INITIAL DECISION RELEASE NO. 363
ADMINISTRATIVE PROCEEDING
FILE NO. 3-12943

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	:	
	:	INITIAL DECISION
THOMAS J. DUDCHIK and	:	December 5, 2008
RODNEY R. SCHOEMANN	:	

APPEARANCES: Edward G. Sullivan, William P. Hicks, and Douglas Dykhuizen for the Division of Enforcement, Securities and Exchange Commission.

Thomas J. Murphy for Thomas J. Dudchik.

Peter J. Anderson and Gregory S. Kaufman for Rodney R. Schoemann.

BEFORE: Robert G. Mahony, Administrative Law Judge.

The Securities and Exchange Commission (SEC or Commission) issued its Order Instituting Cease-and-Desist Proceedings (OIP) Pursuant to Section 8A of the Securities Act of 1933 (Securities Act) on January 30, 2008.

The OIP alleges that Respondents, Thomas J. Dudchik (Dudchik) and Rodney R. Schoemann (Schoemann), violated Sections 5(a) and 5(c) of the Securities Act, which prohibit the offer and sale of securities through the mails or in interstate commerce, unless a registration statement has been filed with the Commission or is in effect as to such securities, in connection with the sale of stock of Stinger Systems, Inc. (Stinger). As relief for these alleged violations, the Division of Enforcement (Division) seeks cease-and-desist orders and disgorgement plus prejudgment interest.

I held a three-day public hearing in Washington, D.C., during May 2008. The Division and Respondents have filed proposed findings of fact, proposed conclusions of law, and supporting briefs. I base my findings and conclusions on the entire record and on the demeanor of the witnesses who testified at the hearing.[1] I applied preponderance of the evidence as the

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[1] References in this Initial Decision to the hearing transcript are noted as "Tr. ___." References to stipulations of the parties are noted as "Stip. ___." References to the Division's exhibits are noted as "Div. Ex. ___." References to Dudchik's and Schoemann's exhibits are noted as "Dudchik Ex. ___" and "Schoemann Ex. ___," respectively. References to the parties' post-

standard of proof. See Steadman v. SEC, 450 U.S. 91, 97-104 (1981). I have considered and rejected all arguments, proposed findings, and proposed conclusions that are inconsistent with this decision.

FINDINGS OF FACT

Respondents

Dudchik, age forty-seven, resides in East Haddam, Connecticut. (Dudchik Answer at 1; Tr. 243.) Dudchik briefly attended George Washington University in Washington, D.C. Subsequently, he earned a degree in Political Science from Trinity College in Hartford, Connecticut. (Tr. 243-44.) Professionally, he served as an officer and a director for a company known as Information Architects/Alydaar (Information Architects) in the late 1980s, and he has served as a consultant to various individuals, corporations, and other organizations. (Tr. 244, 248-53.)

Schoemann, age forty-one, resides in Baton Rouge, Louisiana. (Tr. 307, 309.) Schoemann has a Bachelor's degree in Finance from New York University, a degree in business from the University of New Orleans, and two-year degrees in Accounting and Business from Delgado Community College. (Tr. 307-08.) He owned and operated an ice cream, snowball, and sandwich shop for ten years and sold it when he was twenty-nine. (Tr. 308-09.) Since then, he has supported himself by investing his money in the stock market, owning or being the beneficial owner of more than five percent of several public companies. (Tr. 308-09, 316.)

Other Relevant Entities and Persons

Stinger was incorporated in Nevada on July 2, 1996, and was previously known as United Consulting Corporation (UCC). (Stip. 11 at 1.) UCC was formed to provide consulting services to various industries at its discretion and based on the expertise of any engaged consultants. (Stip. 11 at 2.) In September 2004, Robert Gruder (Gruder) and his partner, Thomas Yates Exley (Exley), acquired UCC and changed its name to Stinger. (Stip. 11 at 2; Div. Exs. 3, 7.) Stinger began trading publicly on November 11, 2004. (Tr. 539.) Currently, Stinger manufactures electronic stun devices and other control products. (Stip. 11 at 2.)

Gruder is the President and Chief Executive Officer of Stinger and a member of the Board of Directors. (Tr. 521; Div. Exs. 4, 9.) Gruder and Dudchik were roommates in college in Washington, D.C., in the late 1970s. (Dudchik Answer at 1; Tr. 243, 541.) They also worked together at Information Architects where Gruder was the Chief Executive Officer, Dudchik was head of Communications, and they both served on the Board of Directors. (Tr. 244-45, 541-42.) They are good friends and have spoken regularly over the past twenty years. (Dudchik Answer at 1; Tr. 245-46, 541-43.) In September 2004, Gruder, on behalf of Stinger, hired Dudchik as a consultant to Stinger. His hiring was memorialized in an agreement dated October 1, 2004. (Tr.

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hearing briefs are noted as "Div. Post-Hearing Br. ___," "Dudchik Post-Hearing Br. ___," and Schoemann Post-Hearing Br. ___."

542; Div. Ex. 27.) Gruder is also a friend and business associate of Schoemann, who he met in 1995, and the two speak periodically. (Tr. 310-15, 543.)

Douglas Murrell (Murrell) resides in Austin, Texas. (Tr. 36.) Murrell has a degree in Business from Delta State University. (Tr. 37.) He worked for twenty years with New York Life Insurance Company until retiring in 1991. (Tr. 38-39.) In 1985, Murrell began a dual career, working part-time in mergers and acquisitions for a company called Austin Young. (Tr. 38-39, 41-42.) Murrell formed his own company, Capital Group Consulting, Inc. (CGC), in 1990, of which he is the President. (Tr. 39-42, 45.) His business is helping people take companies public by buying shell corporations. (Tr. 489-91.) Murrell was a consultant in the merger that resulted in Stinger. (Tr. 44, 199.)

Matt Murrell (Matt) is Murrell's son. In early 2000, at age twenty-four, he became the sole officer, director, and majority shareholder of UCC. (Tr. 198; Div. Exs. 5, 20.)

Gary Henrie (Henrie) is a Utah-based securities attorney who provided legal services for Murrell and Stinger relevant to this proceeding. (Tr. 50-51.)

A. UCC Becomes Stinger

Murrell Acquires UCC

Garrett Sutton (Sutton) formed UCC as a shell corporation that was not publicly traded. (Tr. 52-53, 362-63, 471-72, 490-91, 527-28; Div. Ex. 1.) In 1999, Murrell agreed to acquire UCC from Sutton. On April 4, 2000, UCC's Board of Directors approved the issuance of 750,000 shares to Murrell. (Tr. 49; Div. Ex. 1.) Murrell paid $8,250 for the stock, which equaled seventy-five percent of UCC's one million freely tradeable shares. (Tr. 49, 95-96, 129.) He never received physical certificates for these shares. (Tr. 106; Div. Ex. 15.) Sutton, who did not resign as the sole officer and director of UCC until May 1, 2000, retained Murrell as a consultant to UCC to find a merger candidate. (Tr. 62-63, 65; Div. Ex. 5.) This was UCC's principal business. (Tr. 49, 54.)

Matt Murrell Becomes the Majority Shareholder of UCC

In order to avoid a potential conflict of interest as a consultant to UCC, Murrell sought legal advice from Henrie as to how UCC needed to be structured. (Tr. 56-58.) Henrie understood that Murrell wanted to structure UCC on a going-forward basis to ensure that he was not an affiliate. To do that, Henrie recommended that Murrell have someone who was independent of him, was not supported by him, and did not live in his residence serve as an officer and a director.[2] (Tr. 56-57, 504.) In response to Murrell's inquiry, Henrie advised him that his children could qualify.[3] (Tr. 56-57, 70, 485-86.) Based on this advice, Murrell chose

[2] Murrell was never an officer, director, or an employee of UCC; he was only a merger consultant. (Tr. 58, 170, 199, 233.)

[3] Murrell wanted to choose one of his children because he did not feel comfortable asking others to take on the liability. (Tr. 59.)

Matt because he could trust him. He believed Matt could make independent decisions with good business sense and judgment, and Matt had a master's degree and was the most independent of his children.[4] (Tr. 56-59, 81.) Upon Murrell's recommendation, on March 14, 2000, UCC's Board of Directors issued Matt ten million UCC shares, which made him UCC's majority shareholder.[5] Matt was given the shares because there had to be an officer and a director. (Tr. 93.) On May 1, 2000, Matt became the President, Secretary, Treasurer, and sole director of UCC.[6] (Tr. 66-67, 199-201, 231-32; Div. Ex. 5.)

Matt's Educational and Professional Experience

When Matt became the owner, an officer, and the sole director of UCC, he was twenty-four years old. (Tr. 197.) After spending three years at the University of Texas in Austin, Matt transferred to Texas Tech University from where he graduated with a degree in General Studies. (Tr. 197.) Immediately after college, Matt worked for the State of Wisconsin Department of Natural Resources (DNR) as a natural resource scientist and part-time for the Shamrock Bar (Shamrock), in Madison Wisconsin. (Tr. 63, 82-84, 198.) For DNR, he worked on policy, research, and analysis relating to new laws affecting land use policy in Wisconsin and their implications concerning natural resource management. (Tr. 198.) At Shamrock, Matt was a manager with experience hiring and firing, making business decisions, and working with the owner to develop business plans for expansion and other opportunities. (Tr. 82-84, 217.) He later received a graduate degree from the University of Wisconsin in Landscape Architecture which involved training in urban and regional planning, including comprehensive planning. (Tr. 61, 217.) However, Matt had no financial analytical training other than real estate and business classes. He is not an accountant, and he does not hold any professional accreditations or certifications. He did not have any experience with mergers and acquisitions prior to UCC. (Tr. 197-98, 208, 216-17.)

Matt's Work at UCC

Matt served as the only officer and the sole director of UCC from May 2000 to September 2004 while he was taking graduate school courses and working part-time at DNR and Shamrock.[7] (Tr. 58-59, 66, 198-99, 221, 231.) During this time, Matt did not receive any pay or compensation from the corporation or his father for his work at UCC. (Tr. 58-59, 66-67, 199.) Matt's duties as President of UCC were to maintain current records of the corporation, to review

[4] One of Murrell's other children has also served as an officer and a director of a corporation for which he was a merger consultant. (Tr. 61-62.)

[5] According to the Minutes of Special Meeting of Board of Directors of UCC, the ten million shares were issued to Matt in exchange for $10,000. They were issued on March 14, 2000, about three weeks before Murrell was issued his 750,000 shares. (Tr. 200; Div. Ex. 20.) However, neither Matt nor anyone else paid for the shares. (Tr. 210-11.)

[6] Matt also served as the President of two other companies Murrell acquired from Sutton, in which he owned stock and for which he was serving as a consultant to find merger candidates—Sierra Madre and Stavenger. (Tr. 52, 63-64.)

[7] During those four years, while living in Madison, Wisconsin, Matt was financially independent of his father. (Tr. 66, 234-35.)

tax returns to be filed, to maintain any corporate minutes, and to review potential merger candidates. (Tr. 64-65, 172-73.) However, to the extent any corporate documents were needed, Henrie prepared them. (Tr. 209, 491.) Additionally, Murrell told Matt that he might be involved in shareholder meetings and board meetings; however, he was never called, nor was he ever involved in any such meetings. (Tr. 208-09, 220-21.) In fact, he did not know how many shareholders UCC had, and he never communicated with any of them other than his father. (Tr. 220-21, 239-40.) Additionally, he did not keep the corporate books and records, and he never filed any corporate records with Nevada or any other state.[8] (Tr. 211, 223-24.) He did prepare and sign tax returns that reflected no revenue; then the tax returns were reviewed by his father.[9] (Tr. 219-20.) UCC's only business was to find a merger partner, and Matt only got involved when his father presented him with a merger candidate. (Tr. 233-34.) Matt never communicated with anyone other than his father about merger candidates. (Tr. 211-12, 220.)

UCC's Search for a Merger Candidate

Murrell networked with securities attorneys, broker-dealers, transfer companies, and personal contacts to identify merger candidates for UCC. (Tr. 71.) For all candidates, Murrell reviewed and analyzed the resumes of the officers and directors, and researched their respective industries. (Tr. 73.) Murrell discussed potential merger candidates with Matt. (Tr. 65, 173, 233-34.) The amount that Murrell and Matt spoke depended on the number of active candidates. (Tr. 65-66.) Murrell would send Matt the business plan, the financials, and the resumes of the officers and directors of the candidates. (Tr. 73-74.) Murrell presented Matt with approximately fifty merger candidates, and, after discussing them, if Matt thought one was interesting or promising, he would do some independent research. (Tr. 212, 236.) Matt performed Internet research on the business and the people involved in it, their histories, and their resumes. He also researched the products of the business, their potential, and consumer interest in them; how the business was fairing in the market; and competitors. (Tr. 213-14.) His research was done primarily on Google, as well as in journals, magazines, newspapers, and press releases; it lasted from thirty minutes to twenty hours, but he never copied or downloaded his results. He felt no obligation to preserve any such records. (Tr. 213-15.) Matt did not receive documentation or correspondence from merger candidates, and he never spoke to any officers or directors of the candidates his father presented. (Tr. 212-13, 216.) According to Murrell's and Matt's testimony, any decision not to merge was made by Matt.[10] (Tr. 173-74, 236.)

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[8] Henrie controlled the UCC minute book after Matt became the sole officer and director. (Tr. 480, 503.) When he prepared UCC minutes, corporate documents, or any document that needed Matt's signature from 2000 to 2004, he delivered them to Murrell and received them back with Matt's signature. (Tr. 491.) Henrie never spoke to Matt on the phone, never mailed anything directly to him, and did not even meet him until the hearing in this matter. (Tr. 484, 491.)

[9] As Treasurer, Matt was to manage any financial situations of the company and keep records of them, but the company had no revenue, so there were no such financial situations. (Tr. 208-09.) UCC did not even have a bank account. (Tr. 219.)

[10] For example, Matt made the decision not to merge with a seafood company that initially had promise. (Tr. 236.)

UCC Merges with Electronic Defense Technology, LLC

In or about the spring of 2004, Gruder and Exley began searching for a shell company to acquire and merge with an operating company they were buying. (Tr. 525-29.) They, as the majority owners of EDT Acquisition, bought Electronic Defense Technology, LLC (EDT), a manufacturer of stun devices. (Tr. 525-27.) After not finding a shell company to merge with EDT, on September 6, 2004, Gruder hired Murrell to find a merger candidate. (Tr. 527-29; Div. Ex. 4.) Murrell was hired to locate a "clean shell" corporation, one that had no operating history, no litigation, and no public trading. He was to facilitate the shell's merger with EDT for which he would receive $75,000 and 220,000 shares of the new company created by the merger. (Tr. 530-31.) Murrell recommended UCC as the shell. (Tr. 532.) Murrell believed that Matt controlled UCC, and Matt believed that he made independent decisions on behalf of UCC with the advice of his father. (Tr. 189, 232-33.) However, all of the negotiations for the UCC/EDT merger were between Gruder and Murrell. Matt did not participate in the merger discussions or in drafting the agreement and reorganization plan for the merger. (Tr. 224-26.) Matt discussed the merger only with his father. (Tr. 149, 554.)

In September 2004, to complete the UCC/EDT merger, Henrie sent Matt corporate documents for signing. Matt would fax an executed copy to his father and return the original to him by FedEx.[11] (Tr. 109-10.) Murrell consulted with Matt about signing the merger documents, and told him that he would have to cancel his ten million shares and resign in order to complete the merger.[12] (Tr. 92-93, 109-10, 121-23, 128-29, 221, 223.) Murrell and Matt testified that Matt made the ultimate decision to do the merger; however, if Matt had not approved the merger, Murrell would not have been paid. (Tr. 149, 173, 231, 237-39.)

On September 23, 2004, Gruder acquired UCC, merged EDT into UCC, and changed its name to Stinger. (Tr. 220, 536; Div. Exs. 2, 7, 8, 9, 10, 11, 12, 13, 22.) Upon completion of the merger, Murrell received his $75,000 fee and 220,000 Stinger shares. Gruder and Exley collectively received 9,250,000 Stinger shares, and the company emerged with one million authorized shares that were not part of the restricted stock. (Tr. 534-36.) Thereafter, Matt's ten million shares of UCC were cancelled on September 24, 2004,[13] and Matt resigned as an officer and director of the company on September 25, 2004. (Tr. 91-92, 118-122, 124-25, 128-29, 230, 533-34; Div. Exs. 2, 8, 10, 12, 13.)

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[11] Matt maintained records of the transactions that he signed on behalf of UCC in his own files. (Tr. 239.)

[12] Matt was not paid for the cancellation of his shares, and he made no money as a result of the merger. (Tr. 92.) CGC eventually paid Matt $500 for the ten million shares and his time and effort over the four years he was associated with UCC. (Tr. 68, 199-200, 221-23.)

[13] Gruder and Murrell wanted a company that had ten million shares with one million shares "in the float." They knew that some shares of the corporation into which they were merging had to be cancelled. (Tr. 533-34.)

B. Dudchik's and Schoemann's Acquisition of UCC/Stinger Stock

Murrell Transfers Stock to Dudchik

In the course of the negotiations to acquire UCC, Gruder made it clear to Murrell that it was very important that three individuals, one of whom was Dudchik, receive shares of UCC stock. (Tr. 135-36.) On July 26, 2004, Murrell and Dudchik signed an agreement in which Murrell would transfer approximately 350,000 of his UCC shares to Dudchik in exchange for consultant services in relation to UCC's acquisition of EDT and for other services that may be needed during a twelve month period.[14] (Tr. 167-69, 248-50; Div. Ex. 26.) On September 23, 2004, Murrell authorized the transfer agent to issue a certificate to Dudchik for 345,000 shares of UCC stock. (Tr. 253-56; Div. Ex. 15.) Dudchik ended consulting services with Murrell after the merger in September 2004.[15] (Tr. 250.)

Murrell Sells Stock to Schoemann

Prior to acquiring UCC, Gruder approached Schoemann in late June or early July 2004 about investing in what would become Stinger. (Tr. 327-28.) Schoemann received a Stinger Subscription Agreement and a business plan from Gruder on September 8 and 9, 2004, respectively. (Tr. 329, 390-91; Schoemann Exs. 66-67.) Schoemann conducted research into the market for "taser-like" products. (Tr. 329-30.) After initially seeking a $100,000 investment for five percent of Stinger's equity, Gruder increased the amount he was seeking from Schoemann to $200,000. (Tr. 329-30.) After talking it over with his wife, on September 21, 2004, Schoemann invested $200,000 in Stinger in exchange for 561,000 restricted shares. (Tr. 329-30; Div. Ex. 37.) Schoemann received two share certificates dated October 19 and 27, 2004, for his 561,000 shares, and both were marked "RESTRICTED" on their face. (Schoemann Exs. 15-16.)

A day after he purchased his restricted Stinger shares, Schoemann inquired of Gruder where he could buy freely tradeable shares, and Gruder referred him to Murrell. (Tr. 541.) Schoemann called Murrell on September 23, 2004, which was the first time they spoke. (Tr. 132, 145, 340.) Murrell told Schoemann that he would sell him 100,000 Stinger shares for $100,000, but no agreement was reached. (Tr. 341-42.) In a second call that day, Murrell and Schoemann agreed on $0.75 per share for the 100,000 shares. Schoemann then drafted an agreement, dated September 23rd, and faxed it to Murrell that day and again on September 24th, for his signature. (Tr. 142, 388.) Murrell returned an executed copy of the agreement by facsimile, and the original by FedEx, to Schoemann on September 30 or October 1, 2004. Schoemann did not receive the executed agreement until October 2 or 4, 2004.[16] (Tr. 142-43,

[14] Dudchik was never an officer, director, or consultant of UCC, and he was never in any position of control with UCC or Stinger. (Tr. 170-71, 288, 544-45.)

[15] As of October 1, 2004, Dudchik also consulted for Stinger. He provided camera technology for a stun gun and searched for a company to manufacture it. (Tr. 251-52, 542, 545; Div. Ex. 27.) In exchange for his services, Dudchik received 400,000 restricted shares of Stinger stock, valued at approximately $160,000. (Tr. 256-58, 287; Div. Ex. 27.)

[16] Murrell testified that he and Schoemann did not reach an agreement on September 23, 2004, because he did not sign off on it on that date. (Tr. 183.) The agreement also included a six-

388-89, 403.) The agreement between Murrell and Schoemann states that Schoemann purchased "One Hundred Thousand (100,000) freely tradeable shares of United Consulting, Inc., that next week will be changed to Stinger Systems, Inc . . . ." However, Schoemann believed he was buying Stinger shares prior to the official name change. (Tr. 346; Div. Ex. 16.) Schoemann paid Murrell by check dated September 29, 2004.[17] (Tr. 184-85, 353-54; Div. Exs. 16, 38.) The memo line on Schoemann's check reads: "9/23/04 Stock Purchase Agreement With Option 100,000 Free Tradeable Stinger Systems, Inc., & 100,000 options." (Tr. 338, 389-90; Div. Ex. 38.) Murrell received the check on September 30, 2004. (Tr. 184-85.) In a letter "To Whom It May Concern," dated September 23, 2004, Murrell directed UCC's transfer agent to issue Schoemann a certificate for 100,000 shares.[18] (Tr. 130-31; Div. Ex. 15.)

Murrell's Non-disclosures Regarding Matt; Dudchik's and Schoemann's Due Diligence

Murrell never told Dudchik or Schoemann that Matt was twenty-four years old and was the sole officer, director, and control person of UCC. Nor did he tell them that Matt did not pay for his ten million shares of UCC and did not receive any salary or compensation. Further, he did not tell them that Matt had no contact with merger candidates. Prior to their stock purchases, Murrell did not recall if either Dudchik or Schoemann asked who controlled the company. Murrell also did not remember if either asked who were the officers, directors, or majority shareholders of UCC. They did not ask how much stock the majority shareholders owned and what they paid for it; nor did they seek information about the compensation of the officers and directors. He also did not recall if either of them ever asked to speak to an officer or director, and neither ever inquired about the age, experience, or education level of any officers or directors of UCC, or their sources of income. (Tr. 158-65, 295-96.)

Dudchik understood that Murrell was a consultant to UCC, and he never believed Murrell controlled either UCC or Stinger. (Tr. 278, 289.) In 2004, Dudchik did not have any information about how UCC was structured or have any involvement with it. He did not have

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month option for Schoemann to purchase an additional 100,000 shares from Murrell for $3.00 per share plus fifty percent of any profit made on that stock sold above $3.00 per share. (Tr. 354-55; Div. Ex. 16.) On November 11, 2004, Schoemann and Murrell agreed to cancel the option portion of the September 23, 2004, agreement upon the completion of Schoemann's purchase of additional Stinger stock from the Sutton Law Firm Center Client Trust Account. (Tr. 165-66, 370-72; Div. Ex. 62.)

[17] Schoemann agreed to send Murrell the check on September 28, 2004, because he was uncertain if he wanted to go through with the deal and needed some time to think. (Tr. 143-44, 353-54.)

[18] Murrell testified that he instructed the transfer agent to transfer the shares to Schoemann on September 23, 2004, because he wanted the transaction to occur and because he needed the money. (Tr. 133, 145.) However, Murrell testified that he understood that he did not have a deal until he and Schoemann signed the agreement and the money was in his bank; that was his standard operating procedure. (Tr. 184.) Murrell also believed it was possible that the letter could have been prepared later than September 23, 2004. (Tr. 187-88.) Dudchik was also referred to in the letter, and Murrell requested a certificate be issued for his 345,000 shares. (Div. Ex. 15.)

contact with anyone acting on behalf of UCC, but he understood UCC's purpose was to find a merger candidate. (Tr. 278-79, 295.) He did call Henrie to inquire if he could obtain shares from Murrell, and Henrie informed him that he could. (Tr. 518-19.) During their discussions, Murrell told Dudchik that the shares were freely tradeable, but Dudchik did not ask Murrell for other information to ensure that this was true. (Tr. 177-78, 295.)

Schoemann does his own research for investment decisions. (Tr. 400.) He asked Murrell how long he had held his UCC stock. Murrell told him four years, and they agreed it was freely tradeable.[19] (Tr. 343-44.) However, Schoemann did not ask Murrell if he played any role in the operations of UCC, nor did Schoemann perform any additional research to check Murrell's background. (Tr. 344.) As a general practice, when he knew at least one person running a company, Schoemann would receive a business plan prior to making an investment of one to five percent, and then he would conduct additional research by looking at other companies in the industry. (Tr. 322.)

He did not learn who was running Stinger until after he made his investment.[20] (Tr. 330.) In fact, at the time of his investment, Schoemann did not have any understanding of what UCC was, and he did not inquire of anyone to find out. (Tr. 348.) He did learn from Stinger's business plan that there would be a merger with a shell company, but he testified that he did not know the shell was UCC. (Tr. 348-49.) On October 4, 2004, Schoemann sent the certificate representing the 100,000 shares he purchased from Murrell to his broker, E*Trade, for deposit into his account. (Tr. 385, 387.) Schoemann assumed that E*Trade would only deposit his certificate into his account after it conducted its own due diligence and was satisfied that the stock was freely tradeable. (Tr. 387.)

C. Trading Dudchik's and Schoemann's UCC/Stinger Shares

Murrell's UCC/Stinger Stock

When Gruder approached Murrell about acquiring UCC, Murrell had held his 750,000 shares for four years and considered them to be freely tradeable based on the advice of his securities attorney. (Tr. 105-06.) In addition to holding the it for four years, Murrell believed his stock was free trading because he was not an officer or director and he had a legal opinion from a securities attorney. He also believed that Matt was an independent person making decisions for UCC. (Tr. 191-92.)

Henrie's Opinion Letters

On or before October 1, 2004, Murrell asked Henrie for a legal opinion as to the tradeability of the shares he sold to Dudchik and Schoemann. (Tr. 472-73.) Henrie subsequently

[19] Murrell did not tell Schoemann anything else. (Tr. 352.)

[20] Schoemann testified that he did not make his investment until after the company became Stinger but before its official name change. (Tr. 345-46.) Murrell held the same belief. (Tr. 188.)

provided an opinion letter to Stinger's (formerly UCC's) transfer agent, Colonial Stock Transfer (Colonial),[21] dated October 1, 2004, stating the following:

> The information indicates that the Shares were not registered pursuant to Section 5 of the Securities Act so that the Shares were "restricted securities" within the meaning of Rule 144(a)(3). Consequently, the Shares may be sold without registration under the Securities Act pursuant to Rule 144 promulgated thereunder if each of the conditions of Rule 144 is satisfied.
>
> Subparagraph (k) of Rule 144 allows that the Shares may be sold without any restriction under Rule 144 if the Shares are sold for the account of a person who is not an affiliate of the Company at the time of the sale and has not been an affiliate during the preceding three months, provided a period of at least two years has elapsed since the latter of the date the securities were acquired from the Company or from an affiliate of the Company.
>
> . . .
>
> Mr. Murrell was not an affiliate of the Company at the time he transferred the Shares and none of the recipients are affiliates of the Company. Accordingly [sic] to the transfer rules of Rule 144, the recipients from Mr. Murrell received the same holding period for the Shares that Mr. Murrell had going back to July 4, 2000.
>
> [I] am of the opinion that the shareholders who received stock from Mr. Murrell have shares that are not subject to the resale limitations of Rule 144.[22]

(Div. Ex. 46.) In preparing this opinion letter, Henrie reviewed UCC's corporate documents which indicated that Matt was UCC's majority shareholder and sole officer and director.[23] (Tr. 481-82.) As a result of Matt's status, he concluded that the company could not do anything without Matt's approval and signature. He further concluded that Murrell was not an affiliate of UCC.[24] (Tr. 486-87.) Henrie looked to Murrell for substantive information for his opinion,

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[21] Henrie sent the letter to Colonial, knowing that it might rely on it. It was his understanding, at the time he sent the letter, that the transfers referenced on the third page had already occurred. (Tr. 487-89.)

[22] Henrie did not know if anyone paid him for rendering this opinion letter, but he would have looked to Murrell, who was his client at the time, for payment. Stinger and Gruder became clients of his in November 2004, but did not pay him for this opinion. (Tr. 467-70, 473.)

[23] When determining whether someone is an affiliate under Rule 144, Henrie initially looks to see if the person in question is an officer, director, or ten percent shareholder, and then he looks to see if the person is a key employee or in some other way can control the corporation. He did this for UCC and Stinger. (Tr. 480-81.)

[24] Henrie understood that the merger could not have been completed without Matt's approval, agreement, and execution. (Tr. 516.)

including whether or not Murrell was an affiliate.[25] (Tr. 478.) Specifically, he learned that Matt was a college graduate, had moved away from home, and was self-supporting. (Tr. 484-85.) This information led him to the conclusion that Matt was independent.[26] (Tr. 504.) Henrie never spoke with Matt in the process of formulating his opinion, and he relied on Murrell's oral representations in regards to Matt's independence. It never occurred to him to interview Matt to determine independently that Matt had the control Murrell suggested. (Tr. 479, 484, 487.) He did not know that Matt had no role in the merger discussions and negotiations with Gruder; but it would not have been important for him to know that Matt was not involved in the merger negotiations if he made the final decision. (Tr. 491-92.) Henrie testified that, but for the fact that Matt owned ten million shares of UCC, Murrell would have been an affiliate.[27] (Tr. 499.)

On November 8, 2004, Henrie issued a second opinion that was posted to the Pink Sheets to the effect that Stinger shares were freely tradeable. (Tr. 517-18.) Previously, on October 1, 2004, Colonial issued certificates to Dudchik and to Schoemann for 345,000 and 100,000 shares of Stinger, respectively. (Div. Exs. 15, 35, 57.)

D. Public Sales of Stinger Stock

Stinger Did Not File a Registration Statement with the Commission until February 7, 2005

After the merger, the corporate structure of Stinger authorized ten million shares of stock for Gruder and his company management. (Tr. 98-99.) Gruder became President of Stinger in September 2004, and he still holds that position. (Tr. 521.) The company began trading publicly on November 11, 2004. (Tr. 539.) Gruder intended to file a registration statement for the company immediately; however, no registration statement for Stinger was filed with the Commission until February 7, 2005. (Tr. 99, 269, 539; Stip. 9; Div. Ex. 54.)

Stinger Finds a Market Maker

After a broker-dealer in California declined to make a market in Stinger stock, Gruder had Murrell contact James T. Mathis (Mathis) with First Southwest Company (First Southwest) in Dallas, Texas. (Tr. 151-53.) Mathis, a supervisor of First Southwest's trading desk, made the decision to make a market in Stinger stock. (Tr. 432-33.) However, with respect to restricted

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[25] Sutton also provided Henrie with information for his opinion letter. (Tr. 478.) Henrie learned from Murrell and Sutton that Murrell was a consultant for UCC to find a merger partner from 2000 to 2004. (Tr. 489, 505-06.) Henrie also knew that Murrell would be bringing potential merger candidates to Matt for his consideration and advising Matt as to the appropriateness of those candidates. (Tr. 505-06.) He was never privy to the conversations between Murrell and Matt, so he did not know if Murrell was instructing Matt on what to do for UCC; however, he believed Matt acted independently. (Tr. 515, 519.) Murrell had a past regulatory incident of which he did not inform Henrie; Henrie would have liked to have known about it. (Tr. 194-95, 490.)

[26] Henrie knew Matt had a college degree, but he did not recall discussing if Matt had any business experience. (Tr. 504-05.)

[27] Matt never sold or attempted to sell any of his UCC stock. (Tr. 67.)

securities, First Southwest retained the right, in its sole discretion, to "require that such securities not be sold or transferred until they clear legal transfer." (Tr. 455-56; Div. Ex. 29 at 6.) Additionally, in order to make a market in an unregistered stock, First Southwest required financial statements to be on file, but they did not have to be audited. (Tr. 432.)

Murrell had Mathis contact Henrie regarding the preparation of Stinger's Rule 15c2-11 information.[28] (Tr. 153.) Mathis verified that a 15c2-11 form was filed for Stinger prior to the beginning of trading, and he relied on the information to post the quotes.[29] (Tr. 424-25, 427.) He completed the Pink Sheets form, indicating that the securities were exempt under Rule 144(k), and he sent it to First Southwest's legal department, from whom he received no response, prior to sending it to the Pink Sheets. (Tr. 457-59.) Mathis called Henrie to determine the tradeability of Murrell's and Dudchik's Stinger shares,[30] which had no legend or any other restrictions on the certificates. Henrie indicated they were freely tradeable and exempt under Rule 144(k). (Tr. 441-42, 456-57.) Mathis took Henrie's oral opinion at face value and also relied on Henrie's written opinion letters. (Tr. 443-44.) On November 11, 2004, First Southwest entered the first quote on the Pink Sheets and executed the first public trade of Stinger stock. (Tr. 420, 424, 539.)

Dudchik's Sales

Dudchik understood the shares he acquired from Murrell to be free trading. (Tr. 279.) The certificate for his 345,000 shares did not bear a restrictive legend. (Tr. 279-80; Div. Ex. 35.) He read Henrie's opinion letters and spoke to Henrie prior to November 2004, and he understood that the shares were freely tradeable. (Tr. 280-82.) In early October 2004, Gruder referred Dudchik to First Southwest to open a trading account. (Tr. 260, 420-21.) Dudchik understood that First Southwest was obligated to make sure that the shares placed on deposit were able to be traded. He spoke to Mathis who, after conferring with First Southwest's attorneys, informed him that the shares were freely tradeable. (Tr. 285-86, 459.) During the first week of public trading, from November 12 to November 19, 2004, Dudchik sold 81,400 of his Stinger shares obtained from Murrell, through his First Southwest account, generating net proceeds of $865,935. (Tr. 265-67; Stips. 1, 8; Div. Exs. 33-34, 48.)

Schoemann's Sales

On November 12, 2004, Schoemann knew that Stinger had begun publicly trading. (Tr. 376.) From November 12 to November 22, 2004, Schoemann sold the 100,000 Stinger shares purchased from Murrell, through his E*Trade account, generating $967,901. (Tr. 376-78, 397-98; Stips. 2, 4, 6; Div. Exs. 47, 51, 53.) The certificate for his 100,000 shares did not bear a

[28] Securities Exchange Act of 1934 Rule 15c2-11 requires brokers or dealers to have certain documents and information in their records prior to publishing any quotation for a security. 17 C.F.R. § 240.15c2-11 (2008).

[29] Henrie prepared the information for the Pink Sheets, and he submitted it and caused it to be posted on the Pink Sheets. (Tr. 154, 493, 499-500, Stips. 11-12; Div. Ex. 43; Schoemann Ex. 3.)

[30] On the required First Southwest forms, Dudchik and Murrell both indicated that they were not affiliates of Stinger, and Mathis relied on this account documentation. (Tr. 442-43.)

restrictive legend. (Div. Ex. 57.) He relied on E*Trade depositing his 100,000 share certificate into his account in making the decision to sell the shares. (Tr. 387-88.) He also reviewed Henrie's November 8, 2004, opinion letter included in the 15c2-11 materials published in the Pink Sheets prior to trading the stock, and there was nothing in it that gave him concern that his shares were not freely tradeable. (Tr. 395-96, 404.)

DISCUSSION AND CONCLUSIONS

Paragraphs II.C.13, II.C.14, and II.C.15 of the OIP allege that, from November 11, 2004, through November 24, 2004, Dudchik and Schoemann violated Sections 5(a) and 5(c) of the Securities Act by offering to sell, selling, and delivering after sale to members of the public, Stinger stock when no registration statement was filed or in effect and no exemption from registration was available.

Section 5(a) of the Securities Act provides:

> Unless a registration statement is in effect as to a security, it shall be unlawful for any person, directly or indirectly—
> (1) to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to sell such security through the use or medium of any prospectus or otherwise; or
> (2) to carry or cause to be carried through the mails or in interstate commerce, by any means or instruments of transportation, any such security for the purpose of sale or for delivery after sale.

15 U.S.C. § 77e(a) (2008). Section 5(c) of the Securities Act provides:

> It shall be unlawful for any person, directly or indirectly, to make use of any means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell or offer to buy through the use or medium of any prospectus or otherwise any security, unless a registration statement has been filed as to such security, or while the registration statement is the subject of a refusal order or stop order or (prior to the effective date of the registration statement) any public proceeding or examination under section 8.

15 U.S.C. § 77e(c) (2008). The purpose of the registration requirement, and the Securities Act as a whole, is to "protect investors by promoting full disclosure of information thought necessary to informed investment decisions." SEC v. Ralston Purina Co., 346 U.S. 119, 124 (1953).

A prima facie case for a violation of Section 5 of the Securities Act is established by showing that: (1) no registration statement was in effect or filed as to the securities; (2) a person, directly or indirectly, sold or offered to sell the securities; and (3) the sale was made through the use of interstate facilities or the mails. See SEC v. Cont'l Tobacco Co. of S. Carolina, Inc., 463 F.2d 137, 155 (5th Cir. 1972). A showing of scienter is not required. See SEC v. Universal Major Indus. Corp., 546 F.2d 1044, 1047 (2d Cir. 1976).

The Division has presented a prima facie case here, and both Dudchik and Schoemann concede as much. (Dudchik Post-Hearing Br. 9; Schoemann Post-Hearing Br. 15.) Thus, the burden shifts to Respondents to prove the availability of any exemptions. See Ralston Purina, 346 U.S. at 126. Exemptions from registration are affirmative defenses that must be proved by the person claiming the exemptions. See Swenson v. Engelstad, 626 F.2d 421, 425 (5th Cir. 1980) (collecting cases); Lively v. Hirschfeld, 440 F.2d 631, 632 (10th Cir. 1971) (collecting cases). Claims of exemption from the registration provisions of the Securities Act are construed narrowly against the claimant. See SEC v. Murphy, 626 F.2d 633, 641 (9th Cir. 1980) (citing SEC v. Blazon Corp., 609 F.2d 960, 968 (9th Cir. 1979)); Quinn & Co. v. SEC, 452 F.2d 943, 946 (10th Cir. 1971) (citing United States v. Custer Channel Wing Corp., 376 F.2d 675, 678 (4th Cir. 1967)). "Evidence in support of an exemption must be explicit, exact, and not built on mere conclusory statements." Robert G. Weeks, 56 S.E.C. 1297, 1322 (2003) (citing V.F. Minton Securities, Inc., 51 S.E.C. 346, 352 (1993)).

A. Section 4(1) Exemption

Dudchik and Schoemann claim that their sales of Stinger stock were exempt under Section 4(1) of the Securities Act. (Dudchik Post-Hearing Br. 11-12; Schoemann Post-Hearing Br. 15-22.) Section 4(1) exempts from the registration requirements "transactions by any person other than an issuer, underwriter, or dealer." 15 U.S.C. § 77d(1). The intent of Section 4(1) is "to exempt routine trading transactions between members of the investing public and not distributions by issuers or the acts of others who engage in steps necessary to those distributions." Owen V. Kane, 48 S.E.C. 617, 619 (1986), aff'd, 842 F.2d 194 (8th Cir. 1988).

The Division argues that Dudchik and Schoemann are statutory underwriters. (Div. Post-Hearing Br. 14.) Section 2(a)(11) of the Securities Act defines "underwriter" to include "any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security . . . ." 15 U.S.C. § 77b(a)(11). Section 2(a)(11) further defines "issuer" to include "any person directly or indirectly controlling or controlled by the issuer . . . ." Id. "A control person, such as an officer, director, or controlling shareholder, is an affiliate of an issuer, and is treated as an issuer when there is a distribution of securities." SEC v. Cavanagh, 155 F.3d 129, 134 (2d Cir. 1998). An "affiliate of an issuer" is "a person that directly, or indirectly through one or more intermediaries, controls, or is controlled by, or is under common control with, such issuer." 17 C.F.R. § 230.144(a)(1) (2008).

"Control" is defined as "the possession, direct or indirect, of the power to direct or cause the direction of the management and policies of a person, whether through the ownership of voting securities, by contract, or otherwise." 17 C.F.R. § 230.405. "The affiliate inquiry is based on the totality of the circumstances, 'including an appraisal of the influence upon management and policies of a corporation by the person involved.' Affiliates are most often officers, directors, or majority shareholders—people who exercise control and influence over the company's policies or finances." SEC v. Freiberg, No. 2:05-CV-00233PGC, 2007 WL 2692041, *15 (D. Utah Sept. 12, 2007). Courts have looked to whether or not the person in question was capable of obtaining the required signatures of the issuer and its officers and directors on a registration statement. See SEC v. Lybrand, 200 F. Supp. 2d 384, 395 (S.D.N.Y. 2002) (quoting Cavanagh, 1 F. Supp. 2d 337, 366 (S.D.N.Y. 1998)). The Division's position hinges on the

contention that Murrell was an affiliate of UCC, and, as such, a statutory issuer. (Div. Post-Hearing Br. 14.)

Murrell Was an Affiliate of UCC

I find that Murrell was an affiliate of UCC as he controlled the company through his son, Matt. On April 4, 2000, the UCC Board of Directors issued Murrell 750,000 UCC shares for $8,250. This was part of the arrangement for Murrell to acquire UCC from Sutton. However, in order to create the appearance that he was not a control person and an affiliate of UCC, and based on the advice of Henrie, Murrell, who was retained by Sutton as a consultant, on March 14, 2004, had UCC issue ten million shares to Matt without cost, making him the majority shareholder. This was about three weeks before Murrell was issued his shares. Thereafter, on May 1, 2004, Matt became the sole officer and director of UCC.

Prior to joining UCC, Matt, a twenty-four year-old college graduate with a degree in General Studies, had no actual experience performing the duties of an officer and director of a public company or with mergers and acquisitions, which was the sole business of UCC. This lack of experience was reflected in the actual work Matt performed for UCC. Specifically, Matt was tasked with few duties, such as maintaining corporate records and minutes, preparing tax returns, and reviewing potential merger candidates, for which he received no compensation. In fact, Matt did not maintain the records and minutes, and he did not communicate with anyone other than his father about the business. Any work he did, such as preparing and signing tax returns, which was reviewed by Murrell, was essentially no work at all, since the company had no revenues.

Murrell also informed Matt that he might be involved with board meetings which meant that he would be meeting with himself as the sole officer and director. He never attended shareholder meetings and, in fact, did not know how many shareholders UCC had. Matt evaluated a merger candidate only when Murrell presented him with one. After discussing a candidate with his father, if he thought it had potential, Matt conducted independent research on the company. However, Matt's research was primarily done through Google searches, it was not documented, and it did not include any conversations or correspondence with the candidates or their officers or directors. The testimony establishes that Matt made the final decision whether or not to merge with a company. For example, he decided against merging with a seafood company and decided in favor of merging with EDT, which is the only one he ever approved out of about fifty Murrell presented. Matt, Murrell, and Henrie testified that the merger would not have happened if Matt did not sign off on it. Dudchik and Schoemann rely on this testimony to establish Matt's independence.[31] (Dudchik Post-Hearing Br. 11-12; Schoemann Post-Hearing Br. 22.)

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[31] Henrie's opinion that Matt was the control person of UCC was based on the corporate documents and information provided by Murrell. He never spoke with Matt in formulating his opinion and he was never privy to any conversations between Murrell and Matt to verify Murrell's representations. See V.F. Minton, 51 S.E.C. at 352 (finding an attorney's letter opinion that an unregistered sale of securities qualified for the Rule 144(k) exemption unpersuasive when the attorney relied upon and essentially restated the representations and

However, the extent of Matt's involvement in UCC's merger with EDT was very limited. Matt had no involvement in the merger negotiations, which were between Gruder and Murrell, and he had no involvement in drafting any of the merger documents; he simply signed and returned them to his father as he was instructed. As a condition of approval of the merger, and to ensure that his father got paid, he agreed to cancel his ten million UCC shares and resign as the sole officer and director for which he received no consideration at the time. The evidence conclusively establishes that Murrell possessed the power to direct or cause the direction of the management, policies, and decisions of UCC with respect to the EDT merger notwithstanding Matt's titles and shareholdings. Thus, Matt was a figurehead of UCC installed to facilitate the business of his father. For his service, Murrell's company, CGC, eventually paid Matt $500.

Dudchik and Schoemann Acquired UCC Shares from Murrell with a View toward Distribution

"Individual investors who are not professionals in the securities business may be 'underwriters' within the meaning of that term as used in the Securities Act if they act as links in a chain of transactions through which securities move from an issuer to the public." Quinn and Co., Inc., 44 S.E.C. 461, 464 (1971). "A sale by the intermediary in such a distribution is a transaction by an underwriter and thus not exempt from registration under Section 4(1)." John A. Carley, Securities Act Release No. 8888 (Jan. 31, 2008), 2008 SEC LEXIS 222, *26-27. To hold otherwise, public distributions could be effected easily without registration and other protections afforded by the securities laws. See Quinn, 44 S.E.C. at 465.

"[T]he key to whether stock is purchased for investment lies in consideration of the totality of the circumstances in light of the object and purposes of the Securities Act." Lewis v. Ling, 353 F. Supp. 241, 244 (S.D.N.Y. 1973). "There must be some indicia that the motivation of the original sale was to evade the requirement for registration." Id. at 245. Investment intent is properly determined by what was done rather than what was said. See id. "The duration that shares have been held is always recognized as relevant to investment intent." Id. at 246 n.12; see also, SEC v. Computronic Indus. Corp., 294 F. Supp. 1136, 1139 (N.D. Tex. 1968).

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opinions of interested parties). Furthermore, the record shows that Murrell was not entirely forthright with Henrie as he did not tell Henrie that Matt had no role in the merger discussions or that he, Murrell, had a past regulatory incident, both of which Henrie would liked to have known. Dudchik also suggests that Mathis's/First Southwest's opinion that Murrell was not an affiliate is significant. This argument is also flawed in that Mathis relied on Henrie's oral and written opinions and representations, including the 15c2-11 information Henrie provided to the Pink Sheets, all of which Henrie prepared based on information provided by Murrell with little investigation of his own. It is important to note that, in his April 9, 2008, Motion for Summary Disposition (Motion), Schoemann represents, "There are facts suggesting that from May 1, 2000 to September 24, 2004, despite positions held by Matt Murrell, Doug Murrell effectively controlled UCC," contrary to his current position that Murrell was not an affiliate of the company. (Motion at 6.)

Sales by Dudchik

The chain of events establishes that Dudchik had a long-standing friendship and prior business relationship with Gruder. Gruder made it clear to Murrell that it was very important that Dudchik receive shares of UCC stock. On July 26, 2004, Murrell and Dudchik entered into an agreement in which Murrell agreed to transfer approximately 350,000 of his UCC shares to Dudchik. On this date, Murrell was an affiliate of UCC. Thereafter, on September 23, 2004, the transfer agent was directed to issue the stock certificates, which was the same day of the merger when UCC became Stinger. After the merger, Dudchik sold his Stinger shares during the first week of public trading in November 2004. These quick sales clearly establish his intent not to hold the stock for investment. Dudchik attempts to minimize this selling pattern by stating that he sold less than a quarter of his unrestricted shares. (Dudchik Post-Hearing Br. 12.) However, the sales of 81,400 shares is a significant amount and fails to establish that he had acquired the Stinger shares for investment purposes. Further, there is evidence that the motivation of the original sale was to evade the requirement for registration in order to make a market in Stinger to benefit Gruder, as he was a very close, long-time friend and business associate of Gruder. Thus, Dudchik acquired the shares from an affiliate with a view toward distribution, making him a statutory underwriter. His sales constituted an unregistered distribution for which no exemption was available which was a violation of Sections 5(a) and (c) of the Securities Act. See SEC v. M & A West, Inc., 538 F.3d 1043, 1049 (9th Cir. 2008) (finding individual was a statutory underwriter for purchasing stock from affiliates of companies as of the dates on which the transactions were agreed).

Sales by Schoemann

The formation of a contract, including for the purchase or sale of securities under the Exchange Act, is dependent upon the purchaser and seller coming to a meeting of the minds (i.e., mutual assent to the terms of the transaction). See Northland Capital Corp. v. Silver, 735 F.2d 1421, 1427-28 (D.C. Cir. 1984) (holding there was no mutual assent for a securities transaction when no agreement on the terms was reached and a closing, contemplated by the parties as necessary for the deal, did not occur).

Schoemann contends that no agreement was achieved because he and Murrell never had a meeting of the minds.[32] (Schoemann Post-Hearing Br. 19.) The Division cites Empro Mfg. Co. v. Ball-Co Mfg., Inc., 870 F.2d 423 (7th Cir. 1989), for the proposition that intent (the state of mind of the parties to an agreement) is objective. (Div. Post-Hearing Br. 20.) Schoemann attempts to distinguish the agreement in Empro which was based on a letter of intent that one of the signing parties unsuccessfully attempted to enforce. (Schoemann Post-Hearing Br. 19.) Schoemann's distinction fails, however, because the court in Empro did not enforce the letter of intent because it was subject to several conditions and, ultimately, "a formal, definitive Asset Purchase Agreement signed by both parties." Empro, 870 F.2d at 424. "'[I]ntent must be determined solely from the language used when no ambiguity in its terms exists.'" Id. at 425 (collecting cases).

[32] In his Motion, Schoemann represents, "On September 23, 2004, Mr. Schoemann entered into an agreement with Murrell to buy 100,000 shares of UCC." (Motion at 3.)

Murrell and Schoemann agreed on the terms for the 100,000 share sale after their second phone conversation on September 23, 2004. This was a day or two after Schoemann purchased restricted UCC/Stinger shares. Schoemann drafted and faxed the agreement to Murrell that same day. The agreement states that it is "being executed this 23rd day of September 2004." The executed agreement has a handwritten notation of "9/23/2004" next to the signature of Schoemann, and I find that the date is in the same handwriting as Schoemann's signature. Further, the memo line on Schoemann's September 29, 2004, check refers to the "9/23/04 Stock Purchase Agreement . . . ." Murrell testified that the agreement was not executed when he received it from Schoemann, and that he did not execute and return it to Schoemann until September 30 or October 1, 2004. However, the document indicates a date of execution, which is the evidence I credit. Therefore, I do not credit Murrell's testimony that the agreement was not executed and dated by Schoemann when he received it.

Thereafter, in a November 11, 2004, letter to Murrell, Schoemann explicitly refers to the "September 23, 2004 agreement." The November letter uses the same format as the agreement in that it states that it "is being executed this 11th day of November 2004," is executed by both parties, and has a handwritten notation of "11/11/04" next to Schoemann's signature. A second date of "11/12/04" also appears on the signature line next to Murrell's signature. Lastly, in a letter to UCC's transfer agent, dated September 23, 2004, Murrell indicates that he transferred 100,000 shares of UCC to Schoemann for consideration and requests that the appropriate certificate be issued to him.

No ambiguity exists in Schoemann's and Murrell's agreement; there are no contingencies, and there is no evidence that a subsequent agreement would supersede the Stock Purchase Agreement With Option. The evidence conclusively establishes Schoemann and Murrell entered into their agreement on September 23, 2004. Accordingly, I find that, as of that date, Schoemann was a statutory underwriter. See M & A West, 538 F.3d at 1049 (finding individual was a statutory underwriter for purchasing stock from affiliates of companies as of the dates on which the transactions were agreed).

Schoemann, like Dudchik, acquired these shares of UCC/Stinger from Murrell, an affiliate of UCC, with a view toward distribution that does not qualify for an exemption from registration. Schoemann sold the shares he purchased from Murrell during the first two weeks of public trading; these sales are clearly indicative of his intent not to hold the stock for investment. Additionally, he specifically purchased the shares from Murrell in an attempt to obtain freely tradeable shares after he had made a substantial investment in Stinger by purchasing restricted shares. Like Dudchik, there is evidence that the motivation of the original sale was to evade the requirement for registration in order to make a market in Stinger to benefit Gruder, as Schoemann was also a friend and business associate of Gruder. Therefore, Schoemann's sales were an unregistered distribution in violation of Sections 5(a) and 5(c) of the Securites Act.

B. Rule 144 Safe Harbor

Dudchik and Schoemann also claim that their sales of Stinger stock were exempt under Rule 144 of the Securities Act. (Dudchik Post-Hearing Br. 9-11; Schoemann Post-Hearing Br. 22-23.) Rule 144 provides a non-exclusive safe harbor for the unregistered resale of restricted

and other securities held by affiliates of an issuer. The rule sets forth specific standards that, if met, permit persons who hold such securities to sell them publicly without being deemed "underwriters" under Section 2(a)(11) of the Securities Act and in reliance on the Section 4(1) exemption from registration. See Lybrand, 200 F. Supp. 2d at 393-94. At the time of Dudchik's and Schoemann's sales, Rule 144(d)(1)(ii) required that "[a] minimum of one year must elapse between the later of the date of the acquisition of securities from the issuer or from an affiliate of the issuer, and any resale of such securities in reliance on this section for the account of either the acquirer or any subsequent holder of those securities." 17 C.F.R. § 230.144(d)(1) (2007). At the time of Dudchik's and Schoemann's sales of Stinger stock, Rule 144(k) provided:

> The requirements of paragraphs (c), (e), (f) and (h) of this section shall not apply to restricted securities sold for the account of a person who is not an affiliate of the issuer at the time of the sale and has not been an affiliate during the preceding three months, provided a period of at least two years has elapsed since the later of the date the securities were acquired from the issuer or from an affiliate of the issuer.

17 C.F.R. § 230.144(k) (2007).[33]

As discussed above, Dudchik and Schoemann both acquired their UCC/Stinger shares from an affiliate of an issuer, Murrell. Accordingly, their sales of Stinger stock must satisfy the requirements established by Rule 144. Dudchik acquired his shares from Murrell no later than September 23, 2004, and sold them less than two months later. This amount of time is not sufficient to meet the one and two-year holding periods of Rule 144(d) and Rule 144(k), respectively. Thus, Dudchik cannot claim the Rule 144 safe harbor exempted his sales from registration. For Schoemann, the analysis is identical, except that the holding periods are calculated not from the date of acquisition, but from the date "the full purchase price or other consideration is paid or given by the person acquiring the securities from the issuer or from an affiliate of the issuer." 17 C.F.R. § 230.144(d)(1) (2007).

Despite this adjustment, Schoemann's sales are still not exempt as he paid the full purchase price to Murrell on September 29, 2004, also only a little more than a month prior to his sales. Dudchik and Schoemann further contend that they can tack the holding period of Murrell, which was four years from 2000-2004, onto their holding periods in order to satisfy the Rule 144 requirements. (Dudchik Post-Hearing Br. 10-11; Schoemann Post-Hearing Br. 22-23.) However, this argument requires that the party from whom the shares are acquired be a non-affiliate, and, since Murrell was an affiliate, it fails. See Resale of Restricted Securities; Changes to Method of Determining Holding Period of Restricted Securities Under Rules 144 and 145, 55 Fed. Reg. 17,933, 17,941 (Apr. 30, 1990) (to be codified at 17 C.F.R. pts. 200, 230) ("No such tacking will be permitted, however, where the seller has purchased from an affiliate of the issuer whose presence in the chain of title will trigger the commencement of a new holding period.");

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[33] Rule 144(k) has since been repealed and replaced by Rule 144(b), which replaced the two-year holding period of Rule 144(k) with a one-year holding period. See Revisions to Rules 144 and 145, Exchange Act Release No. 33-8869 (December 6, 2007). Applying the current rule would not change the analysis and conclusions in this Initial Decision.

M & A West, 538 F.3d at 1051 ("Tacking is not permitted, however, if the purchaser acquires the securities directly from an affiliate in a private transaction."). Thus, Dudchik and Schoemann cannot avail themselves of the Rule 144 safe harbor.

I conclude that Dudchik and Schoemann have not carried their burdens to show that their sales of Stinger stock were exempt transactions pursuant to the Section 4(1) exemption or the Rule 144 safe harbor. Accordingly, their sales of Stinger stock violated Sections 5(a) and 5(c) of the Securities Act.

SANCTIONS

The Division seeks cease-and-desist orders against, and disgorgement of ill-gotten gains plus prejudgment interest from, Dudchik and Schoemann. (OIP ¶ III.B; Div. Post-Hearing Br. at 26-28.)

A. Cease-and-Desist Orders

Section 8A(a) of the Securities Act authorizes the Commission to impose a cease-and-desist order upon any person who "is violating, has violated, or is about to violate" any provision of the Securities Act or the rules and regulations thereunder.

In KPMG Peat Marwick LLP, 54 S.E.C. 1135, 1183-92 (2001), the Commission addressed the standard for issuing cease-and-desist relief. It explained that the Division must show some risk of future violations. However, it also ruled that such a showing should be "significantly less than that required for an injunction" and that, "absent evidence to the contrary," a single past violation ordinarily suffices to raise a sufficient risk of future violations. Id. at 1185, 1191.

"Along with the risk of future violations, the Commission considers the seriousness of the violation, the isolated or recurrent nature of the violation, the respondent's state of mind, the sincerity of the respondent's assurances against future violations, the respondent's recognition of the wrongful nature of his or her conduct, and the respondent's opportunity to commit future violations." Id. at 1192. In addition, the Commission considers "whether the violation is recent, the degree of harm to investors or the marketplace resulting from the violation, and the remedial function to be served by the cease-and-desist order in the context of any other sanctions being sought in the same proceeding." Id. The Commission weighs these factors in light of the entire record, and no one factor is dispositive.

Based on an analysis of these factors, I conclude that the proven violations were serious and recurrent. They also involved the reckless disregard of regulatory requirements. No Respondent has offered assurances against future violations or recognized the wrongful nature of his conduct. On the other hand, the violations are not recent, and the Division has not presented evidence of harm to specific investors or to the market in general. The last two factors are outweighed by the other factors previously discussed. See Robert W. Armstrong, III, Exchange Act Release No. 51920, 2005 SEC LEXIS 1497, at *66 (June 24, 2005) (imposing a cease-and-desist order against a respondent for misconduct that ended ten years earlier).

Dudchik, at the time of the hearing, was unemployed, and he has never had a position in the securities industry. (Tr. 289-90.) However, he is forty-seven and his previous business experience, including serving as an officer and director for Information Architects and as a consultant to Murrell and Stinger, suggest that he can be expected to have a lengthy career with similar opportunities to acquire and sell securities, and could readily repeat the type of misconduct proven here. Schoemann, age forty-one, makes his entire living by investing money in the stock market and significant ownership in public companies, affording him many opportunities to engage in the same misconduct. Thus, cease-and-desist orders will help to ensure that Dudchik and Schoemann will take greater care to obey the law when active in the financial markets in the future. I will impose cease-and-desist orders against Dudchik and Schoemann for all proven violations.

B. Disgorgement

Pursuant to Section 8A(e) of the Securities Act, the Division seeks orders requiring disgorgement of ill-gotten gains by Dudchik and Schoemann. Disgorgement is defined as "'an equitable remedy designed to deprive [respondents] of all gains flowing from their wrong.'" SEC v. AMX, Int'l, Inc., 872 F. Supp. 1541, 1544 (N.D. Tex. 1994) (citations omitted). A violator is returned to where he or she would have been absent the misconduct. Disgorgement deprives a wrongdoer of his or her ill-gotten gains and deters others from violating the securities laws. See SEC v. First City Fin. Corp., 890 F.2d 1215, 1230-32 (D.C. Cir. 1989). "The effective enforcement of the federal securities laws requires that the SEC be able to make violations unprofitable. The deterrent effect of an SEC enforcement action would be greatly undermined if securities law violators were not required to disgorge illicit profits." Manor Nursing Ctrs., Inc., 458 F.2d 1082, 1104 (2d Cir. 1972). An order to disgorge a certain amount need only be a reasonable approximation of the profits causally connected to the violation. See First City, 890 F.2d at 1231.

Once the Division shows that its disgorgement figure reasonably approximates the amount of unjust enrichment, the burden of going forward shifts to the respondent to demonstrate clearly that the Division's disgorgement figure is not a reasonable approximation. See SEC v. Lorin, 76 F.3d 458, 462 (2d Cir. 1996); SEC v. Patel, 61 F.3d 137, 140 (2d Cir. 1995). Any risk of uncertainty as to the disgorgement amount falls on the wrongdoer whose illegal conduct created the uncertainty. See First City, 890 F.2d at 1232.

The Division has shown that Dudchik and Schoemann made profits (ill-gotten gains) of $865,935 and $967,901, respectively, from their unregistered sales of Stinger stock, and I will order disgorgement in those amounts, subject to any proven inability to pay.

C. Prejudgment Interest

Section 8A(e) of the Securities Act provides that the Commission may order disgorgement, "including reasonable interest," in any administrative proceeding in which a cease-and-desist order is sought. This statutory provision also authorizes the Commission to adopt rules and regulations and issue orders concerning rates of interest and periods of accrual. The Commission promulgated Rule 600 of its Rules of Practice, Interest On Sums Disgorged, in

1995. The Division contends that the starting date for the computation of prejudgment interest should be the dates of the last violations. (Div. Post-Hearing Br. 28.) I will order Dudchik and Schoemann to pay prejudgment interest on the amounts of disgorgement as calculated in accordance with Rule 600 of the Commission's Rules of Practice, subject to any proven inability to pay.

D. Inability to Pay

Although no statutory requirement addresses inability to pay disgorgement or interest, the Commission may consider evidence of ability to pay as a factor in determining whether a respondent should be required to pay disgorgement and interest. See 17 C.F.R. § 201.630(a).

Only Dudchik makes a claim of inability to pay, providing a sworn financial statement admitted under protective order. (Dudchik Post-Hearing Br. 22-25.) Although he is forty-seven years of age, and the cease-and-desist order imposed in this Initial Decision is unlikely to have a significant adverse impact on his ability to earn an income, a review of Dudchik's sworn financial statement supports his claim that the disgorgement and prejudgment interest requested by the Division are beyond his ability to pay now or in the reasonably foreseeable future.

The Division focuses on the need for deterrence, but ignores the issue of collectability. The Commission has stated:

> We are cognizant of the inadvisability of assessing penalties so heavy that the persons against whom they are assessed are unable to pay them. Such a situation results in the expenditure of agency resources in unsuccessful attempts to collect the penalties. Moreover, the imposition of a sanction that cannot be enforced may ultimately render the deterrent message intended to be communicated by the sanction less meaningful.

First Sec. Transfer Systems, Inc., 52 S.E.C. 392, 397 (1995).

The Government Accountability Office (formerly the General Accounting Office) has similarly stated:

> Levying fines is an important mechanism that regulators use to sanction those who violate securities . . . industry rules. However, for fines to be an effective means of ensuring adherence with the rules, regulators must collect them.

Report to the Ranking Minority Member, Committee on Energy and Commerce, House of Representatives, SEC and CFTC: Most Fines Collected, but Improvements Needed in the Use of Treasury's Collection Service 1 (GAO-01-900) (General Accounting Office, July 2001).

When a respondent properly makes a claim of inability to pay, two principles emerge from the Commission's First Securities opinion: (1) financial sanctions should be imposed with due regard for collectability, so as to avoid, to the extent possible, the imposition of sanctions that are likely to be uncollectable; and (2) the collection of financial sanctions is as much, if not

more, of a deterrent to misconduct as the imposition of showplace sanctions. Consideration of collectability should not lead to the assessment of financial sanctions that are so low that they lack any meaningful deterrent value; however, consideration of deterrence should not lead to the assessment of financial sanctions that are so high that they lack any meaningful prospect of being collected.

It is in the public interest to reduce the total of Dudchik's disgorgement and prejudgment interest to $50,000. Dudchik is reminded of the need to keep current his confidential financial disclosure statements in the event that the Commission reviews this Initial Decision. See 17 C.F.R. §§ 201.410(c), .630(b).

RECORD CERTIFICATION

Pursuant to Rule 351(b) of the Commission's Rules of Practice, I certify that the record includes the items set forth in the record index issued by the Secretary of the Commission on November 10, 2008.

ORDER

Based on the findings and conclusions set forth above:

IT IS ORDERED THAT, pursuant to Section 8A of the Securities Act of 1933, Thomas J. Dudchik shall cease and desist from committing or causing any violations or future violations of Sections 5(a) and 5(c) of the Securities Act of 1933;

IT IS FURTHER ORDERED THAT, pursuant to Section 8A of the Securities Act of 1933, Rodney R. Schoemann shall cease and desist from committing or causing any violations or future violations of Sections 5(a) and 5(c) of the Securities Act of 1933;

IT IS FURTHER ORDERED THAT, pursuant to Section 8A of the Securities Act of 1933, Thomas J. Dudchik shall pay disgorgement and prejudgment interest in the amount of $50,000; and

IT IS FURTHER ORDERED THAT, pursuant to Section 8A of the Securities Act of 1933, Rodney R. Schoemann shall disgorge $967,901 plus prejudgment interest as calculated by and in accordance with Rule 600 of the Securities and Exchange Commission's Rules of Practice.

Payment of the disgorgement and prejudgment interest shall be paid in accordance with the order of finality issued pursuant to Rule 360(d)(2) of the Commission's Rules of Practice. Payment shall be made by wire transfer, certified check, United States Postal money order, bank cashier's check, or bank money order, payable to the Securities and Exchange Commission. The payments, and a cover letter identifying the Respondents and the proceeding designation, shall be delivered to the Comptroller, Securities and Exchange Commission, Operations Center, 6432 General Green Way, Stop 0-3, Alexandria, Virginia 22312. A copy of the cover letter and the

instrument of payment shall be sent to the Commission's Division of Enforcement, directed to the attention of counsel of record.

This Initial Decision shall become effective in accordance with and subject to the provisions of Rule 360 of the Commission's Rules of Practice. Pursuant to that Rule, a party may file a petition for review of this Initial Decision within twenty-one days after the service of the Initial Decision. A party may also file a motion to correct a manifest error of fact within ten days of the Initial Decision pursuant to Rule 111 of the Commission's Rules of Practice. If a motion to correct a manifest error of fact is filed by a party, then that party shall have twenty-one days to file a petition for review from the date of the undersigned's order resolving such motion to correct a manifest error of fact.

The Initial Decision will not become final until the Commission enters an order of finality. The Commission will enter an order of finality unless a party files a petition for review or a motion to correct a manifest error of fact, or unless the Commission determines on its own initiative to review this Initial Decision as to any party. If any of these events occur, the Initial Decision shall not become final as to that party.

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Robert G. Mahony
Administrative Law Judge