



State of Utah  
DEPARTMENT OF COMMERCE  
Division of Securities

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May 20, 1992

Gerald A. Bollinger  
Kunzman & Bollinger, Inc.  
1601 Northwest Expressway, Suite 430  
Oklahoma City, Oklahoma 73118

Re: EBCO U.S.A. Inc.

File # 002-4042-21/A13099-21

Dear Mr. Bollinger:

This letter is in response to your letters dated April 3, 1992 and April 8, 1992, regarding your request for a no-action letter for the offer and sale of oil and gas properties by EBCO U.S.A. Inc. to individuals or companies. Such transaction is more fully described in your letters.

You asked the Division of Securities ("Division") to address the following question:

Whether the sale of oil and gas properties, as described in your letters, to individuals or companies in the oil industry constitutes the sale of a security as defined by Section 61-1-13(22)(k) or Section 61-13(22)(o) of the Utah Uniform Securities Act ("Act")

Section 61-1-13(22)(k), defines a security as, among other things, an investment contract. Section 61-13(22)(o) defines a security as a certificate of interest or participation in an oil, gas, or mining title or lease or in payments out of production under such a title or lease.

It is the opinion of the Division that such transaction, as described in your letters do not constitute a security as defined in Section 61-13(22)(k) or Section 61-13(22)(o) of the Act.

In arriving at this position the Division notes, in particular, the following representations:

- (a) EBCO conducts auctions of various interests in oil and gas properties which are owned by numerous different and unrelated sellers.

- (b) The oil and gas properties to be auctioned may include any or all of the following: working interests, overriding royalty interests, royalty interests, operations, reversionary interests, oil and/or gas properties, producing properties, non-producing properties, properties with additional developments potential, properties without additional development potential, shut-in properties, undeveloped properties and other interests.
- (c) These properties are offered without warranty as to production, title or condition, on an "as is" basis.
- (d) These properties are sold subject to any existing operating agreement, production purchases agreement, farmout agreement or other contract and existing encumbrances and title defects, if any.
- (e) The seller or EBCO will record or deliver to the purchaser the conveyancing documents notice in favor of the purchaser.
- (f) EBCO receives a commission based on the sales price of the properties sold.
- (g) Information relating to the property is provided to the prospective purchaser. However, EBCO does not independently verify such information.
- (h) All information provided to interested parties includes the name and telephone number of additional sources of information concerning the properties which are available. These additional sources of information include state agencies with jurisdiction over oil and gas properties and private companies which can provide information with respect to liens, drilling records, plugging reports, production reports, decline curves, etc.
- (i) A seller is required to offer its entire ownership of the type of interest in the property that is being offered for sale. The seller may retain a royalty, overriding royalty, horizontal severance of the subject property where the seller retains all of its existing rights in certain formations or depths under the whole property, or adjacent acreage.
- (j) There must be only one purchaser of the property.
- (k) Before a buyer is allowed to purchase a property, the buyer must satisfy EBCO that it is engaged in the business of oil and gas exploration and production as an ongoing business.

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Based upon the facts presented, the Division will not recommend any enforcement action if the sell of the oil and gas properties are effected as described in your letter.

Because this position is based upon the representations made to the Division of Securities it should be noted that any different facts or conditions of a material nature might require a different conclusion. Further, this response does not purport to express any legal conclusion on the questions presented.

Please note that this no-action letter relates only to the referenced transaction and shall have no value for future similar offerings.

Very truly yours,

EARL S. MAESER, DIRECTOR  
UTAH DIVISION OF SECURITIES



Steven J. Nielsen  
Director of Registration

jmj

KUNZMAN & BOLLINGER, INC.  
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April 3, 1992

FEDERAL EXPRESS

Mr. Steven J. Nielsen,  
Director Registration  
Department of Commerce,  
Division of Securities  
160 East 300 South  
Salt Lake City, Utah 84145-0802

RE: Interpretive Opinion Request  
Sections 61-1-13(18)(k) and (o)  
Utah Uniform Securities Act  
Our File No. 85100 - 430.44

Dear Mr. Nielsen:

This firm represents EBCO U.S.A., Incorporated ("EBCO"), an Oklahoma corporation based in Oklahoma City. EBCO's predecessor company was established in 1979. EBCO currently employs approximately 23 people and has a net worth in excess of \$500,000.

In order to provide an alternative to the traditionally inefficient buying and selling process in the oil and gas industry, EBCO assists members of the oil and gas industry in buying and selling oil and gas properties. EBCO is generally regarded as the leading company in its field, with sales in excess of \$20,000,000 during the last fiscal year. Its clients have included: Fina, Texaco, Arco, Amoco, Oryx, Sampson Resources and Dyco Petroleum. The volume of business conducted by EBCO demonstrates that its services are valuable to the oil and gas industry.

The following conditions generally apply to all sales:

- (1) Typically, EBCO conducts an auction once a month of hundreds of various interests in oil and gas properties situated throughout the United States which are owned by numerous different and unrelated sellers. The gross proceeds of an auction may be as large as several million dollars, paid by hundreds of

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purchasers. The sales price of an individual property or lot may range from almost nothing (there is no required minimum bid) to \$50,000 or more. The auctions may be conducted anywhere in the United States, but historically the auctions have been limited to Houston, Dallas, Oklahoma City and Denver.

In addition to auctions, sometimes sealed bids are requested by EBCO for a property, which eliminates the necessity for prospective purchasers to personally attend an auction. A sealed bid is a bid on a bid form provided by EBCO which can be submitted in person, by mail or by delivery, and must contain a bank letter guaranteeing funds equal to the amount of the bid tendered.

- (2) The oil and gas properties to be auctioned:
  - (i) may include any or all of the following: working interests, overriding royalty interests, royalty interests, operations, reversionary interests, oil and/or gas properties, producing properties, nonproducing properties, properties with additional development potential, properties without additional development potential, shut-in properties, undeveloped properties and other interests;
  - (ii) are not subject to any geographical restrictions and may be any size of interest;
  - (iii) are offered without warranty as to production, title or condition, on an "as is" basis; and
  - (iv) are sold subject to any existing operating agreement, production purchase agreement, farmout agreement or other contract and existing encumbrances and title defects, if any.
- (3) The seller or EBCO will record or deliver to the purchaser the conveyancing documents or

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notices in favor of the purchaser. The purchaser is charged a nonrefundable recording fee by EBCO for each assignment to be recorded.

- (4) All payments for properties are currently made to EBCO or an unrelated bank as escrow agent.
- (5) EBCO receives a commission based on the sales price of the properties sold.
- (6) The following information generally is provided (subject to the purchaser's verification through its own due diligence) by the seller with respect to each property:
  - (i) location;
  - (ii) well name;
  - (iii) size and type of interest offered;
  - (iv) oil production per day;
  - (v) gas production per day;
  - (vi) name of the operator; and
  - (vii) name of the seller.

Certain additional information provided by the seller concerning cash flow and production history generally is available to prospective purchasers at EBCO's offices with respect to most of the properties and will be mailed to prospective purchasers upon request for a nominal fee and postage, however, EBCO will not have independently verified such information.

In addition to the foregoing, in every direct mail brochure sent to prospective purchasers, EBCO sets forth the name and telephone number of additional sources of information concerning the properties which are available. These additional sources of information include state agencies with jurisdiction over oil and

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gas properties and private companies which can provide information with respect to liens, drilling records, plugging reports, production reports, decline curves, etc.

- (7) Notice and promotion of each auction generally will be by means of the following:
  - (i) direct mail brochures to qualified persons on EBCO's mailing list (approximately 16,000), and
  - (ii) publication of notices in various trade journals, such as Oil and Gas Investor, Oil and Gas Journal and American Oil & Gas Reporter. There is no advertising to the public in general circulation newspapers or other publications which are not oil and gas trade journals whose subscribers generally are members of the oil and gas industry.
- (8) Expenses of notice and promotion of an auction, which includes a catalog of the properties, room rental and refreshments, are paid by the sellers and are approximately \$35,000 to \$50,000 per auction, or more.
- (9) A seller is required to offer its entire ownership of the type of interest in the property that is being offered for sale, but may retain a royalty, overriding royalty, horizontal severance of the subject property where the seller retains all of its existing rights in certain formations or depths under the whole property, or adjacent acreage, and there must be only one purchaser. Future development of the properties is not emphasized to prospective buyers, however, potential undrilled locations, zones located behind pipe and other similar information may be pointed out.
- (10) Before a buyer is allowed to purchase a property, the buyer must satisfy EBCO that it is engaged in the business of oil and gas exploration and production as an ongoing business. EBCO generally will conclude that a person or entity that meets at least one of the tests set forth below is in the oil and gas business.

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- (i) any individual or business entity that is, and has been for at least 5 years, actively engaged in and derives at least fifty-one percent of its annual gross income from the exploration or production of oil or gas;
- (ii) any individual or business entity that derives at least seventy-five percent of its gross annual income from the exploration or production of oil or gas;
- (iii) any individual or business entity that is directly engaged in the business of exploration and production of oil or gas and derives at least \$500,000 of annual gross revenues from such business; or
- (iv) any individual or business entity which currently operates 25 or more oil or gas wells.

In addition, EBCO may conclude under the particular facts and circumstances of the case that a prospective buyer is in the oil and gas business even though he fails to satisfy any of the tests set forth above.

- (11) EBCO has formed a wholly-owned subsidiary corporation, EBCO Resources, Inc., which is a member of the National Association of Securities Dealers, Inc. ("NASD"), but is not a registered broker-dealer in Utah. In certain cases, EBCO Resources, Inc. will conduct the auction of the oil and gas properties instead of EBCO.

Attached as exhibits to this letter are two copies of each of the following:

Exhibits

- A - Sample Agreement between EBCO and a seller;
- B - Sample Investment Profile, Bidder Identification Form and Acknowledgment, and Buyer's Terms and Conditions of Sale;

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- C - Sample Direct Mail Brochures;
- D - Sample Guide for Preparing Oil and Gas Properties for Sale provided to sellers;
- E - Sample sale catalog of properties; and
- F - Sample trade journal notices.

In our opinion, the offer and sale of oil and gas properties by EBCO as discussed above does not involve the offer or sale of a security within the meaning of Sections 61-1-13(18)(k) and (o) of the Utah Uniform Securities Act (the "Act"). Section 61-1-13(18)(k) defines the term "security" to include an investment contract. The test of an investment contract is whether the transaction involves an investment of money in a common enterprise with profits to come solely from the efforts of others. SEC v. W.J. Howey, 328 U.S. 293 (1946). The transactions discussed above should not be deemed to be investment contracts for the following reasons: (i) there is no common enterprise because there is only one purchaser of each property; (ii) there is no reliance on the efforts of others because the purchaser is in the oil and gas business and has full access to information concerning the property from the seller and therefore is able to fend for himself; and (iii) there is no emphasis on the efforts of others that will make the properties more valuable. See Ballard & Cordell Corp. v. Zoller & Danneberg, 544 F.2d 1059 (10th Cir. 1976).

In Woodward v. Wright, 266 F.2d 108 (10th Cir. 1959), the seller retained an interest in the lease and became the operator after the purchasers acquired their interests in the lease. However, the purchasers owned the controlling interest in the property and controlled its operation even to the point of terminating the seller as operator when they became dissatisfied with his efforts. The court stated this was not an investment contract.

In SEC v. C.M. Joiner Leasing Corp., 320 U.S. 344 (1943), the Supreme Court held that the sale of oil and gas leases accompanied by the representation that the seller would drill a well in the general area which would enhance the value of the leases involved the sale of an investment contract. The court stated that the drilling of the well was not an unconnected or uncontrolled phenomenon merely pointed out by the seller, instead it permeated the whole transaction. However, if the sellers had omitted the economic inducements of the promised exploration

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well, the court stated it would have been a quite different proposition. In that case the purchasers would have been left to their own efforts in order to profit from the leases.

In Deutsch Energy Co. v. Mazur, 813 F.2d 1567 (9th Cir. 1987), the purchasers contracted to buy producing wells and undeveloped drill sites from the sellers, and the parties agreed to enter into an operating agreement designating a third party as operator, under which the purchasers would retain significant managerial powers, including the power to veto any decision by the sellers to replace the operator or to abandon wells as dry holes. The court found there was no investment contract.

Also, the sales by EBCO discussed above do not involve a pooling of funds for the joint benefit of the owners of the property. Nor is the development of the property dependent on the success of the sale. Additional favorable factors for avoiding investment contract classification include: (i) full information or access to information concerning the property is provided to the purchaser; (ii) the purchaser is sophisticated, experienced and knowledgeable concerning the oil and gas industry; and (iii) the purchaser is free to actually participate in the development and operation of the property consistent with the nature of the interest in the property that is purchased.

Section 61-1-13(18)(o) defines the term "security" to include a "certificate of interest of participation in an oil, gas or mining title or lease or in payments out of production under such a title or lease." In construing fractionalized interests under the Securities Act of 1933, it has been held that only that interest which is created by subdivision of a portion of the owner's interest for the purpose of a public offering for sale is a security. Lynn v. Caraway, 252 F.Supp. 858 (W.D. La. 1966). Also, if the seller transfers the whole of what he owns, there can be no creation of a fractional undivided interest in oil and gas, even though what he sold was a fractional interest. Woodward v. Wright, 266 F.2d 108 (10th Cir. 1959). However, in Graham v. Clark, 332 F.2d 155 (6th Cir. 1964), the court held that the transfer of all of the seller's interest in an oil and gas lease and the producing wells situated thereon was not a security, notwithstanding the reservation of an oil payment to be paid out of the working interest that was sold. In addition, in Fearneyhough v. McElvain, 598 F.Supp. 905 (C.D. Ill. 1984), a landowner's lease of all of its oil and gas rights was held not to be a security, notwithstanding the reservation of a standard 1/8 landowner royalty interest. Therefore, although certain interests may be retained by the sellers, as noted in paragraph (9), page 4, the oil and gas properties offered for

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sale by EBCO should not be deemed to be fractionalized interests which would be securities within the meaning of Section 61-1-13(18)(o) of the Act.

It is respectfully requested that the Division concur in our opinion and issue an interpretive opinion that the offer and sale of oil and gas properties by EBCO as discussed above does not involve the offer or sale of a security within the meaning of Sections 61-1-13(18)(k) and (o) of the Act.

Pursuant to R177-25-5, please be advised as follows:

- (1) there is no legal action, judicial or administrative, which relates, directly or indirectly, to the facts set forth above; and
- (2) sales as described above have been commenced in reliance on the exemption from Sections 61-1-7 and 61-1-15 of the Act provided by Section 61-1-14(2)(a) of the Act and the exclusion from broker-dealer registration provided by Section 61-1-13(3)(d)(ii) of the Act, if such sales are deemed to involve the sale of a security under the Act.

Pursuant to R177-18-4, a check in the amount of \$120 is enclosed. If any further information is desired in connection with this matter, please communicate with the undersigned.

Very truly yours,

KUNZMAN & BOLLINGER, INC.

*Gerald A. Bollinger*  
Gerald A. Bollinger

GAB:pb  
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Enclosures