated do not include the transcript of prior testimony given to the Commission's staff investigators by Paul Dawson which was received as an exhibit for limited purposes at the original hearings — at which Rice was not present — in this proceeding. See Securities Exchange Act Release No. 9839, November 3, 1972, footnote No. 11 and text thereto, at p. 4) These portions of the earlier transcript and exhibits designated by the Division were received in evidence by the undersigned's order of August 14, 1972 as part of the record respecting Respondent Rice. The Respondent did not designate for inclusion any portions of the transcript of the hearings involving the other respondents or of exhibits received during such hearings, but did offer an additional exhibit "M" of his own, which was received without objection from the Division.

6/ See footnote 1 above.

7/ The record as it affects Respondent Rice includes those portions of the transcript of the hearings and those exhibits introduced in this proceeding that are so specified in footnote 5 above.

witnesses. Preponderance of the evidence is the standard of proof applied.

FINDINGS OF FACT AND LAW

The Respondent.

Respondent Rice, 63, was employed as a registered representative by Stone Summers from about September, 1968, to September, 1970, when he was let go because of the firm's decision to eliminate or minimize its "retail" business. Before coming to Stone Summers, Rice had had about 9 or 10 years of experience in the brokerage business, including a brief (and unsuccessful) fling at running his own (essentially one-man) brokerage firm. Prior to that, Rice had worked for a variety of employers in a variety of occupations unrelated to the securities business.

At Stone Summers, Rice's supervisor during the relevant period was Tom Summers and, in his absence, his brother, Bob Summers.

Rice has had about 3½ years of college; his major was accounting.

Charges Against Respondent Rice.

The Order For Proceeding of May 13, 1970, charges, inter alia, that Rice (and the other respondents) wilfully violated and wilfully aided and abetted violations of Sections 5(a) and 5(c) [8/] of the Securities

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8/ 15 U.S.C. §77e . As applicable here, Sections 5(a) and 5(c) make it unlawful to use the mails or interstate commerce facilities to sell or deliver a security unless a registration statement is in effect as to such security, or to offer to sell a security unless a registration statement has been filed as to such security.

Act during the period 11-1-68 to the date of the Order through use of jurisdictional means in offering to sell, selling, and delivering after sale various shares of the common stock of United Australian Oil, Inc. ("UAO") at a time when no registration statement was filed or in effect as to such securities under the Securities Act. 9/

Rice's violations of Sections 5(a) and 5(c) of Securities Act.

The record establishes that during November and December of 1968 Stone Summers sold to various other broker-dealers 698,000 shares of UAO stock as to which no registration statement under the Securities Act was filed or in effect at the times of the sales. 10/ Of these shares sold by Stone Summers, 100,000 had been purchased from Paul Dawson ("Dawson") and resold as principal, another 100,000

9/ The Order of May 13, 1970, in Section II C, D thereof also included charges that Rice (and the other respondents) wilfully violated and wilfully aided and abetted violations of the antifraud provisions of Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-6 and Rule 10b-5 thereunder in connection with the Registrant's distribution of, bidding for, and trading activities in, UAO stock. Examination of the Division's briefs indicates it has abandoned any effort to establish that Rice aided or abetted Registrant's violations of Rule 10b-6, and the record does not support the charge that he did. It is further concluded that the record does not contain sufficient evidence supporting the Division's contention that Rice wilfully violated Rule 10b-5 by failing to inform purchasers (other broker dealers) of UAO stock involved that the stock was unregistered. Nor does the record establish violations of Section 17(a) or 10(b) on any other basis under the cited charge.

The Order of May 13, 1970, in Section II F thereof, further included charges that Rice (and the other respondents) violated Section 10(b) of the Exchange Act and Rule 10b-5 thereunder in other respects, but this charge has been abandoned by the Division and lacks support in the record.

10/ The mails and telephones were utilized in these transactions.

shares had been sold as agent for Dawson, and 498,000 were sold as agent for Charles I. Allen ("Allen").

Rice was the registered representative for both the Dawson and the Allen accounts at Stone Summers and both customers dealt directly with Rice in arranging the subject transactions in UAO stock. Rice received the customary commissions for acting as registered representative in the transactions.

As will be discussed more fully below, Respondent Rice has failed to establish the availability of any exemption 11/ to the registration requirements; accordingly, it is concluded that Rice wilfully 12/ aided and abetted Registrant's violations of Section 5(a) and 5(c) of the Securities Act in connection with the purchase from and sales for Dawson and Allen of the UAO stock.

Respondent Rice's Contentions.

Respondent Rice asserts a number of defenses and makes a number of contentions, none of which is supported by the record or by applicable legal principles and authorities.

11/ The burden of proving entitlement to an exemption from the general policy of the Securities Act requiring registration devolves upon the person claiming the exemption. S.E.C. v. Raleston Purina Co., 346 U.S. 119 (1953); S.E.C. v. Culpepper, 270 F. 2d 241, 246 (C.A. 2, 1959); Penaluna & Co. v. S.E.C., 410 F. 2d 861, 865 (C.A. 9, 1969) cert. den., 396 U.S. 1007 (1970).

12/ It is well established that a finding of wilfullness under Section 15(b) of the Exchange Act does not require an intent to violate the law and that it is sufficient that a respondent intentionally engaged in conduct which constitutes a violation. Tager v. Securities and Exchange Commission, 344 F. 2d 5, 8 (C.A. 2, 1965); Dunhill Securities Corporation, Sec. Exch. Act Rel. 9066, p. 4 (Jan. 26, 1971).

(1) Jurisdiction.

First, by way of attacking the Commission's jurisdiction, Rice asserts that all of his dealings with Dawson and Allen took place in Oklahoma City, Oklahoma, and were therefore intrastate and not within the jurisdiction of the Securities Act. In a kindred vein, Rice argues that while he participated in the purchase of UAO stock from Dawson and Allen,[13/] he did not participate in the sale of any UAO stock for Dawson or Allen, on the theory that the physical acts connected with selling the UAO stock by Stone Summers were handled by personnel of the firm other than himself.

Neither contention is valid. The record establishes abundantly that the mails and other instrumentalities of interstate commerce (e.g. telephones) were utilized in effecting the subject transactions. Allen's UAO stock was purchased under an agreement made by him in Texas from the president of UAO[14/] and the stock itself was transported by automobile from Texas by an employee of the seller to Allen in Oklahoma City, and both the Allen stock and the Dawson stock were sold by Stone Summers[15/] to a variety of broker-dealer purchasers,

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13/ Actually, Stone Summers did not buy any UAO stock from Allen but merely sold 498,000 (of the 500,000 shares he presented for sale) shares as his agent.

14/ This point is discussed in greater detail below in another connection.

15/ Stone Summers's business as a broker dealer was primarily wholesale though it had some retail customers. All of the UAO stock here involved was sold to other broker dealers, not to individual customers.

both within and without Oklahoma. Jurisdiction therefore clearly exists. Rice played a key role in aiding and abetting Stone Summers's participation in the unlawful distribution of UAO stock since it was he who brought the stock in to Stone Summers, on behalf of his customers,[16/] either to be purchased by Stone Summers as principal and then resold or to be sold as agent for Dawson and Allen.

The argument such as Rice makes that he did not personally sell the UAO stock and should therefore not be held to have aided and abetted an unlawful distribution of unregistered stock was specifically considered and rejected by the Court of Appeals for the Ninth Circuit in Nees v. S.E.C., 414 F. 2d 211, 220 (C.A. 9th, 1969).

(2) Non-Availability of Exemptions from Registration.

Secondly, Respondent Rice contends that the UAO shares here involved were exempt from registration under Sections 4(3) and 4(4)[17/] of the Securities Act. As already noted, the burden of proving entitlement to an exemption from the general policy of the Securities Act requiring registration rests with the person claiming the exemption.[18/]

16/ Indeed, as is developed below in another connection, Rice had an understanding with Allen to share in the profits that Allen expected to realize from his selling of his UAO stock.

17/ Subject to certain exceptions, Section 4(3) provides an exemption for a dealer as to trading occurring after a period of distribution. H.R. Rep. No. 85, 73d Congress, 1st Sess., p. 16 (1933). Section 4(4) exempts brokers' transactions executed upon customers' orders but not the solicitation thereof.

18/ See footnote 11 above.

Respondent Rice here fails to sustain that burden. Indeed, Rice does not seriously dispute what the record abundantly establishes, namely, that Allen and Dawson were both statutory underwriters within the meaning of Section 2(11) of the Securities Act.[19] The Commission has held that the brokers' exemption in Section 4(4) is not available when the broker knows or has reasonable ground to believe that his customer is an underwriter since in that circumstance the broker likewise violates Section 5 by participating in a non-exempt transaction.[20] Likewise, the Commission has held that the dealers' exemption in Section 4(3) is not available to a dealer who is selling unregistered securities for an underwriter.[21]

Dawson and Allen became involved with UAO sometime prior to the sales of UAO stock here involved. In 1967 Dawson was the manager of, and Allen performed legal services for, Sound Tronics of Oklahoma, Inc. ("Sound Tronics"), a background music company owned by H.B. Todd ("Todd"), president of UAO. Sound Tronics was acquired by UAO in that year for shares of UAO stock. Todd gave both Dawson[22] and

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19/ Section 2(11) defines an underwriter to include any person who purchases securities from an issuer with a view to distribution or participates in any such undertaking. For the purposes of this definition the term "issuer" is defined to include any person who controls the issuer.

20/ Herbert L. Wittow, Securities Exchange Act Release No. 9303, p. 6 (August 24, 1971); Quinn and Company, Inc., Securities Exchange Act Release No. 9062, p. 7 (January 25, 1971), aff'd 452 F. 2d 943 (C.A. 10, 1971).

21/ Quinn and Company, Inc., supra, at p. 8.

22/ Before Dawson and Todd severed their relationship, Dawson was Todd's "right-hand man" not only as respects Sound Tronics but on UAO matters generally, at a time when UAO was in the process of acquiring various subsidiaries.

Allen[23] UAO stock in partial payment for the services they had rendered Sound Tronics. In 1967 and 1968 Dawson and Allen sold some of their UAO stock; in both cases Rice, who was then working for Hagen & Co., a registered broker-dealer in Oklahoma City (in which firm the Summers brothers were also then working as traders), was the account representative who handled those sales of UAO.[24] Thereafter, after the Summers brothers became officers, directors and part owners of the newly-organized Stone Summers, in the latter half of 1968, Rice became a registered representative with Stone Summers and acted as such in connection with the distribution of the UAO stock of Dawson and Allen that is involved in this proceeding.

By letter dated November 1, 1968, Dawson sent Rice two certificates for 100,000 shares each of UAO stock dated August 26, 1967. His letter recited that "this stock is free trading stock and is not investment legend stock," and requested Rice to sell the shares for him.[25] No one at Stone Summers, including Rice, with

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23/ Allen's father-in-law was once made a member of the board of directors of UAO. At one point Allen and Dawson hoped to acquire an equity interest in Sound-Tronics/UAO in exchange for their personal services to the firm as part of a management team, but these hopes never came to fruition.

24/ Rice knew both Allen and Dawson personally and was aware that they had obtained the stocks in exchange for services performed for Sound Tronics. (Dawson also worked for Todd on assignments connected with UAO, and Rice was aware of this).

25/ Later, Dawson wrote Rice a letter on November 12, 1968 giving instructions to sell the UAO stock at 30¢ minimum rather than the originally - set 40¢ minimum. On November 22, 1968, Dawson sent Rice a telegram telling him to disregard previous limitations and to sell all his UAO stock at market.

whom Dawson was directly dealing, asked Dawson the pertinent questions about his acquisition of the stock, even though Rice and at least Tom Summers (at the supervisory level) were well aware that Dawson had been associated with UAO's subsidiary, Sound Tronics, and with UAO's president, Todd. Rice and Tom Summers failed to make adequate inquiry of Dawson or other sources even though they knew that Dawson had earlier had trouble getting Todd to remove a restrictive legend as to shares of UAO that Rice had earlier sold for Dawson while Rice was at Hagen & Co.[26/] Rice testified at the instant hearing that Dawson had told him either that he had bought some UAO stock "off the market" or that he had received it in payment of prior services rendered Sound Tronics.[27/] Notwithstanding these obviously suspicions circumstances, Stone Summers went blithely ahead, sent the two 100,000 share certificates to UAO, which acted as its own transfer agent, for transfer into street name in small denominations, which was done without question, and then proceeded to distribute the unregistered UAO stock as described earlier.

The 498,000 shares of UAO stock sold for Allen by Stone Summers as agent was part of 500,000 shares obtained by Allen from Todd, after

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26/ While Rice was still with Hagen & Co. he became sold on the proposition that Todd would build another Litton Industries out of UAO, and expressed that view to Tom Summers.

27/ After extended examination and cross examination on the point, Rice professed to be unable to recall which it was. In any event, in light of his prior experience with Dawson and UAO stock, Rice, who had some 10 years experience in the securities business, should have inquired further as to the source of Dawson's stock.

Allen had earlier negotiated for the purchase of 500,000 shares of the stock from other holders, including the Boucher Trust ("Boucher Trust stocks"). This earlier prospective deal fell through after Allen found that the stock involved (which had been drafted into a bank in Oklahoma City) was marked with a restrictive legend. He traveled to Dallas to talk to Todd to see if the restrictions on the Boucher Trust stock could be removed. Todd told him he could not or would not do so but, as Allen testified, Todd told him that another holder, whom Todd identified only as W. H. Walker,[28/] happened to have 500,000 shares of UAO that he would sell Allen at the same price, 20¢ a share. Allen arranged to buy that stock and to pay for it by cashier's checks to W. H. Walker as the stock was sold through Rice at Stone Summers. On Saturday, December 7, 1968, Allen received the 500,000 shares of UAO stock, delivered by an employee of Todd's[29/] by automobile to Allen in Oklahoma City, such shares being then already in 1,000 share certificates in Stone Summers' name, in accordance with Rice's earlier instructions as to procedure in this type of situation. On the following Monday Allen delivered the stock to Rice to be sold through Registrant.

Allen had informed Rice of his proposed purchase of the Boucher Trust stock, of the problem encountered when the stock was

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28/ Allen later learned that "W. H. Walker" was an alias for Todd.

29/ Later, when Allen paid for the stock as it was sold off, he delivered the cashier's checks drawn in favor of "W. H. Walker" to this same employee of Todd's.

found to be restricted, and of his intentions to go to Dallas to see if the restrictions could be removed. This much Rice conceded in his testimony. Allen also told Rice later of the circumstances under which he acquired the UAO stock from Todd. This Rice denied, testifying that he understood from Allen that the Boucher Trust stock restrictions had been cleared up and that it was that stock which Allen had obtained. Based on observation of the witnesses and the long-standing friendship of Allen and Rice, who had known each other for some twenty years, 30/ it is concluded that the testimony of Allen on this point must be credited. However, even if Allen had not disclosed to Rice that he had gotten his 500,000 shares of UAO from Todd, the number of shares involved, together with the fact that Rice concededly knew that the Boucher Trust stock had been restricted, would have imposed on him and upon Stone Summers an affirmative duty to make suitable inquiry to verify that the stock involved was in fact freely saleable.

Allen's and Rice's testimony are also in sharp conflict on another point respecting the selling by Stone Summers of Allen's 498,000 shares of UAO. Allen testified that he and Rice made a "side" deal under which they would share equally the profits realized from the sale of Allen's UAO stock, with a view to forming a partnership to set up their own broker-dealer firm or some form of business

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30/ See footnote 36 below.

that would involve bringing prospective merger partners or acquisition prospects and potential buyers together. Allen testified that this understanding was first reached when he contemplated buying the Boucher-Trust UAO stock and continued after he got the stock instead through Todd. This so-called "side" deal was not made known to other personnel at Stone Summers and its possible existence only came to light when two Internal Revenue Service agents (who were conducting an investigation into Todd's and UAO's activities jointly with the Commission and the U. S. Postal Inspection Service) called on Allen to inquire about the fact that while he had realized $30,000 in profit on the sale of his UAO stock he only reflected $15,000 of it on his income tax returns. Allen testified further that Rice told him that he could not possibly have admitted the existence of any such side deal to the IRS agents (who later interviewed Rice) because to do so would cause him, Rice, to lose his license. The record is clear that Allen never actually paid Rice any part of the $30,000 profit and he later amended his tax returns to reflect retention by him of the full amount, after, as he put it, "Rice denied the deal". In his testimony Rice denied the existence of any side deal, though he did concede that he and Allen had from time to time discussed in general terms the possibility of going into business together. In his brief Rice urges that it is illogical to assume such an agreement by Allen since under the originally-contemplated purchase of the Boucher-Trust UAO stock Allen would have had to borrow money to

acquire the stock[31] and thus would have incurred expense and risk while Rice would have had none.[32] Further, Rice argues that Allen, though he was Rice's friend and confidant over a period of some fifteen to twenty years, is not to be believed because in 1968 he was suspended from the practice of law for commingling a client's funds with his own.[33]

Based upon observation of the witnesses and the record as a whole it is concluded that Allen's testimony is to be credited over Rice's on this point and that the two in fact had some sort of understanding for sharing profits out of the sale of Allen's UAO stock, though such sharing may have been contigent upon their going into some form of business together or in utilizing the "shared" proceeds for travel and other expenses incident to attempting to bring merger partners together or otherwise advancing common business goals.

In any event, even assuming arguendo that Rice's version of the non-existence of the "side" deal were established by the record, this would only go to the question of appropriate sanctions because, even under Rice's version of the facts as to how Allen had acquired the 500,000 shares of UAO stock, there were sufficient "red flags"

31/ As already noted, the stock Allen purchased through Todd didn't have to be paid for until it was sold off.

32/ This argument overlooks the fact that Rice was a necessary link in getting the UAO stock sold off and the profits realized.

33/ For some reason not disclosed by the record, Allen never applied for reinstatement to the practice of law following his suspension and is currently ineligible to practice.

raised to have called upon both Rice and Stone Summers to make more diligent inquiry from all appropriate sources as to the source of the stock and its free tradeability.

Instead of making appropriate inquiry, Rice and Stone Summers were satisfied by the fact that the certificates presented by Allen and Dawson had no restrictive legends and were accepted for transfer by the transfer agent (UAO). The Commission has encouraged issuers who issue securities in so-called "private offerings" to place a legend on the certificates and to issue stop-transfer instructions as a precaution against illegal distributions.[34/] However, the failure of an issuer to take such measures cannot relieve a broker-dealer of his duty as a professional in the securities business to make reasonable inquiry to assure himself that he is not participating in an illegal sale of unregistered securities.[35/] The need for further inquiry should have been particularly obvious to Rice who was very well acquainted with both Dawson and Allen[36/] (both of whom had

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34/ See Securities Act Release No. 5121 (December 30, 1970); Securities Act Release No. 4997, p. 16 (September 15, 1969).

35/ Quinn and Company, Inc., Securities Exchange Act Release No. 9062, p. 10 (January 25, 1971).

36/ Rice and Allen had been friends over a period of some 20 years and confided at least some of their business affairs and interests to each other. Occasionally Allen would refer a potential customer to Rice as indicated elsewhere herein. Allen and Rice had vague plans for going into business together. Partly through Allen, Rice came to know Dawson quite well, and paid a number of visits to Dawson's Sound Tronics offices. Rice became quite familiar with Dawson's relationship to Todd and UAO and with some of the problems that eventually led to Todd's and Dawson's "splitting the blanket."

sold UAO stock through Rice previously when he was with Hagen and Company) as well as with Todd and UAO and Sound Tronics.[37/]

Since Respondent Rice has failed to meet his burden of showing that an exemption was available for the sale of the 698,000 shares of unregistered UAO stock, it is concluded that such sales constituted wilful violations of Sections 5(a) and 5(c) of the Securities Act and that Rice wilfully aided and abetted such violations.

(3) Rice's Responsibilities as a Registered Representative.

As another defense to the charge that he wilfully aided and abetted the sale of unregistered UAO stock, Respondent Rice urges that under the procedures extant at Stone Summers it was not his responsibility to ascertain whether stock was freely tradeable or not. His job, Rice contends, was just to find a customer with some stock to sell and from there on it was out of his hands. Tom or Bob Summers, the firm's traders, or Fern Morris, the cashier, would check with the transfer agent or otherwise ascertain that the stock Rice brought in was not restricted, Rice contends. This argument has several fatal flaws.

Firstly, the record does not support Rice's contention that Tom Summers relieved Rice as a registered representative of his usual obligations to know his customers and to check out the sources of the stock. While

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37/ Through his contacts with Allen and Dawson, Rice came to know a good deal about UAO and Sound Tronics, and came to know Todd fairly well personally. Rice attended a number of meetings at which Todd was present. At one point, probably in early 1968, Rice tried (unsuccessfully) to interest Todd and his engineers in having UAO acquire Texterior Oil Company. Rice was aware that UAO was in an active acquisition program. In addition, as noted elsewhere herein, Rice also became knowledgeable about UAO through his sales of UAO stock for Dr. Farr.

Stone Summers had no written procedures manual covering the point, the Summers brothers testified that Rice had more years of experience in the securities business than either of them did and that they were satisfied that Rice was conversant with the pertinent laws and regulations and that he would carry out his obligations as a registered representative. While it was Tom Summers and Bob Summers who decided what issues the firm traded, from the standpoint of determining whether the firm could likely make some money on the stock in light of its market activity and other similar factors,[38] that fact in no way relieved Rice as a registered representative from making proper inquiry concerning the free-tradeability of particular shares of a stock that he brought into the firm for possible trading where there were factors present that put him on notice of the need for such inquiry.

Nor is it a defense for Rice to say that Tom Summers was satisfied if the stock bore no restrictive legend and was transferred into street name by the Transfer agent (particularly where UAO was its own Transfer agent) where the record shows that Rice failed to make the inquiry demanded by the circumstances to ascertain the essential facts and to apprise Tom Summers of them.[39]

Rice's duty to make further inquiry was particularly strong here where the record shows not only that he had long and close associationship with Dawson and Allen[40] but that he also was quite familiar with UAO and

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38/ Rice could not finally commit Stone Summers to purchase UAO stock from a customer or to handle it as agent. Tom or Bob Summers had to approve the proposal first.

39/ Cf. Stead v. S.E.C., 444 F.2d 713, 716 (C.A. 10, 1971), where the court states that merely calling the transfer agent was "obviously not a sufficient inquiry."

40/ See footnote 36 above.

with Todd, partly through his association with Allen and Dawson.[41] As already noted, Rice had traded UAO stock for Allen and Dawson while he was at Hagen & Co.; the record also shows that while he was with Hagen & Co. Rice ran into problems selling UAO stock for Dr. Charles H. Farr, a former officer of UAO.[42]

Secondly, on the issue of the salesman's responsibilities, the Commission's decisions make it clear that a registered representative is not relieved of Section 5(a) and 5(c) violations by reliance upon his employer.[43] Salesmen, no less than broker-dealers, should be aware of the requirements necessary to establish an exemption from the registration requirements of the Securities Act and should be reasonably certain such an exemption is available before engaging in the offer and sale of unregistered securities.[44] The Commission's decision in Mark E. O'Leary et al., supra,

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41/ See footnote 37 above.

42/ In 1967 Farr and his associates purchased 410,000 shares of UAO stock from the Nortex Co. These shares, along with a block owned by Todd, gave Farr and Todd control of UAO since they held 820,000 shares out of the 3,000,000 UAO shares outstanding. Farr and his group later got 800,000 more shares of UAO in exchange for Omni, Inc., which became another subsidiary of UAO. All of Farr's shares of UAO were restricted, but after he and Todd had a falling out the restrictions were removed and Farr sold 250,000 shares through Rice at Hagen & Co. Later Farr sold another 400,000 shares there through Rice, but these had to be repurchased after Farr learned they weren't his to sell. Farr dealt through Rice because while he was with UAO he heard Rice was interested in trading UAO stock. Rice knew that the stock he sold for Farr had previously been marked restricted and knew of Farr's association with UAO, but nevertheless made no proper inquiry to ascertain whether the stock was in fact freely tradeable. These transactions involving Farr's UAO stock are not covered by the Order for Proceeding and are relevant here only to show Rice's familiarity with UAO and his background in trading the stock without proper inquiry.

43/ Mark E. O'Leary et al., Securities Exchange Act Release No. 8361, July 25, 1968.

44/ Strathmore Securities Inc., Securities Exchange Act Release No. 8207, p. 8 (December 13, 1967); Mark E. O'Leary et al., supra. See also R. Baruch and Company, Securities Exchange Act Release No. 7932, p. 4 (August 9, 1966).

was affirmed by the United States Court of Appeals.[45/]

(4) Rice's non-reliance on legal opinions.

Lastly, Respondent Rice asserts as a defense that he relied upon the legal advice of Tom Summers and Allen.

This argument is without validity and represents but another aspect of Rice's overall attempt to evade his responsibilities as a registered representative.

Tom Summers, though a law school graduate, has never practiced law or been admitted to practice, and his expertise in the securities industry derives from his experience in that field as a trader and registered representative rather than from legal practice or legal study as such. Tom Summers could not have rendered a legal opinion on the free tradeability of the UAO shares here involved, even if Rice had given him all the necessary facts concerning the origin of the stock, which, of course, as found above, he had not. And the record contains no evidence that Tom Summers ever purported to render or convey any legal opinion as a lawyer to Rice or to anyone else respecting the subject UAO stock.

Turning to attorney Allen, he was a general-practice attorney, including divorce, damage suits, collections, etc. who neither was, nor professed to be, expert in the field of securities law.[46/] While this record does not disclose exactly when in 1968 he was suspended from the practice of law, it appears that this occurred prior to the November-December period

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45/ O'Leary et al. v. S.E.C., 424 F.2d 908 (C.A.D.C., 1970).

46/ In the early part of 1968 he "sat in" with Rice for a fee in a case involving Rice's Former broker-dealer employer; however, Rice was not a party to the proceeding.

in 1968 when Allen obtained his 500,000 shares of UAO stock from Todd and sold most of them. Of course, an attorney offering his shares of a stock for sale would hardly be the one from whom an objective opinion regarding its saleability should be solicited. In any event, the record is entirely clear that Allen never rendered a legal opinion on the saleability either of Dawson's UAO stock or of his own.

Moreover, even if Rice or Stone Summers had received legal opinions advising that the UAO stock here involved was exempt from registration, when in fact it was not, such opinions would not have exonerated Rice but could only have been taken into account in mitigation in connection with determining appropriate sanctions.[47/]

Conclusions

In general summary of the foregoing, it is concluded that in November and December of 1968 Respondent Paul L. Rice wilfully aided and abetted violations of Sections 5(a) and 5(c) of the Securities Act of 1933 in connection with the participation by Stone Summers & Company in the distribution of 698,000 shares of the common stock of United Australian Oil, Inc., as more particularly found above.

PUBLIC INTEREST

The registration requirements of Section 5 are one of the key provisions enacted by the Congress for the protection of investors, and

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47/ Mark E. O'Leary et al., supra, affirmed 424 F.2d 908 (C.A.D.C. 1970); Morris J. Reiter, 41 S.E.C. 137, 141 (1962); The Whitehall Corporation, 38 S.E.C. 259, 270 (1958).

registered representatives play an important role in ensuring that the registration requirements are complied with.

The Division of Enforcement urges that only a flat bar order will adequately protect the public, emphasizing what it regards as untruthful testimony on the part of Respondent Rice.

Although the record in this proceeding and the findings made herein would support a bar order, particularly in light of the aborted understanding Rice had with Allen for sharing in the profits that Allen might realize from the sale of his UAO stock, it is concluded that the record herein also presents certain mitigating factors that warrant imposition of a lesser sanction.

Among the mitigating factors are Respondent Rice's age, 63, and his health.[48/] In addition, the lack of effective procedures at Stone Summers for ensuring that registered representatives took proper steps to ascertain whether a stock was restricted or not made it easier for Rice to default on his obligations as a registered representative. While, as concluded above, this circumstance did not serve to free Rice of his obligations as a registered representative, it is a factor that is properly taken into account in assessing sanctions. In light of these mitigative factors and on the basis of the entire record herein it is concluded that the public interest will be adequately protected by a bar order with a provision that after one year the Respondent may apply to become employed by a broker dealer subject to effective supervision.

48/ Rice testified that he suffers from Parkinson's disease and high blood pressure and related nervous disorders, for which he was under doctor's care, and taking various medications, at the time of the hearing.

ORDER

Accordingly, IT IS ORDERED that Respondent Paul L. Rice is hereby barred from association with a broker-dealer, except that after a period of one year from the effective date of this order he may become associated with a registered broker-dealer upon a satisfactory showing to the staff of the Commission that he will be adequately supervised.

This order shall become effective in accordance with and subject to Rule 17(f) of the Commission's Rules of Practice, 17 CFR 201.17(f).

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.[49/]

David J. Markun
Administrative Law Judge

April 30, 1973
Washington, D.C.

49/ 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. Certain proposed findings and conclusions have been omitted as not relevant or as not necessary to a proper determination of the issues presented.