

FEDERAL TRADE COMMISSION

v.

THE GUARANTY FUND OIL COMPANY, E. M. THOMASSON, N. V. S. MALLORY, AND JOHN G. MENKE, INDIVIDUALLY AND AS TRUSTEES AND OFFICERS OF THE GUARANTY FUND OIL COMPANY.

COMPLAINT IN THE MATTER OF THE ALLEGED VIOLATION OF SECTION 5 OF AN ACT OF CONGRESS APPROVED SEPTEMBER 26, 1914.

Docket 864—January 16, 1923.

SYLLABUS.

Where two concerns, and individuals instrumental in, and responsible for their organization; for the purpose of aiding in the sale of said concerns' shares, and with a capacity and tendency so to do,

- (a) Caused to be distributed letters, circulars, maps and other literature, containing numerous essentially false and misleading assertions concerning the properties, assets, oil production, earnings, and prospects of said concerns, which had the capacity and tendency to deceive purchasers and prospective purchasers into believing them to be firmly established producing enterprises whose shares offered a safe and profitable investment;
- (b) Misrepresented alleged income from production available for dividends or interest, the fact being that at the time of said representations said concerns had no production;
- (c) Paid so-called dividends, not derived from earnings but provided by said individuals, upon outstanding shares at the rate advertised and represented, thereby rendering more plausible and credible the foregoing misrepresentations;

With the result that they were thereby aided in selling a large number of shares, to the injury of competitors:

Held, That such false and misleading advertising, and such misleading course of conduct, under the circumstances set forth, constituted unfair methods of competition.

COMPLAINT.

The Federal Trade Commission having reason to believe from a preliminary investigation made by it that The Guaranty Fund Oil Company; E. M. Thomasson, N. V. S. Mallory and John G. Menke, individually and as Trustees and Officers of said company have been and are using unfair methods of competition in interstate commerce in violation of the provisions of Section 5 of an Act of Congress entitled "An Act to create a Federal Trade Commission, to define its powers and duties and for other purposes," and it appearing to the Commission that a proceeding by it in respect thereof would be of interest to the public, issues this com-

Complaint.

5 F. T. C.

plaint, stating its charges in that respect on information and belief, as follows:

PARAGRAPH 1. The Guaranty Fund Oil Company is an unincorporated voluntary association operating under certain Articles of Association and a declaration of trust whereby E. M. Thomasson, N. V. S. Mallory and John G. Menke are made trustees to hold and administer the properties and assets of the Association. They also purport to act as President, Secretary and Treasurer, and Vice President, respectively, of the Guaranty Fund Oil Company. The said Articles of Association and declaration of trust were executed about the first day of September, 1921, and recorded in Stephens County, State of Texas. The principal office of said Association is in the City of Denver, State of Colorado.

PAR. 2. Ever since the formation of said Association the respondents Thomasson, Mallory and Menke, and each of them, acting for themselves as beneficially interested in said trust and acting for said Association as trustees and officers thereof, have been and are now, engaged in soliciting orders for and selling shares of beneficial interest in the properties, assets and business of said Association. In soliciting such orders said respondents have made and still make use of letters, circulars, maps and other literature setting forth information and representations concerning the oil leases, properties, assets and prospects of said Association, which said respondents send from the City of Denver, State of Colorado, to numerous prospective purchasers at their several places of residence in various States of the United States. Upon receiving orders for aforesaid shares as a result of such solicitation, said respondents fill the same by sending certificates for the shares so purchased, from said City of Denver to the purchasers of said shares at their several places of residence in various States of the United States.

PAR. 3. The aforesaid letters, circulars, maps, and other literature used in solicitation as above set out contain numerous false and misleading assertions concerning the properties, assets, oil production and prospects of said Association, among which are assertions to the effect that purchasers of shares will receive four per centum quarterly interest on the par value of the shares purchased, that the payment of such interest is guaranteed, that the Association owns producing oil wells or interests therein and is producing oil in sufficient quantities, and thus making sufficient earnings, to cover the payment of said four per centum interest out of earnings, that the Association is drilling for oil amidst wells producing great quanti-

ties of oil and is shortly to start drilling wells in such territory, and that the existing earnings from producing wells and the exceptionally good prospects of finding large quantities of oil in the near future through drilling operations assures an income to the owners of such shares and reasonably assures not only a big annual return on an investment in such shares but a possible return of many thousand per cent; whereas in truth and in fact the Association never has and does not now own any producing oil well or any interest therein, never was and is not now producing any oil, never has made and is not now making any earnings whatsoever and the only monies out of which the Association ever could or can now pay dividends or interest on its said shares are monies derived from the sales of such shares, never has and is not now engaged in drilling operations and has no present intention to commence such operations, and the payment of said four per centum quarterly interest is not guaranteed.

PAR. 4. That aforesaid false and misleading assertions and representations have the capacity and tendency to mislead and deceive the public into the belief that the purchase of the aforesaid shares is a safe and profitable investment, that a return of four per centum quarterly on the par value thereof is guaranteed, that the Association owns producing oil wells or interests therein from which it derives profits and earnings more than sufficient to pay, and out of which are and will be paid, the said four per centum quarterly return upon all the said shares sold or to be sold and sufficient to provide further returns on such shares, and that the Association is now drilling and intends in the near future to commence drilling oil wells in territory and under conditions which practically assure the additional production of large quantities of oil and consequently the payment of large additional profits and return to the holders of said shares.

PAR. 5. In marketing the shares of beneficial interest in the properties, assets and business of said Association, the respondents and each of them are in competition with other persons, partnerships and corporations engaged in marketing the capital stocks and shares of beneficial interest in oil companies and enterprises, including such companies and enterprises when engaged in marketing their own stocks and shares of beneficial interest.

PAR. 6. That the above alleged acts and things done by respondents, and by each of them, constitute an unfair method of competition in commerce within the intent and meaning of Section 5 of an Act of Congress entitled "An Act to create a Federal Trade Commission, to define its powers and duties and for other purposes," approved September 26, 1914.

Findings.

5 F. T. C.

REPORT, FINDINGS AS TO THE FACTS, AND ORDER.

Pursuant to the Act of Congress approved September 26, 1914, the Federal Trade Commission issued and served its complaint upon respondent, The Guaranty Fund Oil Company, an unincorporated voluntary association operating under certain articles of association and a declaration of trust, and upon E. M. Thomasson, N. V. S. Mallory, John G. Menke, individually and as trustees and officers of said The Guaranty Fund Oil Company, charging them and each of them with unfair methods of competition in commerce in violation of the provisions of said Act.

Said respondents having entered their appearance by their attorney and filed their answer herein, hearings were held before Commissioner Huston Thompson, a Commissioner of the Federal Trade Commission theretofore duly appointed, and testimony and documentary evidence were thereupon offered and received in support of the allegations of said complaint and in support of the allegations of said answer of respondents, which evidence was duly received, duly certified and duly forwarded to the Commission.

The Federal Trade Commission having duly considered the record and being now fully advised in the premises makes this its findings as to the facts and conclusion:

FINDINGS AS TO THE FACTS.

PARAGRAPH 1. The Guaranty Fund Oil Company is an unincorporated voluntary association, existing and operating under and by virtue of a certain declaration of trust wherein respondents, E. M. Thomasson, N. V. S. Mallory and John G. Menke, are named as trustees to administer the property of said association or trust. Respondent, The Guaranty Fund Oil Company, holds itself out to be a common law trust of which E. M. Thomasson is president, N. V. S. Mallory, secretary and treasurer, and John G. Menke is vice-president. Said declaration of trust was executed on or about September 1, 1921, and was recorded in Stephens County, Texas. The principal office of said trust or association is in the City of Denver, State of Colorado. Respondent, The Guaranty Fund Oil Company, holds itself out as the successor, and is in fact the successor, to the Guaranty Fund Syndicate which was organized by individual respondents herein, in March, 1921. A very limited reorganization, principally a modification of the name and a declaration of trust changed the Guaranty Fund Syndicate into the Guaranty Fund Oil Company. Both have had the same organizers and officers, and shareholders of

the former, by reason of the fact of being such shareholders, became shareholders of the latter concern. The assets and liabilities of the former were taken over by the latter concern.

PAR. 2. Ever since the organization of respondent, The Guaranty Fund Oil Company, and of its predecessor, The Guaranty Fund Syndicate, said respondents, Thomasson, Mallory and Menke, and each of them acting for themselves as beneficially interested in said respondent, The Guaranty Fund Oil Company, and its predecessor, The Guaranty Fund Syndicate, and acting for said respondent and its predecessor as trustees and officers thereof, have been and are engaged in soliciting orders for and selling shares of stock of beneficial interest in the properties, assets and business of said respondent, The Guaranty Fund Oil Company and its said predecessor. In soliciting such orders respondents have made, and at the time of the testimony above referred to, still made use of letters, circulars, maps and other matter to set forth information and representations concerning the oil leases, properties, assets and prospects of said respondent The Guaranty Fund Oil Company and its predecessor, The Guaranty Fund Syndicate, which said respondents have sent, and send from the City of Denver, State of Colorado, to purchasers and prospective purchasers, shareholders and prospective shareholders of said respondent and its said predecessor, at their several places of residence in the various states of the United States, and upon receiving orders for shares as aforesaid as a result of such solicitation, said respondents filled the same by sending certificates or other evidences of ownership for the shares so purchased, from said City of Denver to the purchasers of said shares at their several places of residence in the various states of the United States.

PAR. 3. The aforesaid letters, circulars, maps and other literature used in solicitation of purchasers and prospective purchasers of shares as above set forth, contained numerous assertions concerning the properties, assets, oil production and prospects of said respondent, The Guaranty Fund Oil Company and its predecessor, The Guaranty Fund Syndicate, which are essentially false and misleading, and which have the capacity and tendency to deceive such purchasers and prospective purchasers into the belief that said respondent company and its said predecessor were firmly established oil-producing concerns and that shares of said company and its said predecessor were a safe and profitable investment; and said false and misleading representations were made with the intent and for the purpose of aiding respondents in the sale of said shares, and had a capacity and tendency so to aid.

Findings.

5 F. T. C.

PAR. 4. In a circular letter dated September 9, 1921, addressed to stockholders of the Thomasson, Mallory Production Company, and circulated from the City of Denver, State of Colorado, among persons outside the State of Colorado in the various states of the United States, who were solicited as purchasers or prospective purchasers of the shares of beneficial interest of said respondent, The Guaranty Fund Oil Company, the following assertions were made as to properties of said respondent, The Guaranty Fund Oil Company:

* * * * *

"We have acquired a half interest for The Guaranty Fund Oil Company, in a well in the townsite of Breckenridge. I can not tell you exactly what it will produce until it is put on the pump. It did produce 175 barrels a day when it quit flowing."

"It is this production that will pay the four per cent quarterly interest on the outstanding stock of The Guaranty Fund Oil Company, and of course the receipts from the sale of the shares we are now offering, will be used to acquire more production and complete the drilling of our own well at Breckenridge. * * *"

"Let me repeat my figures:

"25 bbls. daily at \$1.25 equals \$937.50 a month; deducting \$200 a month operating expenses leaves \$737.50 or \$2,212.50 a quarter.

"Suppose we have outstanding 3,000 shares or a total of \$30,000 worth of the stock of The Guaranty Fund Oil Company; to pay four per cent quarterly interest on the \$30,000 requires \$1,200, which, out of an income of \$2,212.50 quarterly leaves \$1,012.50 per quarter for additional interest, unexpected expenses, or sinking fund to buy more production, on only 25 bbls. daily production.

"We have set aside 2,000 shares to be sold, and have 1,000 shares already sold, making a total of 3,000 shares on which we will pay four per cent quarterly, or sixteen per cent annually, and as much more as possible."

(a) By context and implication said statements quoted in this paragraph give the impression that Guaranty Fund Oil Company has acquired a half interest in a well in the townsite of Breckenridge, which is producing a net revenue to said respondent company of \$2,212.50 a quarter, and that said revenue is sufficient to pay four per cent quarterly dividends or "interest" on 3,000 shares of beneficial interest in said company, leaving a surplus of \$1,012.50 per quarter, and will be used for the purpose of paying such dividends or "interest."

(b) In truth and in fact, at the time of issuing and circulating the statements in said circular as hereinbefore in this paragraph set

forth, respondent, The Guaranty Fund Oil Company, had no oil well, nor had it an interest in any oil well from which it received production amounting to 25 barrels a day, or any other amount. It had merely a claim to one-quarter of the production from a well whose total production was from three and one-half to twelve barrels a day, and no part of said production was in fact ever actually secured by said respondent, The Guaranty Fund Oil Company. Neither at that time nor at any time prior thereto had respondent, The Guaranty Fund Oil Company, paid dividends or interest from the proceeds of oil production, upon its outstanding shares.

(c) Its statements in said circular hereinbefore in this paragraph set forth, are false and misleading and have the capacity and tendency to deceive persons solicited as purchasers or prospective purchasers of said shares, into the belief that respondent, The Guaranty Fund Oil Company, was then a firmly established concern with production sufficient to pay large net returns upon its shares, and that its shares were a safe and profitable investment. Said false and misleading representations were made with the object and for the purpose of aiding in the sale of said shares, and had the capacity and tendency so to aid.

PAR. 5. In a circular issued and circulated by respondents to persons solicited as purchasers or prospective purchasers of shares, from the City of Denver, State of Colorado, in and to the various states of the United States no later than October, 1921, these statements were incorporated.

"Our producing well, in which we own a half operating interest should give us sufficient income to pay 4% quarterly interest on our outstanding shares and what we are offering for sale. Proceeds from the sale of shares now offered will purchase more production and drill our own well. We are playing the game in a safe way by building up our own production returns while we drill our own well. Speculation with a good oil company drilling in the midst of big producing wells and the shares earning at least 4% quarterly on the par value thereof, or equal to 26½% annually on your actual investment, is an ideal way to put your money to work. We offer you all the possibilities of speculation with an assured income while you are waiting for the results of our drilling."

* * * * *

"We have production now from which to pay 4% quarterly interest on the par value of our shares."

(a) In truth and in fact, at the time that said circulars were issued and circulated, incorporating said statements as hereinbefore

Findings.

5 F. T. C.

set forth in this paragraph, the portion of production of the well which must have been referred to—the Bateman well—claimed by respondents, would not have been sufficient, if secured, to pay 4% quarterly dividends or “interest” on outstanding shares of respondent, the Guaranty Fund Oil Company, and as a matter of fact no production whatever from said well or any other well had been, up to that time, secured by respondent.

(b) The representations made by said respondents as hereinbefore set forth in this paragraph, were false and misleading and had the tendency and capacity to mislead and to deceive persons solicited as purchasers or prospective purchasers of the shares of the respondent, The Guaranty Fund Oil Company, into the belief that said respondent, The Guaranty Fund Oil Company, was a firmly established concern, and had sufficient production to pay a large net return upon the outstanding shares of said company. Said false and misleading representations were for the purpose and with the object of aiding in the sale of said shares.

PAR. 6. In a circular issued by said respondents, and circulated to persons solicited as purchasers or prospective purchasers of shares of beneficial interest, said Guaranty Fund Syndicate, predecessor to respondent, The Guaranty Fund Oil Company, on or about April 15, 1921, soliciting investment in said shares, the following representations are incorporated in a statement under this headline:

“What you will get by investing \$100 in the Guaranty Fund Syndicate. * * *

“(5) Oil production trust note guaranteeing 4% quarterly, or 16% annual dividends on the full par value of your certificate of ownership in the Guaranty Fund Syndicate, and secured by trust mortgage on oil production income. We issue these notes for one year periods.”

* * * * *

“FACTS IN BRIEF.”

“You are * * * guaranteed at least 16% yearly dividend on the full par value of your certificate of ownership in the Guaranty Fund Syndicate for at least two years, payable quarterly, and secured by trust mortgage on oil production income”, * * *

“In addition to the 16% yearly dividend guaranteed, your share of the enormous profits from our syndicate’s oil wells in the Breckenridge district.”

* * * * *

(a) In truth and in fact at the time the representations were made as hereinbefore set forth in this paragraph, the Guaranty Fund

Syndicate, predecessor to respondent company, had no oil production income to mortgage for any purpose whatever, nor had it profits enormous or otherwise from "our syndicate's oil wells in the famous Breckenridge district."

(b) Said representations by respondents as herein above set forth in this paragraph were, and are, false and misleading and have had, and have a capacity and tendency to mislead and to deceive persons solicited as purchasers or prospective purchasers of said shares, into the belief that said Guaranty Fund Syndicate, predecessor to respondent, Guaranty Fund Oil Company, was a firmly established concern with large profits from oil production, and capable of paying high net returns upon its shares.

(c) Such false and misleading representations had the object and purpose, as well as the capacity and tendency to aid respondents in the sale of said shares.

PAR. 7. In a circular issued by respondents and circulated by them from the City of Denver, State of Colorado, among persons solicited as purchasers or prospective purchasers of the shares of said Guaranty Fund Syndicate, predecessor to the Guaranty Fund Oil Company, in the various states of the United States, under date of April 14, 1921, the following representations were incorporated among others:

"You will note from the enclosed printed matter that we have added another feature to the Guaranty Fund Syndicate—that of guaranteeing 4% quarterly or 16% annually for a period of not less than two years. These dividends will be paid from oil production set aside for that particular purpose."

* * * * *

(a) In truth and in fact, at the time that the representations in said circular as herein above set forth in this paragraph were made and circulated, The Guaranty Fund Syndicate, predecessor of The Guaranty Fund Oil Company, had received no oil production, and respondents had not, up to that time, nor did they afterward, pay such dividends or "interest" upon said shares, from the proceeds of oil production.

(b) Said representations by respondent in said circular as herein above set forth in this paragraph, are false and misleading and have the capacity and tendency to mislead and to deceive persons solicited as purchasers or prospective purchasers of said shares, into the belief that said Guaranty Fund Syndicate, predecessor to The Guaranty Fund Oil Company, was a firmly established concern capable of paying from oil production, high net returns upon its shares.

Conclusion.

5 F. T. C.

(c) Such false and misleading representations had the object and purpose as well as the capacity and tendency to aid respondents in the sale of oil shares.

PAR. 8. Individual respondents, Thomasson, Mallory and Menke, did actually pay at times at the rate of 4% quarterly or 16% annually upon outstanding shares of beneficial interest in respondent, The Guaranty Fund Oil Company and its predecessor, The Guaranty Fund Syndicate, but no part of said payment was made from oil production or other earnings of said concerns prior to October, 1921. Said payments had the effect of aiding in making plausible and worthy of belief by purchasers and prospective purchasers of oil shares, the false and misleading statements incorporated in circulars in paragraphs 3 to 7 inclusive herein, to the effect that production was sufficient to make such payments.

PAR. 9. Through such circulars and by other means, respondents sold, prior to July 1, 1922, to persons residing in various states of the United States, and in Canada, 8,395 shares of respondent's, The Guaranty Fund Oil Company's shares of a par value of \$83,950, for which they received \$60,230.67, and said respondents delivered to said purchasers, through the mails or by other means in interstate commerce evidences of ownership of said shares to purchasers in various states outside the State of Colorado. Such sales and such deliveries were made in the States of California, Illinois, Ohio, Oregon, Washington, Connecticut, Pennsylvania, Massachusetts, Missouri and other states and in the Dominion of Canada.

PAR. 10. In marketing said shares of beneficial interest in the properties, assets and business of said respondent, The Guaranty Fund Oil Company and its predecessor, The Guaranty Fund Syndicate, the individual respondents, and each of them, have been in active competition with other persons, partnerships and corporations engaged in selling the capital stock and shares of beneficial interest in other oil companies and enterprises.

CONCLUSION.

The acts, practices and activities of respondents and each of them, under the conditions and in the circumstances set forth in the foregoing findings as to the facts, are unfair methods of competition in commerce, and constitute a violation of Section 5 of the Act of Congress approved September 26, 1914, entitled: "An Act To create a Federal Trade Commission, to define its powers and duties, and for other purposes."

ORDER TO CEASE AND DESIST.

This proceeding having been heard by the Federal Trade Commission upon the complaint of the Commission, the answer of respondent, the testimony and documentary evidence offered and received, and the arguments of counsel for the respective parties hereto, and the Commission having made its findings as to the facts and its conclusion that the respondent, The Guaranty Fund Oil Company, has violated the provisions of the Act of Congress approved September 26, 1914, entitled "An Act to create a Federal Trade Commission, to define its powers and duties, and for other purposes."

It is now ordered, That respondents, The Guaranty Fund Oil Company and E. M. Thomasson, N. V. S. Mallory and John C. Menke, individually and as trustees and officers of The Guaranty Fund Oil Company, an unincorporated, voluntary association operating under a declaration of trust, and the officers, directors, agents, servants and employees of respondent, The Guaranty Fund Oil Company, do cease and desist from representing to persons solicited as purchasers or prospective purchasers of shares of beneficial interest in The Guaranty Fund Oil Company, by means of circulars or otherwise, in substance that said company has production from oil wells or has other earnings sufficient to pay large net returns upon outstanding shares, when in truth and in fact it did not have such production nor earnings; or

From representing to persons solicited as purchasers or prospective purchasers of shares of beneficial interest in respondent, The Guaranty Fund Oil Company, by circulars or otherwise, that said company has enormous profits from oil production, or other sources, when it has no such profits, or that it has profits other or greater than are actually enjoyed, and

From guaranteeing dividends, interest or other returns to shareholders when said respondent has not the funds out of which such dividends, interest or other returns are to be paid.

It is further ordered, That respondent, within sixty days from and after the date of the service upon it of this order, file with the Commission a reply setting forth in detail the manner and form in which it has complied with the order to cease and desist hereinbefore set forth, to which report shall be attached copies of all circulars, circular letters or like literature issued by respondents in the making of sales or the soliciting of purchasers or prospective purchasers of the shares of respondent, The Guaranty Fund Oil Company.

372

FEDERAL TRADE COMMISSION DECISIONS

Complaint.

5 F. T. C.