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UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

ALLSTATE PETROLEUM, INC.
125 East 50th Street
New York 22, New York

File No. 8-10775

RECOMMENDED DECISION

SIDNEY L. FEILER
Hearing Examiner

Washington, D. C.

May 21, 1965.

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APPEARANCES:

Messrs. Robert G. Willner, Alan R. Sloate and Carmine A. Asselta, for the Division of Trading and Markets.

Mr. Alfred Shayne, 101 West 55th Street, New York, N. Y. pro se.

BEFORE: SIDNEY L. FEILER, HEARING EXAMINER

I. THE PROCEEDINGS

These are proceedings pursuant to Section 15(b) and 15A of the Securities Exchange Act of 1934 ("Exchange Act")[1/] to determine what, if any, remedial action is appropriate in the public interest pursuant to Section 15(b) of the Exchange Act with reference to the registration as a broker and dealer of Allstate Petroleum, Inc. ("the registrant"); whether to permit the notice of withdrawal of registrant from registration filed by it to become effective, and if so, whether it is necessary in the public interest or for the protection of investors to impose terms and conditions under which said notice of withdrawal may be permitted to become effective; and whether, within the meaning of Section 15A(b)(4) of the Exchange Act, it should be found that Milton J. Helmke, George C. Foltz, Henry L. Hahn, Joseph Messina, principals of the registrant, and Alfred Shayne, Donald D. Dunklee, and William Fisher, salesmen of the registrant, should be found to be causes of any remedial action ordered.

The matters put in issue by the amended order for these proceedings are:

A. Whether the registrant willfully violated Section 15(b) of the Exchange Act and Rule 17 CFR 240.15b-2, promulgated by the Commission thereunder, and Helmke, Foltz, Messina, Hahn, Shayne, Dunklee and Fisher

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1/ These proceedings were instituted prior to the adoption of the Securities Acts Amendments of 1964, 78 Stat. 565 (August 20, 1964). References to provisions of the Securities Act and the Exchange Act are to provisions as they existed prior to the adoption of the amendments.

aided and abetted such violations in that registrant in its application for registration and amendments thereto made false and misleading statements with respect to material facts and registrant failed, and said individual respondents failed to cause registrant to file amendments promptly to correct these inaccuracies. 2/

B. Whether, during the period of approximately May 30, 1962 to July 30, 1962 or later, registrant, Helmke, Foltz, Hahn, Messina, Shayne, Dunklee and Fisher willfully violated Sections 5(a) and (c) of the Securities Act of 1933 ("Securities Act") in that registrant, Helmke, Foltz, Hahn, Messina, Shayne, Dunklee and Fisher, sometimes collectively referred to as "the respondents", directly and indirectly made use of the means and instruments of transportation and communication in interstate commerce and of the mails to offer to sell and sell certain securities of El Dorado, Buhler Lease No. 1 ("Buhler") and the Nicholson Lease No. 1 ("Nicholson") when no registration statements have been filed or were in effect under the Securities Act as to such securities. 3/

2/ Every registered broker-dealer, pursuant to these provisions, is required to promptly file an amendment to its broker-dealer registration if the information contained in the original application or any amendment supplemental thereto is or becomes inaccurate for any reason.

3/ Section 5 of the Securities Act provides, in pertinent part, that it shall be unlawful to make use of the instruments of transportation or communication in interstate commerce or of the mails to offer to sell or to sell a security unless a registration statement is in effect as to it.

C. Whether, during the aforementioned period, respondents, singly or in concert, willfully violated and aided and abetted willful violations of the anti-fraud provisions of the Securities Acts [4/] in offering, selling, and inducing the purchase of and effecting transactions of the securities mentioned in paragraph B above and in connection therewith made false and misleading statements of material facts and omitted to state material facts and obtained money and property thereby and engaged in conduct and activities which constituted fraud and deceit upon certain persons.

D. Whether, during the period from approximately May 30, 1962 to July 30, 1962 or later, registrant, aided and abetted by Helmke, Foltz, Messina and Hahn, willfully violated Section 17(a) of the Exchange Act and Rules 17 CFR 240.17a-3 and 17 CFR 240.17a-4, promulgated by the Commission thereunder, in that said persons, singly and in concert, failed to make, keep current and preserve certain books and records which registrant was required to keep current and preserve under said Section and Rules. [5/]

4/ Section 17(a) of the Securities Act and Sections 10(b) and 15(c)(1) of the Exchange Act and Rules 10b-5 and 15c1-2 (17 CFR 240.10b-5 and 15c1-2) thereunder are sometimes referred to as the anti-fraud provisions of the Securities Acts. The composite effect of these provisions, as applicable here, is to make unlawful the use of the mails or interstate facilities in connection with the offer or sale of any security by means of a device or scheme to defraud or untrue or misleading statements of a material fact, or any act, practice, or course of conduct which operates or would operate as a fraud or deceit upon a customer or by means of any other manipulative or fraudulent device.

5/ Under these provisions registered broker-dealers are required to make and keep current specified books and records and to preserve them for a period of not less than six years.

Pursuant to notice, a hearing was held in New York, N. Y. before the undersigned Hearing Examiner. All the respondents were served with the Amended Order for these Proceedings, but only one respondent, Shayne, appeared and participated in the hearing.

A joint answer was filed by the registrant, Helmke, Foltz, Hahn, and Messina. In this answer, the aforesaid respondents allege that they had no intention of misleading anyone, that this was the first and only securities offering ever made by the registrant, that the registrant was completely ignorant of applicable rules and regulations, and that reliance was placed on Shayne to handle sales and office procedures. These respondents did not further participate in the proceedings after filing their answer.

The respondents, Dunklee and Fisher, have signed written consents to the entry of an order finding that they had willfully violated the Securities Acts as alleged in the Orders for Proceedings and further finding that they are causes of any Commission order which may be entered revoking the registration of registrant (Div. Ex. 2). They testified in these proceedings as witnesses but did not otherwise participate.

The parties appearing at the hearing were accorded full opportunity to be heard and to examine and cross-examine witnesses. At the conclusion of the presentation of evidence, opportunity was afforded the parties to state their positions orally on the record. Oral argument was waived. Opportunity was then afforded the parties for filing proposed findings of fact and conclusions of law, or both, together with briefs in

support thereof. Proposed findings, together with a supporting brief, were submitted by the Division. No formal documents were received from Shayne, although he did file a letter after the close of the hearing, restating his position.

Upon the entire record and from his observation of the witnesses, the undersigned makes the following:

II. FINDINGS OF FACT

A. The Registrant

1. Registrant was incorporated in March, 1960 but remained dormant until March, 1962. Registrant has been registered with the Commission as a broker-dealer pursuant to Section 15(b) of the Exchange Act since June 15, 1962. On June 27, 1962, registrant requested that it be permitted to withdraw its registration immediately. It later requested that the effective date be postponed to August 10, 1962. The withdrawal has not become effective (File No. 8-10775-1).

2. The registrant originally maintained its office at 125 East 50th Street, New York, N. Y. In July, 1962, it moved to 30 East 42nd Street, New York, N. Y., but soon abandoned this office. Its last known address was in New Orleans, Louisiana at Messina's home.

3. At all times here relevant Helmke has been president, a director and beneficial owner of 10% or more of the common stock of the registrant; Foltz has been a vice-president and beneficial owner of 10% or more of the common stock of the registrant; Hahn has been vice-president, a director and general manager of the registrant. He was in active charge of the registrant's New York office during the period mentioned in the

Amended Order for these Proceedings. Messina, during the relevant period, has been the secretary-treasurer, a director and beneficial owner of 10% or more of the common stock of the registrant.

B. Salesmen of the Registrant

4. Alfred Shayne was employed by the registrant from approximately April 19, 1962 to about July 28, 1962. During the first eight weeks of his employment, he was a salaried employee and assisted Hahn in establishing the registrant's office, sales organization, and other preparations for the sale of securities undertaken by the registrant. After his initial period of employment, he was functioning chiefly as a salesman and was compensated on a commission basis. He recommended the employment of Dunklee and Fisher as salesmen to Hahn and they were hired. Shayne also entered into discussions with other individuals with reference to their employment with the registrant, but the negotiations did not come to fruition. Shayne, Dunklee, and Fisher, so far as the record indicates, were the sole salesmen employed by the registrant during the period here material. Dunklee and Fisher were employed during the months of June and July, 1962.

5. The Application for Registration as a Broker and Dealer filed by the registrant on May 16, 1962 required the furnishing of the names of any salesmen or other employee, or any other person directly or indirectly controlling or controlled by the registrant who had been convicted, within ten years, of any felony or misdemeanor involving the purchase or sale of any security or arising out of the conduct of the

business of a broker or dealer, or who was permanently or temporarily enjoined from engaging in, continuing any conduct or practice in connection with the purchase or sale of any security; or who had been found by the Commission to have violated any provision of the Securities Acts, or any rule or regulation under those Acts (Item 8). This item had originally been answered "No" as to each of the subdivisions and no amendment was ever filed changing this response.

6. In 1951, Shayne was found to have violated the anti-fraud provisions of the Securities Acts while employed as a salesman for a broker-dealer and to be a cause of the revocation of registration directed as to that registrant.[6/]

7. Dunklee, in 1959, on a stipulation of facts and consent by him, was found to be a cause of an order of revocation entered against a registrant because of its failure to amend its application for registration to indicate that Dunklee was in control of its operations. Dunklee was named as a cause of the order of revocation which was entered.[7/]

6/ Henry B. Rosenfeld Co., 32 S.E.C. 731, 740. In its decision the Commission considered an application by Shayne who was then also registered as a broker and dealer for cancellation of his registration or withdrawal of it on certain conditions. The Commission denied these requests, stating that Shayne had made repeated willful representations to customers and that withdrawal would not be consistent with the public interest and for the protection of investors but that the violations were of a nature requiring revocation (supra, p. 741).

7/ Jefferson Associates, Inc., 39 S.E.C. 271 (1959).

8. On April 9, 1947, Dunklee was convicted in the United States District Court for the Southern District of Iowa of violating the Securities Act and the Mail Fraud Statute (Div. Ex. 7). On December 3, 1945, Dunklee was convicted in the State of Minnesota on a charge of swindling, through the use of what was designated as a "fake oil lease investment contract" (Div. Ex. 8).

9. William Fisher was found by the Commission to be a cause of an order of revocation issued against a broker-dealer for violation of the net capital rule.[8/] A permanent injunction was also issued against Fisher by the United States District Court for the Southern District of New York on June 3, 1958 enjoining further violations of the net capital rule in proceedings instituted against A. J. Gould & Co., Inc. (Div. Ex. 5).

10. The records of Shayne, Dunklee, and Fisher, as set forth above, should have been brought to the attention of the Commission in appropriate amendments to the registrant's broker-dealer application. The failure to do so rendered the application inaccurate and incomplete and violative of the rules and regulations relating to the filing of broker-dealer applications and amendments thereto.[9/]

8/ A. J. Gould & Co., Inc., 38 S.E.C. 141 (1957).

9/ Burley and Company, 23 S.E.C. 461 (1946); Wright, Myers & Bessell, Inc., Sec. Exch. Act Rel. No. 7415 (September 8, 1964); Universal Securities of Buffalo, 39 S.E.C. 372 (1959); Alexander Dvoretsky d/b/a Dennis & Company, 39 S.E.C. 605 (1959); Steven Randall & Co., Inc., 38 S.E.C. 863 (1959); Roberts Securities Corporation, 38 S.E.C. 63 (1957); Waldinger d/b/a American Securities Co., 37 S.E.C. 733 (1957); Martin Weiss d/b/a Martin Weiss & Co., 9 S.E.C. 27 (1941); Frank B. Hamlin, 2 S.E.C. 511 (1937).

11. Hahn did not testify in the instant proceeding. In the investigative testimony, which was incorporated in the record in these proceedings as an exhibit, Hahn denied knowing anything of the background of the salesmen which would prevent their employment in the securities business.

12. Shayne testified that he told Hahn of the Commission proceeding against him. His testimony on this point is credited. While Shayne was under the misapprehension that a lapse of ten years since the issuance of the Commission's order would remove the bar against him, and told that to Hahn, there is no evidence that Hahn made any effort to check Shayne's assertions. Hahn also ignored warnings by both a Commission employee and his own accountant that he should check the background of the salesmen. Under all these circumstances the undersigned concludes that the violation found was willful and that Hahn, who was in charge of the local office where these salesmen were employed, aided and abetted the violations found. Dunklee and Fisher also aided and abetted such violations by not making a full disclosure of their records. Shayne, who, in his own testimony, made partial disclosure of his background to Hahn, did not give Hahn accurate information as to the extent of the bar against him and must also be held as an aider and abettor. Helmke, Foltz, and Messina did not actively direct the activities in the New York office of the registrant. However, they designated Hahn to carry on its operation and were in communication with him. Their ownership interest in the registrant put them in the position to control the affairs of the registrant and while their role in this violation is of a secondary nature, they also must be held

to have aided and abetted the violations found.[10/]

C. Violations of the Registration Provisions of the Securities Act

13. It is alleged in the Order for these Proceedings that from approximately May 30, 1962 to July 30, 1962, or later, the registrant and the individual respondents named in the Order willfully violated the registration provisions of the Securities Act, Sections 5(a) and (c), in that respondents, directly and indirectly, made use of the means or instruments of transportation or communication in interstate commerce or of the mails to offer to sell and sell securities of El Dorado, Buhler Lease Number 1 ("Buhler") and the Nicholson Lease Number 1 ("Nicholson"), when no registration statements had been filed or were in effect under the Securities Act as to such securities. During the period alleged, the registrant was offering for sale and selling non-producing working interests in the aforementioned three properties on which it held leases. The fractional undivided interests in oil rights which were being sold were securities as defined in the Securities Act, but no registration statement was filed as to any of them.

14. Provision is made in Regulation B of the General Rules and Regulations issued by the Commission pursuant to Section 3(b) under the Securities Act for exemption from the full registration requirements of

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10/ Aldrich, Scott & Co., Inc., 40 S.E.C. 775, 778 (1961). John T. Pollard & Co., Inc., 38 S.E.C. 594, 598 (1958); Alan Russell Securities, Inc., 38 S.E.C. 599, 601 (1958); Lucyle Hollander Feigin, 40 S.E.C. 594, 596 (1961).

fractional undivided interests in oil or gas rights if the aggregate amount at which such issue or offering is issued, offered or sold, does not exceed $100,000. Pursuant to Regulation B, on June 4, 1962, registrant filed a "Schedule D" offering sheet for exemption from registration for non-producing working interests in property designated as the El Dorado Plantation Lease. The effectiveness of the filing of this offering sheet was temporarily suspended by order of the Commission of June 11, 1962; but after certain amendments in the offering sheet had been made to cure the objections specified, the offering sheet as amended became effective on June 18, 1962 (File No. 20-1061A2-1).

15. On May 17, 1962, registrant filed a "Schedule D" offering sheet for exemption from registration under Section 3(b) of the Securities Act and Regulation B thereunder for non-producing working interests in the Vincent Lease, which was also known as the Buhler Lease. The effectiveness of the filing of this offering sheet was temporarily suspended by order of the Commission on May 28, 1962 and it has never become effective (File No. 20-1061A1-1).

16. The registrant engaged in a selling campaign to dispose of participations in all three of its leaseholds. Extensive publicity was given to the drilling program contemplated by the registrant. Advertisements were placed in the Eastern edition of the Wall Street Journal on June 19, June 26 and July 17, 1962, in the Midwest edition of the Journal on July 24, 1962, in the Pacific Coast edition of the Journal on July 19, 1962 and in Barron's on June 25, 1962. Both these publications are periodicals with wide circulation throughout the United States. The advertisements

mentioned that the company was beginning a "10-well deep drilling . . . program on valuable leases in thoroughly geologized, proven and offset field areas showing millions of barrels of oil & gas reserves . . ." (Div. Ex. 49, 102). Hahn and Shayne participated in the preparation of this advertisement as well as other sales material used in the registrant's program.

17. The services of a commercial advertisement company, Laura Dee Advertisement Service, Inc., also were used to print and mail out additional material on behalf of the registrant. These services included the mailing of 1431 envelopes with inserts which included a drilling report and photostat of the advertisement inserted in the Journal; another mailing of 155 envelopes, each containing 8 inserts; a printing of 200 copies of a form letter signed by Helmke on behalf of registrant promising to refund to investors "out-of-pocket" investment on their purchases of participations in earnings on the El Dorado, Nicholson and Buhler leases if at least one well of the three to be drilled was not brought in as a producing well (Div. Ex. 95-E); another mailing of 503 envelopes with 7 or 8 inserts; and 125 copies of a letter referring to and offering participations in the Buhler and Nicholson Leases (Div. Ex. 95-G). The registrant also obtained a copy of a telephone directory of the Department of Defense and prepared a list of names which were sent to Laura Dee by Shayne for use in the mail-outs (Div. Ex. 74-J, Exs. H-2 and H-3 therein). The registrant's salesmen contacted persons who answered the newspaper advertisements inserted by the registrant and offered and sold them participations in the El Dorado and the other two leases. Shayne and Dunklee also sold to

persons who had purchased participations in another joint venture, Cabeza, with which they had been associated.

18. As a result of the selling campaign carried on by registrant and its salesmen, participation in the Nicholson and/or Buhler were offered and/or sold to persons of diverse occupations who resided in 12 states and the District of Columbia. Six persons agreed to purchase participations in all 3 offerings for a total of $18,000 and paid $12,925 of this amount. 8 persons purchased participation in El Dorado for $5,000. One person purchased a participation in Buhler for $625. In addition to the above, registrant confirmed purchases of participations in El Dorado for a total of $5,000 to 8 persons and confirmed purchases in all 3 participations for $2,000 to one person.

19. The salesmen had available to them special brochures on the Nicholson and Buhler Leases and the brochures were sent to persons who responded to registrant's advertisements as well as to others.

20. It is clear from the evidence that the facilities of interstate commerce and of the mails were made use of in the offer and sale of the Buhler and Nicholson non-producing working interests and these offers and sales were made without any registration statement having been filed for these securities, nor was any filing made under Regulation B. These offerings and sales, therefore, were made in violation of the registration provisions of the Securities Act unless there was an exemption from registration available to the registrant.[11]

11/ Securities and Exchange Commission v. Ralston Purina Co., 346 U.S. 119 (1953).

21. While no appearance was made at the hearing on behalf of the registrant or its principals, the answer filed on their behalf indicates that registrant maintained that the Buhler and Nicholson offerings were private offerings within the meaning of Section 4(1) of the Securities Act and exempt from the registration provisions of Section 5. 12/

22. It is settled law that a claim of exemption is to be strictly construed and the person asserting exemption has the burden of proving its availability. 13/ It is asserted in the answer that the Buhler and Nicholson offerings were to be made only to friends of Shayne or Dunklee. Hahn also testified in the investigative proceedings, the transcripts of which were received in the record herein, that it was intended that offerings be made only to a small group of investors. The evidence, however, is to the contrary. Special brochures were prepared for the Nicholson and Buhler offerings and were mailed out to persons who answered newspaper advertisements. Those who bought were residents of 12 states and the District of Columbia, thus indicating a widespread distribution of selling literature. The bulk of the funds raised by the registrant

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12/ Section 4 provides:

> "The provisions of Section 5 shall not apply to any of the following transactions: (1) Transactions by any person other than an issuer, underwriter or dealer; transactions by any issuer not involving a public offering , . .

13/ Securities and Exchange Commission v. Ralston Purina Co., supra; see also Securities and Exchange Commission v. Culpepper, 270 F. 2d 241 (2nd Cir. 1959), Gilligan, Will & Co. v. Securities and Exchange Commission, 267 F. 2d 461 (2nd Cir. 1959); Advanced Research Associates, Inc., Securities Act Rel. No. 4630 (August 16, 1963).

came from persons who agreed to purchase participations in all three offerings. While the number of actual investors was small, this is not decisive of the issue. It was pointed out in the Ralston Purina case that the key question is the association of the investors with the issuer and their knowledge of its affairs.

> "Exemption from the registration requirements of the Securities Act is the question. The design of the statute is to protect investors by promoting full disclosure of information thought necessary to informed investment decisions. The natural way to interpret the private offering exemption is in light of the statutory purpose. Since exempt transactions are those as to which 'there is no practical need for [the bill's] application,' the applicability of § 4(1) should turn on whether the particular class of persons affected needs the protection of the Act. An offering to those who are shown to be able to fend for themselves is a transaction 'not involving any public offering.'" (supra, at p. 124, footnotes omitted). 14/

23. The Commission has pointed out that "negotiations or conversations with or general solicitation of an unrestricted or unrelated group of prospective purchasers for the purpose of ascertaining who would be willing to accept an offer of securities is inconsistent with the claim that the transaction does not involve a public offering even though ultimately there may only be a few knowledgeable purchasers." 15/ This is what happened here. The evidence indicates that there was a widespread solicitation of potential investors through the use of a commercial mailing service which mailed out several thousand pieces of literature and

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14/ See also Meadow Brook Nat'l Bank v. Levine, 153 N.Y.L.J. No. 36, p. 19, Feb. 24, 1965, CCH Securities Law Service (Par. 91,496).

15/ Securities Act Release No. 4552 (November 6, 1962).

general mail-outs of brochures on the Nicholson and Buhler Leases. Additional material was sent by the registrant and its salesmen. The undersigned concludes that these activities were violative of Section 5 of the Securities Act and are chargeable to the registrant, Hahn (who was in charge of the registrant's business office), and the registrant's salesmen, Shayne, Dunklee, and Fisher (who all participated in the solicitation of potential investors). Registrant's officers, Helmke, Foltz, and Messina are also chargeable with these violations even though they did not directly participate in the activities conducted in the New York office. As previously pointed out, they had the power and the obligation to supervise those activities and to prevent violations of the Securities Acts. In addition, they knew of the sales activities being conducted and furnished material for use in the brochures. It is further concluded that the violations were willful.[16/]

24. Participations in the El Dorado Lease were offered under the exemptions available to fractional undivided interests in oil or gas rights in accordance with the provisions of Regulation B prescribed by the Commission in its General Rules and Regulations, pursuant to Section 3(b) of the Securities Act. The exemption is only available if its terms and conditions are strictly complied with by an issuer. There is substantial

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16/ Harry Marks, 25 S.E.C. 208, 220 (1947); George W. Chilian, 37 S.E.C. 384 (1956); E. W. Hughes & Company, 27 S.E.C. 629 (1948); Hughes v. S.E.C., 174 F. 2d 969 (C.A.D.C. 1949); Shuck & Co., 38 S.E.C. 69 (1957); Carl M. Loeb, Rhoades & Co., 38 S.E.C. 843 (1959); Ira Haupt & Company, 23 S.E.C. 589, 606 (1946); Van Alstyne, Noel & Co., 22 S.E.C. 176 (1946); Thompson Ross Securities Co., 6 S.E.C. 1111, 1122 (1940); Churchill Securities Corp., 38 S.E.C. 856 (1959).

evidence that registrant failed to comply with the provisions of Regulation B and that the claimed exemption was not available in registrant's offer of participations in the El Dorado Lease.

25. Rule 320(a) of Regulation B provides in substance that an offering sheet filed with the Commission be effective before any offers to sell are made. The record establishes that the registrant was offering participations in the El Dorado Lease prior to June 18, 1962, the effective date of the filing under Regulation B, and that letters were sent to three persons on June 15, 1962 confirming purchases of participations in the El Dorado Lease (Div. Ex. 76-A, pp. 60-70; Div. Ex. 76-C, Exhs. Q, R, and S therein). Rule 320(b) further provides that an exemption under Regulation B is only available if the offeror, at the time of the initial offer to sell a security, sought to be exempted, shall deliver to every person solicited to buy, a copy of the offering sheet then on file with the Commission (as amended, if amended) accurately describing such security and complying with Rule 330 dealing with the form and content of offering sheets. Nine witnesses who testified to receiving the Schedule "D" material on the El Dorado did not receive a copy of the amended offering sheet on file with the Commission.

26. The advertisements placed by the registrant in the Wall Street Journal and Barron's gave details as to a joint program and the asserted chance of success. Under Rule 320(b) an advertisement may be used without being considered as an "offer to sell" within the provisions of that section when it stated only from whom an offering sheet may be obtained and, in addition, no more than identify the security, state the

price thereof, and state by whom orders will be executed. Otherwise such an advertisement is considered an offer to sell. The delivery of an offering sheet at the time of the offer to every person solicited to buy is required. The advertisement used exceeded the restrictions set down in Rule 320(b) and thus was another instance where a condition for exemption was not complied with.

27. Additional failures to comply with the provisions of Regulation B consisted of the following:

> Purchasers were not furnished satisfactory evidence of the validity of the title which they were to receive, as required by Rule 320(b).
>
> Rule 328 denies exemption from Regulation B to any person using any estimation of the amount of oil or gas recoverable from the tract involved in connection with an offer to sell any fractional or undivided interest in oil or gas rights. Such estimates were made in the registrant's advertisements and other literature.
>
> The registrant did not file with the Commission written reports of its contracts of sale of participation in El Dorado as required by Rule 320(e).

28. The exemptions provided under Regulation B are only available when there is strict compliance with the conditions set forth therein (Rule 320).[17/] It has been established that the provisions of Regulation B were not observed by the registrant in many respects and that therefore an exemption under Regulation B was not available for the public sales of the El Dorado interests by and on behalf of the registrant. It is therefore concluded that by those sales, set forth above, the registrant and the

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17/ W. Frank Minnicks d/b/a Continental Securities Company, 9 S.E.C. 625 (1941); Franklyn J. V. Stowitts, 6 S.E.C. 97 (1939).

individual respondents willfully violated Section 5 of the Securities Act as alleged in the amended order for these proceedings.

D. Violations of the Anti-fraud Provisions of the Securities Acts

27. It is further alleged in the order for these proceedings that the respondents, singly and in concert, willfully violated and aided and abetted willful violations of the anti-fraud provisions of the Securities Act in the sale of the El Dorado, Buhler and Nicholson interests.

1. Material facts with respect to the registrant's offerings

28. According to Tell T. White, a petroleum and natural gas engineer on the Commission's staff, whose unchallenged testimony is credited, the three offerings by the registrant were rank speculations which should be classified as wildcat, random drillings, whose ratio of success would be approximately one out of fifty. Dry holes had been drilled on or about the areas proposed for the El Dorado and Nicholson drillings and the registrant had knowledge of at least five of these dry holes. The dry holes were closer to registrant's drilling sites than two other fields which contained wells, most of which were not making their allowable production. White denied that there was a 50-50 chance of success as stated in the Nicholson brochure. He testified that even if the well were brought in on the proposed site there was nothing to indicate that it would be a commercial producer. He denied that any of the proposed drilling sites were in proven areas.

29. With respect to the proposed Buhler drilling, White testified that three dry holes had been drilled on or about the proposed Buhler area bracketing the one producing well in the field in three different directions. The only producing well in the Buhler field was an economic failure, not making its allowables. The possibility of drilling a commercially successful well on the Buhler site, according to White, was slight.

2. Literature used by the registrant and its correspondence with customers

30. In its offerings to customers the registrant made use of brochures on the Buhler and Nicholson Leases and the Schedule "D" offering sheet on the El Dorado, all supplemented by letters and additional material. The mails were used for the distribution of this material and the services of a commercial mailing company were utilized, as previously detailed.

31. The Buhler brochure purported to give detailed information on the Buhler Lease, including its prospects for commercial success (Div. Ex. 13). It was stated in the brochure "The well to be drilled on the Buhler Lease has been carefully selected from a geological standpoint and has an excellent chance of making a commercial well . . ." (p. 1). Actually, as pointed out in the testimony of Tell White, previously summarized, a well close to the Buhler site had been an economic failure and the chance for a commercial well was slight. It was further stated that from each sale a portion sufficient to drill the well would be deposited in a New York bank (p. 3). Actually, no escrow or special

account for Buhler was established and the registrant used all funds received for various expenses so that by September, 1962 it had exhausted the funds received from investors and did not have money to either return funds to investors or to proceed with its drilling program.

32. The Buhler brochure contained a report of David A. Rowe, petroleum consultant, in which he stated that the drilling of a well on the Buhler site had an excellent chance of success and could possibly be worth as much as $25,200,000 gross income. Nowhere in this brochure or any other material used by the registrant was it stated that the registrant had acquired its leases from L.T.M. Oil Development Corp., of which Rowe was the president. The registrant owed various sums to L.T.M., and its ability to meet those obligations depended on the success of its fund-raising campaign with investors. The evidence establishes that there was in fact no basis for the opinions advanced by Rowe as to the possibility of success of the Buhler well, or the amount of money or oil recoverable. In addition, the brochure included a plat of the Buhler area which failed to show three dry holes which the registrant had knowledge of and included in Schedule "D" filings for the Vincent lease which covered the same area, which filing did not become effective (File No. 20-1061A1).

33. A brochure similar in form to the one used for the Buhler Lease was also used in offerings of the Nicholson Lease (Div. Ex. 12). It is stated in this brochure that the proposed Nicholson well " . . . has been carefully selected from a geological standpoint and has an excellent chance of making a commercial oil and gas well . . ." (p. 1). It is also

set forth that the well was close to the Petkas well which had an accumulation of oil and the proposed well was a direct offset to it. Actually, the Petkas well was a dry hole and the proposed Nicholson drilling was technically not an offset well. The brochure further falsely stated that most of the Kenmore wells had done better than their allowables. An optimistic report by Rowe was also included in this brochure in which Rowe gave as his opinion the proposed well had a 50/50 chance for success and could ultimately produce oil of the gross value of $780,000 to $1,560,000. The proposed drilling was a wildcat and these optimistic predictions had no reasonable basis in fact. As in the case of the Buhler brochure, the Nicholson brochure failed to include five dry holes of which registrant had prior knowledge.

34. The above brochures were supplemented by mail-outs of the Rowe reports themselves and telegrams and letters. Shayne and Dunklee had previously sold offerings for another concern, Cabeza Petroleum Corp. They and the registrant made use of these prior contacts by sending to persons who had purchased participations in Cabeza, telegrams in the name of Shayne and/or Dunklee. In most instances the telegrams were dated May 31, 1962 and were identical in content as follows:

> "We are in southern Louisiana investigating very unusual drilling situation Allstate Petroleum, a group of highly experienced oil men, is starting a ten well deep drill program in thoroughly geologized areas offsetting proven leases, have asked Allstate to send complete information will phone you upon my return to New York." (Div. Ex. 39)

In fact, neither Shayne nor Dunklee had been to the Allstate drilling sites and the telegrams were actually sent by Messina.

35. The telegrams were followed by letters dated June 4, 1962 enclosing copies of the Rowe reports and copies of the Wall Street Journal mailed by registrant to Cabeza customers of Shayne and Dunklee. Letters were signed by Shayne and/or Dunklee and, as in the case of the form telegram previously sent, sought to assure the recipient that the Allstate securities had been carefully selected by them. Some of the language used was as follows:

> " . . . Realizing that you are busy with your own affairs and that you are depending on us for advice and protection of your oil investments, we fully appreciate our responsibility. Our livelihood depends solely upon a satisfied customer, therefore it behooves us to carefully investigate any and every situation which we recommend to our clients.
>
> . . .
>
> For several weeks we have been investigating the background of the above firm, Allstate Petroleum Inc. Of Louisiana. [sic] We knew they owned some very valuable leases, and were starting a 10 well deep drilling program in one of the 'choicest' oil and gas areas in southern Louisiana on thoroughly geologized proven and offset field properties. These leases are surrounded by several major oil and gas companies, having millions of barrels of oil and gas reserves, as the enclosed statistical reports show.
>
> 70% of the wells drilled in this are are successful and Allstate owns some of the most valuable leases in these fields.
>
> We chose Allstate Petro. Inc. because they are a thoroughly experienced and reliable group of successful oil men." (Div. Ex. 74J, Ex. H-43).

In fact, Shayne and Dunklee did not investigate registrant's drilling sites and accepted at face value contents of the Rowe reports and enlarged on them. All the statements in the letter on the value of Allstate properties were false and were not applicable to the registrant's offerings. The wildcat aspect of the drilling program was nowhere mentioned or even hinted at. Shayne admittedly drafted a good deal of the material used by the registrant.

36. The Schedule "D" offering sheet filed with the Commission for the offering of interests in the El Dorado Lease, also contained a series of representations which proved to be false.

37. These included the following:

(a) The representation and actual drilling would be commenced not later than September 17, 1962 (File No. 20-1061A2-1, Schedule "D", amendment at page 6a). In fact no drilling was ever commenced;

(b) The further representation that if sufficient interests were not sold within the effective period of the offering, then the purchaser's money would be refunded (amendment, page 6a), in fact no refund of money was ever offered to investors even though registrant could not proceed with any drilling;

(c) In response to an item in Schedule "D" which requested information on what assurance the purchaser of any of the interests had that the proposed well or wells would ever be drilled and completed, it was stated "The integrity and financial ability of the offeror, plus an escrow account for the actual drilling, is the purchaser's assurance that the well or wells will be drilled and, if successful, completed"

(amendment, page 7). It was also represented that from each sale a portion sufficient to drill and complete the wells would be deposited in a New York bank.

38. While an escrow account for El Dorado was established, it never contained more than $400 and no effort was made to have a sufficient amount set aside in an escrow account or otherwise to proceed with the drilling program.

39. In correspondence, confirmations, and written agreements, registrant represented to prospective purchasers and purchasers of participations in all three of its leases, Buhler, Nicholson and El Dorado, that if all three drillings were dry holes, registrant would return their out-of-pocket loss, i.e., that part of the investment that could not be deducted from their income tax. No funds or special accounts were maintained to assure the ability of the registrant to make good on this representation.

40. Evidence was also presented at the hearing that the registrant sent letters through the mails confirming purchases to at least five persons who had not agreed to purchase participations in any of the registrant's offerings and sent a confirmation to one purchaser before he had agreed to purchase a participation.

3. Representations to customers

41. The misrepresentations concerning the registrant's plans and prospects contained in letters and literature distributed to the public and the omission of definitive facts necessary to place the registrant's program in a clear and accurate perspective were repeated and intensified

in oral presentations to customers made by the salesmen. Most of the investor witnesses who testified either had dealt solely with Shayne or with Shayne and another salesman. The evidence is clear that Shayne presented a very rosy picture of the registrant's prospects to his customers which was incomplete and misleading. He told customers that prospects for oil recovery were very good in the area where registrant was going to drill, that there was a 50-50 or better chance of a successful drilling, a lot of money would be made in a short time, and that out-of-pocket losses would be made up to investors who invested in all three drillings if all were unsuccessful. Actually, as it has been pointed out, there was no reasonable basis for the prediction of success in the registrant's drilling program. They were of the "wildcat" variety with little chance of success.

42. Shayne had assured his customers that he had thoroughly investigated the registrant, its program, and the persons in control of it, yet he did not tell his customers of the existence of dry holes in the area where the registrant planned to drill, nor did he ascertain or reveal to his customers that David A. Rowe, on whose reports registrant relied in the Buhler and Nicholson brochures, was the president of L.T.M., the corporation from which registrant had derived its interests in Buhler, Nicholson, and El Dorado, and who had a financial interest in the ability of the registrant to meet its obligations to L.T.M. Shayne told his customers that the projected drillings were deep wells which had been very successful in Louisiana. He did not qualify this statement by revealing the poor results of drilling in the area where the registrant

proposed to begin its drilling operations. Shayne also made no inquiries as to the investment needs of those to whom he was attempting to sell participations in the registrant's drilling projects.

43. Dunklee and Fisher made similar misrepresentations to their customers as Shayne, but in view of their stipulations, their activities will not be set forth in detail.

44. Hahn also indulged in the same type of activities as his salesmen. He told one customer that there was a better than 70% chance of success in the registrant's proposed drilling and caused a confirmation to be sent to an investor to whom he had spoken but who had not agreed to purchase any participations.

45. The registrant's sales campaign, according to the weight of the evidence, was carried out without any training of the salesmen or supervision of their activities by any responsible official of the registrant. Hahn made no effort to oversee the work of the salesmen and they were permitted to use high-pressure tactics, to cause confirmations to be mailed to individuals who had never placed orders for participations, to sell to investors without regard to their financial needs or investment objectives, and to telephone prospective purchasers at times and places other than the registrant's business office.

4. Conclusions

46. A broker and his salesmen must deal fairly with customers in accordance with the standards of the profession.[18/] Outright false

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18/ Duker v. Duker, 6 S.E.C. 386, 388-89 (1939); A. J. Caradean & Co., Sec. Exch. Act Rel. No. 6903, p. 2 (Oct. 1, 1962).

statements are, of course, expressly prohibited by the securities laws and are inconsistent with the duty of fair dealing. In addition, as the Commission has pointed out, the making of representations to prospective purchasers without a reasonable basis, couched in terms of opinion or fact and designed to induce purchases, is contrary to the obligation of fair dealing borne by those who engaged in the sale of securities to the public.[19/]

47. Another aspect of the standard of fair dealing applicable to the securities business is the refusal by the Commission to permit concealment by a person engaged in the securities business of material facts of an adverse nature, the disclosure of which is necessary to render statements made not misleading.[20/]

48. The evidence fully establishes that the respondents violated the obligations of fair dealing set forth above. The offerings of the El Dorado, Nicholson, and Buhler participations were accompanied by the use of highly misleading literature buttressed by sales activities of the registrant's staff reiterating and emphasizing the misleading representations to investors who were not given full information about the registrant's properties so that they could exercise an informed judgment.

49. The initial newspaper advertisements used by the registrant stressed that it intended to drill in an area of highly successful oil

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19/ Mac Robbins & Co., Inc., Sec. Exch. Act Rel. No. 6846 (July 11, 1962), aff'd. 316 F. 2d 317 (1963); Ross Securities, Inc., Sec. Exch. Act Rel. 7069 (April 30, 1963).

20/ Leonard Burton Corporation, 39 S.E.C. 211 (1959).

drilling with large oil reserves. The failure to reveal that registrant's immediate proposed drilling was in an area of dry holes where there had been little past success made the comparison of the registrant's area to that of greater success incomplete, false and misleading.[21]

50. The registrant used highly optimistic forecasts of the extent of its recovery of oil on its proposed drilling sites. The estimates ran into millions of dollars. None of these reports dealt with the existence of dry holes adjacent to the proposed drilling sites, of which the registrant had knowledge. The Nicholson and Buhler reports were prepared by a person whom the registrant knew was financially interested in the success of the registrant's sales campaign. Under all of these circumstances, the registrant could not accept these reports at face value while it had knowledge of adverse factors which should have been called to the attention of the investing public. The failure to do so was a violation of its obligations under the Securities Acts.[22] Statements in literature which have no reasonable basis in fact are violative of the anti-fraud provisions of the Securities Acts.[23]

21/ Whitehall Corporation, 38 S.E.C. 289 (1958); A. G. Bellin Securities Corp., 38 S.E.C. 178 (1959); Irving Grubman & Co., 40 S.E.C. 671 (1961).

22/ James F. Morrissey, et al., 25 S.E.C. 372 (1947); Central Oils Incorporated, 39 S.E.C. 349 (1959); B. J. Johnson & Company, 20 S.E.C. 429 (1945).

23/ Alexander Reid & Co., Inc., 40 S.E.C. 986 (1962); N. Sims Organ & Co., Inc., 40 S.E.C. 573 (1961).

51. The salesmen fully participated in the registrant's sales campaign and repeated misrepresentations contained in the literature prepared on behalf of the registrant and added their own embellishments to it. Under the circumstances, the salesmen should not have accepted at face value the over-optimistic representations and assumptions in the registrant's literature. They had a duty to inquire here to determine the basis for the representations made.[24/] A cursory examination of the registrant's literature would have revealed there was no reasonable basis for the optimistic predictions of oil recoveryand profits from the registrant's proposed drilling and that there were other substantial misrepresentations and omissions all through the literature. This obligation of inquiry applied particularly to Dunklee and Shayne, who caused telegrams to be sent to potential investors and who stated in other literature that they had thoroughly investigated the registrant and its offerings. It is concluded that by their activities the registrant and the individual respondents willfully violated the anti-fraud provisions of the Securities Acts, as alleged in the order for these proceedings.

52. The registrant also violated the anti-fraud provisions of the Securities Acts by mailing confirmations of sales to persons whose orders had been solicited but who had not in fact agreed to purchase any participations.[25/] These incidents occurred in sufficient number to indicate

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24/ Mac Robbins & Co., Inc., Sec. Exch. Act Rel. No. 6846 (July 11, 1962, aff'd sub nom Berko v. S.E.C., 316 F. 2d 137 (1963).

25/ J. A. Winston & Co., Inc., Sec. Exch. Act Rel. No. 7337 (June 8, 1964); Palombi Securities Co., Sec. Exch. Act Rel. No. 9961 (November 30, 1962); Thompson & Sloan, Inc., 40 S.E.C. 451 (1961); P. J. Gruber & Co., Inc., 39 S.E.C. 17 (1958).

this was a regular practice indulged in by the registrant and its salesmen.

E. Violations of the record-keeping requirements

53. The registrant, as a registered broker-dealer, was required to make and keep current certain books and records as specified in Rule 17 CFR 240.17a-3, promulgated by the Commission pursuant to the provisions of Section 17(a) of the Exchange Act. Rule 17 CFR 240.17a-4 specifies records which must be preserved by every broker and dealer. The evidence establishes that required books and records were not made and kept current by the registrant and that Hahn destroyed records which should have been preserved such as copies of confirmations, copies of correspondence, mailing cards of persons contacted or to be contacted by registrant, letters received from prospective customers, paid and unpaid bills, and invoices and correspondence. In addition, at least in one instance, the recording of commission payments made to Fisher, false entries were made in the registrant's books.[26/]

54. It is concluded that the registrant willfully violated Section 17(a) of the Exchange Act and Rules 240.17a-3 thereunder and that the respondents Helmke, Foltz, Messina and Hahn, persons in control of the registrant, aided and abetted the registrant in these violations.[27/]

26/ The requirement that books and records be kept includes the requirement that such books and records be true and correct. Lowell Niebuhr & Co., Inc., 18 S.E.C. 471 (1945); Pilgrim Securities, Inc., 39 S.E.C. 172 (1959).

27/ Empire Securities Corporation, 40 S.E.C. 1104 (1962).

III. CONCLUSIONS OF LAW; RECOMMENDATIONS

It has been found that the registrant, aided and abetted by the individual respondents herein, willfully violated Section 15(b) of the Exchange Act and Rule 17 CFR 240.15b-2 thereunder in that registrant made in its application for registration and amendments thereto statements which were, at the time and in the light of the circumstances under which they were made, false and misleading with respect to material facts and that no amendments to registrant's broker-dealer application were made to correct these inaccuracies. It has also been found that the registrant and the individual respondents willfully violated the registration provisions of the Securities Act. It has further been concluded that the respondents willfully violated the anti-fraud provisions of the Securities Acts. Finally, it has been found that the registrant, aided and abetted by the individuals in control of its operations, Helmke, Foltz, Messina and Hahn, willfully violated the record-keeping provisions set forth in the Exchange Act and rules promulgated thereunder.

The Commission, pursuant to the provisions of Section 15(b) of the Exchange Act as now amended, so far as it is material herein, is required to revoke the registration of any broker or dealer if it finds that such revocation is in the public interest and that such broker or dealer, subsequent to becoming such, or any person associated with such broker or dealer, willfully violated any provision of the Securities Acts or any rule or regulation thereunder. Willful violations by the registrant, its principals and the salesmen associated with it, have been found.

The registrant, Helmke, Foltz, Hahn and Messina, did not appear at the hearings herein. They did file a joint statement in the nature of an answer. In this answer they denied that they had any intention to mislead anyone or to willfully violate any applicable laws or rules. They denied knowledge of the past employment history of Shayne, Dunklee and Fisher and stated that Shayne took care of the salesmen, bookkeeper, advertising, brochures, mailing and telephone procedures and on many days ran the Allstate offices alone. Finally, it is stated that Allstate was of the opinion that Rowe's valuations were honest and educated opinions.

This answer, not substantiated by any evidence, even if accepted at face value, evidences that the registrant and its principals abdicated functions and responsibilities owed to the investing public. The evidence demonstrates that the registrant's program called for drillings in the nature of "wildcat" operations. Available information on the El Dorado, Buhler and Nicholson leases showed the existence of dry holes and should have, at the very least, alerted the registrant and its officers to do further checking on the very optimistic forecasts furnished them. They certainly knew Rowe's financial interest in their engaging in drilling operations on land where his company held a beneficial interest. Instead of checking, they accepted exaggerated estimates and embroidered them in making their presentation to investors. The evidence clearly establishes that the registrant and its principals conducted their business with gross disregard of their responsibilities under the Securities Acts and disregard

of the interests of investors.[28/]

The contention that great reliance was placed by the registrant and its principals on Shayne is also without merit. The registrant, through its officers, were under a general obligation to supervise the employees of the registrant in the performance of their duties. Hahn was in actual control of the registrant's office in New York and neither he nor the other principals had a right to abdicate their statutory duties to supervise the activities of the salesmen. The Commission, in the case of Reynolds & Co., 39 S.E.C. 902 summarized the responsibility of a registrant and its officers for the activities of its salesmen in the following language:

> "Customers dealing with a securities firm expect, and are entitled to receive, proper treatment and to be protected against fraud and other misconduct, and may properly rely on the firm to provide this protection.
>
> * * *
>
> In the light of these considerations we are of the opinion that, where the failure of a securities firm and its responsible personnel to maintain and diligently enforce a proper system of supervision and internal control results in the perpetration of fraud upon customers or in other misconduct in willful violation of the Securities Act or the Exchange Act, for purposes of applying the sanctions provided under the securities laws such failure constitutes participation in such misconduct, and willful violations are committed not only by

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28/ There is some evidence that various offers of restitution were made to some of the investors in the nature of promises of repayment, issuance of promissory notes, or the issuance of shares in another oil venture. Nothing concrete came of these offers and, as noted before, escrow arrangements which were supposed to protect investors, were never carried out.

> the person who performed the misconduct but also by those who did not properly perform their duty to prevent it." (footnote omitted; p. 917) 29/

It is clear that no effective supervision was exercised over the salesmen and that they were free of any supervision of their activities and could and did make the misrepresentations found without any effort by Hahn and the other principals to see that they were properly instructed and supervised in their activities. It is concluded that the registrant and its officers and Hahn are responsible for the activities of the salesmen and their violations.

Of the salesmen, Shayne, Dunklee, and Fisher, the latter two have signed stipulations consenting to being named as causes of any order which may be entered against the registrant. Shayne alone appeared at the hearing, questioned witnesses, and gave evidence in his own behalf. While Shayne did not submit any brief or proposed findings, he did sent a letter to the undersigned in which he stated that he had great faith in Hahn and his associates, he thought he had finally met some legitimate oil dealers, and only repeated what Hahn had states about the leases, the escrow arrangements and the "out-of-pocket" guarantee.

The contentions made by Shayne fail to take into account Shayne's responsibility as a security salesman. He accepted at face value information furnished by Allstate as to the value of leaseholds. He apparently made no analysis of the literature as was his responsibility before passing

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29/ See to the same effect Best Securities, Inc., 39 S.E.C. 931 (1960); W. M. Bell & Co., 29 S.E.C. 709 (1949); L. H. Feigin, 40 S.E.C. 594 (1961).

on misleading information to his customers.[30/] Instead of making a careful analysis which would have revealed that the registrant's claim as to the value of the leaseholds was exaggerated and not warranted by drilling experience in the areas involved, Shayne repeated and enlarged on these claims. The conduct of Shayne, as well as that of Dunklee, was particularly violative of the interests of investors in that he and Dunklee were parties to the telegrams sent to investors assuring them that they had personally and carefully investigated the registrant's claims. These assertions were reiterated in letters sent to customers. It is admitted that no such personal investigations were made. These salesmen clearly misled potential investors by this assurance. The activities of the salesmen in illegally furthering the plans of the other respondents lead to the conclusion that they all acted in concert in a scheme to defraud.[31/] In view of the violations found in Shayne's participation in the above fraud on investors, it is recommended that the Commission find that Shayne, as well as Dunklee and Fisher, are each a cause of the order of revocation which the undersigned has recommended be entered here.

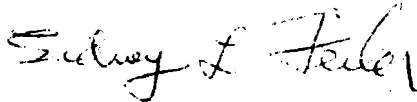
30/ Mac Robbins & Co., Inc. Sec. Exch. Act Rel. No. 6846, July 11, 1962; Berko v. S.E.C. (C.A. 2, 1963), 316 F. 2d 137.

31/ U.S. v. Ross and Gordon, 321F. 2d 61 (C.A. 2, 1963), cert. den. 375 U.S. 894 (1963); Mac Robbins & Co., Inc., supra.

Under all the circumstances, the undersigned concludes that it is in the public interest to revoke the registration of the registrant and recommends that the Commission issue such an order.

It is further recommended that the Commission find that Milton J. Helmke, George C. Foltz, Henry L. Hahn, and Joseph Messina, principals of the registrant, and Alfred Shayne, Donald B. Dunklee and William Fisher, salesmen of the registrant, are each a cause of the order of revocation which the undersigned has recommended be entered here. It is also recommended that the notice of withdrawal from registration filed by the registrant not be permitted to become effective.[32/]

Respectfully submitted,



Sidney L. Feiler
Hearing Examiner

Washington, D. C.

May 21, 1965

32/ All contentions and proposed findings submitted have been carefully considered. This Recommended Decision incorporates those which have been accepted and found necessary for incorporation herein.