

STATE OF OKLAHOMA
DEPARTMENT OF SECURITIES
WILL ROGERS MEMORIAL OFFICE BUILDING, 4TH FLOOR
P.O. BOX 53595
OKLAHOMA CITY, OKLAHOMA 73152

In the matter of:)
)
Walling Heirs Association)
2729 S.W. 44th)
Oklahoma City, OK 73119)
)
Beatrice J. Thedford)
2729 S.W. 44th)
Oklahoma City, OK 73119)
)
Karen Thompson)
2729 S.W. 44th)
Oklahoma City, OK 73119)
)
LaDonna Spradlin)
2729 S.W. 44th)
Oklahoma City, OK 73119)

ORDER

I. INTRODUCTION

This cause involved an application by the Oklahoma Department of Securities (Department) for a permanent cease and desist order to enjoin Walling Heirs Association (the Association) and certain named respondents alleged to be officers, employees or agents of the Association, from offering to sell or selling memberships in the Association. The Department formally commenced this cause through the issuance of a Summary Order to Cease and Desist and Notice of Intent to Issue Permanent Order to Cease and Desist, filed November 9, 1989. (Pleading File, Document No. 1). The Notice alleged that the memberships constituted securities under the Oklahoma Securities Act, 71 O.S. §§ 1, et seq. (the "Act"), and

that the Association had failed either to register the securities with the Administrator of the Department or to obtain an exemption from the Act's registration requirements. 71 O.S. § 301. The Notice also alleged a number of substantive securities law violations, including failure of the individual named respondents to register as broker-dealers, failure of the Association to obtain the Administrator's approval of sales literature used in connection with the sale of the alleged securities; and dissemination of information to prospective purchasers of Association memberships, which omitted material facts necessary to make the statements made, in the light of the circumstances under which the statements were made, not misleading. See, generally, 71 O.S. §§ 101, 201-202, 301.

An evidentiary hearing was held in this cause on December 18-20, 1989, and January 4, 1990, at which the Association and the individual named respondents were represented by counsel. The parties filed proposed findings of fact and post-trial briefs on January 16, 1990. The parties also agreed that the hearing officer would have until January 22, 1990, to issue his findings of fact and conclusions of law. The hearing officer, after consideration of the evidence and exhibits introduced at the hearing, and briefs and proposed findings submitted by the parties, hereby makes the following findings of fact and conclusions of law.

II. FINDINGS OF FACT

1. Walling Heirs Association is an unincorporated association doing business at 2729 S.W. 44th, Oklahoma City, Oklahoma. (Department's Pre-Hearing Conference Status Report, Stipulated Fact 1; Respondent's Pre-Hearing Conference Status Report, Stipulated Fact 1).

2. The Association was formally organized at a meeting held at the Southgate Inn in Oklahoma City, Oklahoma on May 9, 1987, which meeting was attended by approximately 300 individuals, many of whom believed they were heirs of John Walling, who died in the 1830's. (Trial Transcript, January 4, 1990, p. 67; Thedford Deposition, pp. 5-7). Prior to the formal creation of the Association, a number of presumed Walling heirs from time to time had gathered to discuss the possibility of seeking the funds to which they believed they were entitled. (Trial Tr., January 4, 1990, p. 52).

3. Beatrice Thedford (Thedford) organized the Association, and, has at all times relevant to this proceeding, served as President of the Association and as a member of the Board of Directors. (Thedford Deposition, p. 5). Karen Thompson, LaDonna Spradlin, and Juanita Stahlheber are also paid employees of the Association. (Respondents' Stipulated Facts 7-9; Trial Transcript, December 18, 1990, p. 106).

4. Thedford actively recruited members for the Association by placing newspaper advertisements seeking individuals who believed themselves to be heirs of John Walling, Jr. (Thedford Deposition, p. 8; Trial Transcript, December 18, 1989, p. 106).

5. The Association is governed by a Board of Directors, which initially consisted of Juanita Stahlheber, Judy Vanderford, Beverly Watters, and Oweeda Smith. The Board adopted bylaws, the initial set of which was prepared by a Brown Peregory, who assisted Thedford in the establishment of the Association. Thedford and Peregory appointed the initial Board members. (Thedford Deposition, p. 9; Trial Transcript, January 4, 1990, p. 67).

6. Brown Peregory and his wife were paid \$25,000.00 by the Board for their assistance in setting up the Association and preparing the initial set of bylaws. (Thedford Deposition, pp. 18-19).

7. Membership in the Association was sold for \$200.00, with an annual dues obligation of \$25.00 per year. Of the initial membership fee of \$200.00, the Association had promised to set \$50.00 aside for administrative and other administrative costs, and \$150.00 for legal expenses. Some individuals received membership in return for services performed by them for the Association. (Thedford Deposition, p. 18; Trial Transcript, December 18, 1989, p. 17). There are currently in excess of 4,000 members of the Association.

8. The purpose of the Walling Heirs Association is to raise money to file a law suit to identify any assets or claims that might be owed to its members that arise from the Estate of John Walling, Sr., or his immediate relatives; to hire a lawyer to prosecute that law suit; to fund the research necessary for the prosecution of that law suit; and to represent all members of the Association in any negotiated settlement of the law suit. (Thedford Deposition, p. 6; Respondents' Pre-Hearing Conference Status Report, p. 3; Trial Transcript, December 18, 1989, p. 15).

9. Individuals who purchased memberships in the Association paid for those memberships with the expectation of receiving a profit from the Association's activities. (Trial Transcript, December 18, 1989, p. 15; December 19, 1989, pp. 13-14).

10. The original bylaws and articles of the Association set forth the structure of the Association. Those bylaws and articles provide (1) the Association's purpose is to hire a law firm to investigate and pursue the claims of the heirs of William Walling; (2) all members are subject to the approval of the Board of Directors (3) the Board of Directors, by majority vote, may reject or suspend a member; (4) the Board is empowered to appoint spokesmen; (5) a nomination committee chosen by the Chairman of the Board, with the consent of the Board, nominates the Directors; (6) all Association bank accounts shall be "for the expenses of Beatrice Thedford for Association business," and may be used by her as "deemed necessary"; (7) the Board is empowered to take all reasonable actions to pursue Association goals; and (8) the

Association members grant to the Association, acting through its Board, exclusive authority to investigate all matters involving the purposes of the Association. (Ex. 22, Trial transcript, December 19, 1989, pp. 69-70, 80).

11. The name of the Association was originally William Walling Association and was subsequently changed to the Walling Heirs Association. The name was changed to enable the members to recover assets purportedly deriving from the estate of John Walling, Sr. This change-in-name did not disturb the continuity of the Association, which dated from its establishment in May, 1987. (Trial Transcript, December 19, 1989, pp. 127-128).

12. The bylaws and articles were amended on several occasions. The purposes of the Association remained basically the same, except the bylaws now provide that the purpose is to locate and identify the assets of John Walling, Sr. Also, the articles explicitly provide that of the \$200.00 membership fee, \$50.00 shall be taken out for expense and \$150.00 put into an account for legal fees. Also, in the event of a recovery, the "head heirs" are to assign over a ten percent "finders fee" to be divided equally among the "non-head heir" members of the Association. (Ex. 10).

13. Membership was not limited to those who believed themselves heirs of John Walling, Sr. In fact, the Association solicited membership of individuals who were "finders' fee" members. These "finders' fees" were promised a share of ten percent of the top of any recovery from the estate of John Walling, Sr. Potential members were urged to join as "finders' fee"

members, even though they had advised Association employees they were not heirs--or even related by marriage to heirs--of John Walling Sr. In fact, Beatrice Thedford, the President of the Association, offered a membership to a newspaper reporter, who interviewed her about the Association, even though the reporter was not an heir of John Walling, Sr. (Trial Transcript, December 18, 1989, pp. 18, 141-142, 160, 169).

14. Originally, the finders' fee heirs were to obtain ten percent of any recovery off the top, before payment of attorneys' fees. Subsequently, this was changed to permit recovery only after payment of attorney's fees. There was no evidence that this change was communicated to the finders' fee members. (Trial Transcript, December 18, 1989, p. 113).

15. Promotional materials containing newspaper articles were mailed to potential members and members of the Association. These materials represented to potential and new members that the type of law suit necessary to recover from the Estate of John Walling, Sr. would be very expensive for individuals and small groups to pursue, and that membership in the Association increased the chances of recovery. (Thedford Deposition, p. 43; Trial Transcript, December 18, 1989, p. 36; State's Ex. 1).

16. The membership agreements executed by the members also described the purposes of the Association and the relationship between the individual members and the Association. They contained language indicating that the "members realized that [they] alone could not afford to prosecute any claim that [they] may have

without the support of the [other members]." These memberships also stated that if members were no longer in good standing, they would not be entitled to any benefits or participation in the Walling Heirs Association. The Association's bylaws conferred on the Board broad powers to suspend a member for "misconduct" or "cause." (Respondent's Exhibit 3, State's Ex. 10).

17. While members of the Association may not have been prevented or discouraged from sharing their views with members of the Board, the members were not required to perform any work on behalf of the Association. They were not required to do anything other than pay for their membership fees and annual dues to the Commission. (Trial Transcript, December 18, 1989, pp. 167-169).

18. The members did not vote to either hire or to pay Brown Peregory. (Trial Transcript, January 4, 1990, p. 141).

19. The law firm of Bailey and Williams was formally retained by the Association the first week of December, 1987. The evidence is in dispute as to whether the members actually voted to retain the firm prior to the December meeting of the Board. (Trial Transcript, January 4, 1990, pp. 6-7, 78). However, it was the testimony of the Association President Thedford, that the Board retained power to approve the hiring of Crook's firm. (Thedford Deposition, p. 10). Judy Vanderford, another witness, testified that as a Board member she had voted to retain Bailey and Williams. (Trial Transcript, December 19, 1989, p. 78).

20. Beatrice Thedford was the only member of the Board who signed the initial fee agreement with this firm on behalf of the Association. Carter Crook signed the agreement on behalf of Bailey and Williams. The sum of \$35,000.00 was paid to Carter Crook at the time this fee arrangement was signed. (Trial Transcript, December 19, 1989, pp. 82-83). Carter Crook later left the law firm of Bailey and Williams, but nevertheless continued to serve personally as the chief legal counsel. There was no evidence that the members as a whole were given a vote on the initial decision to retain Crook after he left his employ at Bailey & Williams.

21. There was a time when some of the individual members communicated with Carter Crook directly about Association matters. However, Beatrice Thedford and Mr. Crook subsequently advised the members not to communicate directly with Mr. Crook, but to communicate their concerns to Beatrice Thedford. After this time, Beatrice Thedford communicated with Crook on Association business, to the exclusion of other members. (Trial Transcript, January 4, 1990, pp. 118-122).

22. On November 18, 1989, the Walling Heirs Association held a meeting. Because notice of this meeting was mailed bulk mail, an unknown number of the members did not receive timely notice. (Respondents' Exhibit No. 4; Trial Transcript, January 4, 1990, p. 105).

23. Beatrice Thedford served as President of the Association and dominated the activities of the Association and the Board. There was testimony that her fellow Board members were not

consulted and did not have an opportunity to vote on Association business decisions. (Trial Transcript, December 19, 1989, p. 92).

24. At the November, 1989, meeting, the members ratified a number of the Board's past activities. The members voted to (1) approve the continued rental of office space at 2729 Southwest 44th Street, Oklahoma City; (2) approve continued rent of space at \$700.00; (3) waive any conflict of interest that might arise from renting space owned or purchased by Beatrice Thedford; (4) continue payment of salaries to Beatrice Thedford and other named employees; (5) ratify the Directors' past employment of attorneys; (6) continue the employment of Carter Crook; (7) ratify all past acts of the Board; and (8) continue to grant the Board of Directors authority to make additional amendments. (Respondents' Exhibit 4; Trial Transcript, January 4, 1990, Stahlheber testimony).

25. Prior to this meeting in November, 1989, there was not a vote by the membership to approve or initiate the filing of a lawsuit in Texas. No vote on the filing of a lawsuit has been held since the meeting. Similarly, there was no vote of the members prior to this 1989 meeting to pay Beatrice Thedford's salary, other employee salaries, or to pay rent on a building owned by Thedford. (Trial Transcript, January 4, 1990, pp. 154, 157).

26. An Association member and Director testified on behalf of the Respondents that the question on the ballot, "Shall the Board continue to have authority to make additional amendments", was intended to request blanket authority from the members to the Board to amend anything at all, including amendments to the bylaws

and articles, to the attorney contract, and to lease agreements.

27. The Directors and employees of the Association had been advised of the risks of seeking recovery through a lawsuit from the estate of an individual who died in the 1830's. These risks included the possible bar to an action posed by the statute of limitations. (Thedford Deposition, p. 128; Thompson Deposition, p. 39).

28. Beatrice Thedford and other Board members were advised by their legal counsel that the sale of Association memberships could be sales of securities under state law. (Trial Transcript, December 18, 1989, pp. 25-26, Trial Transcript, December 20, 1989, pp. 45, 53).

29. Association funds were commingled with the personal funds of Beatrice Thedford, and moneys from these commingled accounts were used to pay the personal expenses of Thedford. A personal loan was made by Beatrice Thedford to her sister from Association funds. (Trial Transcript, December 18, 1989, pp. 97-98; Trial Transcript, December 20, 1989, Miner Testimony; States Exhibit 29).

30. Association funds were not spent in accordance with the provision set out in the articles and bylaws which required that 75% of all membership fees be set aside in a trust account to be used for attorney fees. (Trial Transcript, December 20, 1989, p. 38, State's Ex. 29).

31. Salaries were paid to Karen Thompson and LaDonna Spradlin, daughters of Beatrice Thedford, from Association funds,

as well as to Beatrice Thedford. (Respondents' Pre-Hearing Conference Status Report, p. 23).

32. The Association office is located on property at 2729 S.W. 44th Street. The Association paid Beatrice Thedford's mortgage payments in this property, as well as her insurance and utility bills. (Thedford Deposition, p. 24).

33. Prior to joining the Association, members were not advised that (1) salaries were paid to Thedford and other officers and employees out of Association funds; (2) Association funds were used to pay the mortgage payments, rent, and utilities at the Association's headquarters; (3) Association funds would be commingled with Beatrice Thedford's personal funds, and Mrs. Thedford would pay for her personal expenses out of Association funds; (4) the memberships had not been registered as securities, (5) the Association funds were not being devoted 75% to attorney's fees. Nor is there any evidence that members were informed of statutes of limitation problems and other risks attendant to the recovery of the assets of an individual who died in the 1830's. (Trial Transcript, December 18, 1989, pp. 29, 31; January 4, 1990, p. 11; December 19, 1989, pp. 10-11) .

34. Prior to the members' annual meeting, in 1989, the members had not been given an opportunity to approve salaries, the filing of a law suit, or the payment of rent, utilities and insurance out of Association funds.

35. Several members testified that their decision to purchase memberships in the Association would have been affected had they been made aware of the information described in Finding of Fact 33, above. (Trial Transcript, December 29, 1989, p. 11).

36. Membership interests in the Association are not registered with the Oklahoma Department of Securities, nor has the Association applied for an exemption from registration with the Oklahoma Department of Securities. (Trial Transcript, December 18, 1989, p. 189).

37. The Respondents, Beatrice Thedford, LaDonna Spradlin and Karen Thompson are not registered as broker-dealers nor as agents of a broker-dealer or issuer thereof in the State of Oklahoma. (Trial Transcript December 18, 1989, p. 190).

38. The promotional and sales literature used by Respondents to solicit the membership omitted the following material facts:

- i. the organizational structure of the Association;
- ii. Respondents' prior business histories, proposed plan of operation, knowledge and experience of officers and principals of the Association, or compensation to management and/or affiliates of the Association;
- iii. financial information for the Association and the principals of the Association;
- iv. the proposed and actual use of proceeds from the sale of membership interests in the Association;
- v. the deposit of Association funds into Thedford's personal bank account from May 1987 through February 1988;
- vi. the risks of an investment with the Association;
- vii. the failure of the Association to comply with the provisions of the Act;

- viii. the amount of salaries paid to Thedford and members of her family by the Association from members' contributions; and
- ix. the use of Association funds to pay mortgage payments, utilities and insurance on property owned by Thedford.

(State's Exhibit #1, Trial Transcript December 18, 1989, p. 1 et seq.

39. The promotional and sales literature utilized by the Association was not filed with the Administrator for her approval, in violation of Rule R-402 of the Administrative Rules of the Oklahoma Securities Commission. (Trial Trans. December 18, 1989, p. 190).

CONCLUSIONS OF LAW

The threshold issue is whether the sales of memberships in the Association constituted sales of "securities" for the purposes of the Oklahoma Securities Act, 71 O.S. Supp. 1989, §§ 1, et seq. The Act lists a number of items under the definition of "security", two of which are relevant to our inquiry. Section 2(r) of the Act states that a "security" means any:

* * *

(11) investment contract

* * *

(16) investment of money or money's worth including goods furnished or services performed in the risk capital of a venture with the expectation of some benefit to the investor where the investor has no direct control over the investment or policy decision of the venture.

The purpose of securities regulation is to protect the investing public. For this reason, the courts have held:

[The definition of security] embodies a flexible rather than a static principle, one that is capable of adaptation to meet the countless and variable schemes devised by those who seek the use of the money of others on the promise of profits.

Securities and Exchange Com'n v. Howey Co., 328 U.S. 293, 299, 90 L.Ed. 1244, 66 S.Ct. 1100 (1946) ("Howey"), State ex rel. Day v. Petco Oil and Gas, 558 P.2d 1163 (1977) ("Petco"). The hearing officer is mindful of the need for flexibility in the determination of what constitutes a security. The hearing officer also believes it appropriate to construe the Oklahoma Securities Act's definition of "security" with reference to federal and state cases construing the same term in the context of similar or related statutory schemes. See 71 O.S. § 501.

Investment Contract

In the Supreme Court's Howey decision, "investment contract", for the purpose of the federal securities laws, was defined as:

[A] contract, transaction, or scheme whereby a person invests his money in a common enterprise and is led to expect profits solely from the efforts of the promoter or third party.

328 U.S. at 299. This definition has been adopted in a number of states, and was cited with approval in Petco, 558 P.2d at 1166. The hearing officer believes it appropriate to use the definition of investment contract employed in Howey for the instant analysis.

The Howey test requires that four separate criteria be satisfied in order for an instrument to constitute a "security". These are (1) investment of money in a (2) common enterprise with (3) an expectation of profit (4) solely through the efforts of others. Each of these criteria is satisfied in the instant case.

First, there is no dispute but that memberships in the Association were sold for "an investment of money". The memberships were sold for a \$200.00 initial membership fee, and \$25.00 annual dues.

The second prong is that there be an investment of money in a "common enterprise." The membership agreements, and articles and bylaws of the Association, as well as the oral testimony, make clear that the pooling of resources to fund a law suit and related legal research, was the essential purpose of the Association. The membership agreements themselves recited acknowledgements that the individual members realized that they alone could not afford to prosecute claims without the support of other members.

Respondents brought out some evidence that an heir's participation in any recovery from the estate of John Walling, Sr., would depend on the independent existence of a valid claim to a portion of that estate. But even if this were the case, there was clearly a "common enterprise" attendant to the funding of a law suit which would supposedly recover the legitimate claims of the heirs. The fact that an investor's individual return is independent of that of other investors does not preclude the satisfaction of the common enterprise element of an investment

contract if the fortunes of all investors, in the final analysis, depend on the efficacy of the promoters' efforts. A pro rata sharing of the profits is not required. See Jones v. International Investors' Inc., 429 F. Supp. 119 (D. Ga. 1977); Plunkett v. Francisco, 430 F. Supp. 235 (D. Ga. 1977).

Moreover, there is no dispute that the Association also knowingly offered and sold memberships to non-heir "finders' fees" applicants, some of whom were not even related by marriage to a plausible Walling heir. Such finders' fees clearly could not possibly have sought recovery from the Walling estate through an individual legal action. They relied exclusively on the common enterprise--which had adopted a ten percent set aside for the "finders' fee" memberships--for their expectation of recovery.

The third criteria that must be satisfied is that the investment be for the "expectation of profit." This test is also satisfied, as the purchasers looked to the activities of the Association in the expectation of receiving a monetary return from those activities. The case is distinguishable from that presented in In re Epic Mortgage Insurance Litigation, 1989 CCH Fed.Sec.Rptr. ¶ 94, 526 (E.D. Va. July 28, 1988), where the fixed rate of return offered by the underlying notes was not dependent on the efforts or activities of a common venture. In our case, the prospects of a return on the initial investment depend on the Association's successful efforts to raise sufficient funds to prosecute a law suit and the successful prosecution of that suit.

The only close issue is the final criteria: whether the investor is "led to expect profits solely from the efforts of the promoter as third party." There was evidence, for example, that some members may have engaged in Association-related activities without prior approval or direction from the Board or from Mrs. Thedford. Judy Vanderford, for example, ran an ad in a Dallas, Texas newspaper looking for prospective heirs. Vanderford also had conversations with the Association's attorney, Carter Crook, to discuss Association matters. Certain members of the Association also performed document searches at courthouses, which they presumably believed helpful to the Association or to their individual determination of heirship. Some of these activities may have taken place without the prior approval or direction of the Board. At the same time, there was testimony from other members that they were neither expected nor required to perform any Association activities when they purchased their Association memberships.

Indeed, the only membership agreement introduced into the record contained absolutely no language suggesting that the members retained the power to control or direct Association activities. Just the opposite appears to be the case, since in the membership agreement the members pledge to cooperate with the Board, to permit the Board to speak on their behalf, and to abide by the bylaws of the Association as written or amended by the Board. Respondents' Ex. 3. There is no indication that the individual members at the time they purchased their memberships were given voting rights to

elect Board members or given any power to select the Association's lawyer or to direct the lawyer's conduct of his work once he was chosen. Further, the articles and bylaws of the Association provided no powers in the general membership to elect Board members or hire or supervise the attorney handling the lawsuit. The articles and bylaws provided instead that Board members and officers would be elected by the Board themselves, and that officers would serve for the duration of the law suit or until their successor was appointed. The Board of Directors--not the individual members--were given powers to enter into contracts necessary to pursue the law suit and to supervise that suit. Further, Beatrice Thedford, the Association President, was given considerable personal powers to spend Association money "as deemed necessary by her" to assist in the pursuit of a Court action. (State's Exhibits 10, 13).

A literal reading of the Howey test would exclude from the definition of security any arrangement where the investor plays any role in the profit-making activities. Mindful of the protective purposes of the federal and state securities laws, the courts have not construed the term so narrowly. In S.E.C. v. Glen Turner Enterprises, 474 F.2d 476, 482 (9th Cir., cert. denied 414 U.S. 821 (1973)), the Ninth Circuit stated:

Strict interpretation of the requirement that profits to be earned must come "solely" from the efforts of others has been subject to criticism. See, e.g., State of Hawaii v. Hawaii Market Center, Haw. 1971, 485 P.2d 105. Adherence to such an interpretation could result in a mechanical, unduly restrictive view of what is and what is not an investment

contract. It would be easy to evade by adding a requirement that the buyer contribute a modicum of effort. Thus the fact that the investors here were required to exert some efforts if a return were to be achieved should not automatically preclude a finding that the Plan or Adventure is an investment contract. To do so would not serve the purpose of the legislation. Rather we adopt a more realistic test, whether the efforts made by those other than the investor are the undeniably significant ones, those essential managerial efforts which affect the failure or success of the enterprise.

Accord, Meyer v. Dans un Jardin, S.A., 816 F.2d 533 (10th Cir. 1987). The hearing officer has determined that this is the appropriate test in the instant case.

It is clear that the significant efforts by the Walling Heirs Association were performed either by the Board, or by Mrs. Thedford, personally. There was conflicting testimony as to whether the members voted to approve the hiring of Carter Crook's law firm, Bailey and Williams. However, two present or former Board members--Beatrice Thedford and Judy Vanderford--stated that the Board approved the hiring of Crook. Also, while certain members had telephone conversations with Crook about association activities in the early days of the Association, the power to communicate with Crook was later centralized in Beatrice Thedford. Further, the filing of the law suit was commenced without members' approval. Mrs. Thedford was personally vested with authority to spend Association funds in pursuit of the Association's objectives, as she deemed necessary to assist the attorneys. Mrs. Thedford exercised broad powers over other areas of the Association

activities, and there is some doubt as to whether she even consulted other directors about Association matters. Finally, there is no testimony or evidence that Mrs. Thedford was required to communicate the members' concerns about litigation strategy to Crook, or that she periodically polled all the members for the purposes of obtaining their input or direction as to the proper conduct of the suit. The evidence also indicates that the members were never offered an opportunity to approve, from the outset, the retention of Carter Crook after he left the employ of Bailey and Williams.

To be sure, there was a members' meeting in November, 1989, at which members were given an opportunity to ratify past Association decisions. But the key issue is whether a security existed at the time the membership was purchased by an Association member. Great Western Bank and Trust v. Kotz, 532 F.2d 1252 (9th Cir. 1976) (nature of instrument is to be determined at time of issuance, not at subsequent time). The ratification by the members of past activities of the Board or Mrs. Thedford does not insulate the memberships from the reach of the Securities Act, when the members had not been clearly empowered to exercise control over the Association at the time of the activities later complained of. The clear wording of the membership agreement and the bylaws indicates that managerial authority was to be concentrated in the Board or Mrs. Thedford. In fact, Respondents' only witness--an Association member and Board member--conceded that the Board sought, and obtained, from the members at the November, 1989 meeting, blanket

permission to amend anything at all relating to Association activities. Thus, the Board members themselves recognized that they had broad discretionary owners to change even those matters which had been approved at the November, 1989 meeting.

Risk Capital Test

The hearing officer also finds that the membership in the Association satisfies the risk capital test found in 2r(16) of the Act. First, the members clearly invest money or money's worth. Second, the funds are clearly invested in risk capital, as they are exposed to loss or profit arising from the successful employment of capital in the venture. Third, the venture element is satisfied, as the Association is clearly engaged in a combined or concerted effort to finance and prosecute a law suit. Fourth, it is clear that the investor is seeking some benefits, in the form of a recovery from the Estate of John Walling. Finally, it is also clear, for the reasons set out in the discussion above, that the investor has no direct control over the essential policy decision of the venture.

The counsel for Respondents place great weight on a statute which permits a voluntary association to bring a law suit on behalf of representative parties. This section, 12 O.S. 1989 Supp., § 2023.2, provides that:

[A]n action brought by the members of an unincorporated association may be maintained only if it appears that the representative parties will fairly and adequately protect the interests of the association and its members. In the conduct of this action the Court may

make appropriate orders corresponding with those described in subsection D of [12 O.S. 1989 Supp., § 2023], and the procedure for dismissal or compromise of the action shall correspond with subsection E of [12 O.S. 1989 Supp., § 2023].

(emphasis added).

The hearing officer notes that in their pre-trial Opposition Brief (Pleading File, Document 9), Respondents omitted the important limiting word "only" from their quote of the statute, and also omitted the language clearly incorporating by reference the statute governing the conduct of class action law suits--12 O.S. 1989 Supp., § 2023. The Respondents would apparently have this hearing officer believe that § 2023.2 is a permissive, rather than a restrictive, grant of authority to representatives of unincorporated associations. The hearing officer is unwilling to conclude that the representatives of the Association have satisfied the statutory mandate which requires that they show they accurately represent the interests of their members. Nor has the Association even attempted, to the knowledge of the hearing officer, to satisfy the requirements of a class action law suit under Oklahoma or Texas Codes of Civil Procedure. See 12 O.S. Supp., 1989, § 2023 and Texas Rules of Civil Procedure, Rule 42; Life Insurance Co. of the Southwest v. Brister, 722 S.W. 2d 764 (Texas Civ. App.-Fort Worth 1986).

RELIEF

WHEREFORE, the undersigned hearing examiner concludes as follows:

1. The membership interests being offered for sale and sold by the Respondents are securities as defined in Section 2(r)(11) and (16) of the Act.

2. Respondents have offered for sale and sold securities in the State of Oklahoma without registering the securities or obtaining an exemption from registration pursuant to Section 401 of the Act, all in violation of Section 301 of the Act.

3. Respondents have offered for sale and sold securities in the State of Oklahoma without registering as broker-dealers or agents pursuant to Section 202 of the Act, all in violation of Section 201 of the Act.

4. The disclosures and information disseminated by Respondents to prospective purchasers omit material facts necessary to make statements made, in the light of the circumstances under which the statements were made, not misleading, in violation of Section 101 of the Act. These omissions include a failure to inform the members and applicants of the risks attendant to seeking recovery on an estate of a man who died approximately 150 years ago; failure to inform the members of the likely costs of pursuing such a claim, and the risks that the Association might not be able to raise enough funds to finance such a law suit; failure to inform the members and applicants that the memberships had not been registered as securities for the purposes of the Oklahoma

Securities Act, failure to inform the members and potential members that Association funds had been commingled with Beatrice Thedford's personal funds or that Beatrice Thedford was empowered to exercise almost single-handed control over the Association finances; failure to inform the members and potential members of the salary levels paid by the Association to Thedford and other Association employees; failure to inform members and potential members that Association funds were not devoted 75% to payment of attorneys fees.

5. Respondents have used sales literature in connection with the offer or sale of a security which was not filed with or approved by the Administrator, in violation of Section 402 of the Act.

6. Issuance of this Permanent Order to Cease and Desist pursuant to Section 406 of the Act is in the public interest.

RULINGS ON PARTIES' PROPOSED FINDINGS

RESPONDENT'S PROPOSED FINDINGS

Proposed Findings 1-6

The Respondents' proposed findings focus on the fact that the Association originated in the concern of Walling family members, dating back perhaps to the 1940's, with the issue of whether they were entitled to any money from the estate of a deceased ancestor. This is not relevant to the determination of whether the memberships sold after the formation of the Association in May, 1987, constituted securities. As set forth in my Findings of Fact,

the memberships advertised and sold to purported heirs and finders' fees after that date constituted securities.

Proposed Findings 7-9

These proposed findings are essentially correct, except that the testimony indicated that only 250-300 people may have been present at the meeting. (Trial Transcript January 4, 1990, p. 75).

Proposed Findings 10-12, 14-15

Who hired Carter Crook? There was conflicting testimony on this issue, as Respondents' only witness testified that Crook's law firm was hired by a show of hands at the November, 1987 meeting. (Trial Transcript, January 4, 1990, p. 78). There was also testimony that members did not vote on the retention of Carter Crook's firm for their lawyer. (Trial Transcript, January 4, 1990, pp. 6-7). Further, Mrs. Thedford, the President of the organization, indicated that the final approval of the hiring of Bailey and Williams remained subject to the Board's approval. (Thedford Deposition, p. 10). Another Board member, Judy Vanderford, testified that the Board had retained Bailey and Williams. (Trial Transcript, December 19, 1989, p. 19). The hearing officer finds it appropriate to give greater weight to Mrs. Thedford's testimony, as she was the President and key spokesman for the Association.

Even if we accepted that the members voted to retain Carter Crook's law firm in November, 1987, there is no evidence that the members as a whole voted to retain Carter Crook after he left the employ of Bailey and Williams. Further, it appears that Carter Crook was the only lawyer presented or introduced to the members by the Board, raising a doubt as to whether the Board afforded the members any genuine choice in the matter. Finally, there is no dispute but that (1) the power to communicate with and give direction to Carter Crook became concentrated in the hands of Beatrice Thedford. There was no testimony that Mrs. Thedford or the Board polled members or otherwise solicited advice as to the direction of the law suit, or that she was required to pass this advice or input on to Carter Crook; (2) the control over Association finances and the expenditure of funds in connection with the law suit were concentrated in the hands of Beatrice Thedford; (3) the Board sought and obtained approval from the members at the 1989 meeting, to amend the attorney relationship (or any other aspect of the Association's operations). On balance, the hearing officer does not find that the members exercised such direct control over the relationship with Crook as to remove the memberships from the scope of the securities laws.

Proposed Finding 13

This finding has been adopted by the hearing officer.

Proposed Findings 16-23, 28

The hearing officer does not find it relevant to the issues in this case that certain present or former members of the Association are disgruntled with the management of the Association. The issue of whether or not the memberships were securities does not depend on the level of content of any particular member or group of members with the activities of this organization.

Proposed Findings 24-27

The hearing officer finds that the members have not had considerable input or authority to direct the operation of the Association. The 1989 members' meeting served primarily to ratify past acts and indeed gave the Board blanket authority to amend at their discretion its legal relationship with its attorney, its articles and bylaws, or any other aspect of the Board's operations.

Department's Proposed Findings

The hearing officer's findings essentially incorporate each of the proposed findings, to the extent relevant, to the determination of the issues before him. However, with respect to Department's proposed findings 31-32, the hearing officer finds the evidence in dispute as to whether the members initially voted to retain the law firm Bailey Williams. However, as discussed above, the hearing officer does not find the resolution of this factual issue completely dispositive of the issue of whether or not a security existed, as control over the conduct of the law suit and

over the relationship with Crook remained in the hands of Beatrice Thedford or the Board.

Finally, the hearing officer declines to adopt the recommended finding that Respondents have engaged in acts, practices, and/or a course of business which operated as a "fraud or deceit" in violation of Section 101(2) of the Act. The hearing officer has not been referred to any case or statutory authorities that describe the level of scienter or intent necessary to establish this element of the Department's case, and is reluctant to find the existence of a "fraud or deceit" on the record before him.

Respectfully submitted,

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CERTIFICATE OF MAILING

On this 22 day of January, 1990, a true and correct copy of the foregoing was mailed to:

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