

TURNING



BUD JACOBSON,
EARL HASTINGS
AND ARIZONA'S
1951
SECURITIES ACT

BY RICHARD G. HIMELRICK

This year, 2011, marks the 60th anniversary of Arizona's modern securities laws—the 1951 Securities Act.¹ That law was slow in coming and followed a colorful history.

The securities laws that preceded the 1951 Act were enacted between 1909 and 1921.² The centerpiece of these was the 1912 Investment Company Act,³ which was copied almost verbatim from the 1911 blue-sky statute in Kansas.⁴ The 1912 Act was enacted after Governor George W.P. Hunt urged the Arizona Legislature to enact securities laws to stop wildcat promoters and others from selling worthless stock. After the Act passed unanimously, Hunt publicized it as one of his administration's main accomplishments. Yet despite Hunt's enthusiasm, the 1912 Act was crude legislation by today's standards.⁵

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Prosecutors found the Act's criminal provisions too weak to use. It did not provide civil remedies. And the red tape and expense created by its registration provisions discouraged legitimate companies from attempting registration.

Despite these shortcomings, legislative change was slow to come. It was not until 1948 that two events precipitated interest in new securities laws.

The Postwar Boom

The first event leading to a movement toward a new law was the interest in business and economic legislation that followed the explosion of Arizona's economy after World War II.⁶ With the stimulus of the government's unprecedented defense and research

spending, Arizona's population increased by 50 percent between 1940 and 1950, and companies like Motorola, AiResearch, Alcoa and Goodyear Aircraft moved into the state.⁷ Manufacturing and

service industries developed that did not exist before the war, and business, legal and government leaders who were committed to building the state emerged.⁸ These business-minded leaders formed committees to plan for postwar growth and recommend legislative changes. Among these were special legislative committees to study state operations and Arizona's securities laws.

The Riccardi Stock Swindle

The second catalyst for new securities legislation was a series of stock swindles in the late 1940s that the Corporation Commission was incapable of controlling. One of these schemes, involving a disbarred attorney and career criminal named Constantino Riccardi,⁹ accelerated interest in new securities laws.

During 1948, a group of Arizona investors whom Riccardi had defrauded in a mining swindle pressured the Corporation Commission to investigate.¹⁰ By then, Riccardi had at least a dozen arrests and had served prison time in California and New York.¹¹ When the Commission's investigation began, Riccardi was in New Jersey under arrest on new fraud charges involving a divorced princess who, before that, was the wife of the Kresge chain-store owner.¹² Riccardi had proposed to the princess despite being married.¹³

The Commission's investigation was front-page news.¹⁴ It focused attention on the weaknesses in Arizona's securities laws and revealed that the Commission lacked the personnel to screen securities dealers and stock offerings like Riccardi's scam.

Riccardi's scheme and a 1949 stock fraud involving a company named Road-O-Scope attracted the attention of the Arizona Attorney General's office. At the time, Edward "Bud" Jacobson and Joseph P. Ralston worked together in the AG's office. Both were recent graduates of the University of Arizona College of Law. In 1949 they occupied adjoining offices in the State Capitol, where their work as assistant attorneys general included securities matters. Jacobson would later become a longtime Snell & Wilmer partner; Ralston later would join with Francis Ryley and Read Carlock to found Ryley, Carlock & Ralston. A 1949 Securities & Exchange Commission (SEC) memo described Edwards and Ralston as young "fire balls" who



A smiling Edward "Bud" Jacobson through the years.

were exasperated with Arizona's securities laws.

The Road-O-Scope investigation was ongoing, and the company claimed to have developed a mirror device that helped drivers see vehicles approaching at intersections. The device did not work and was incapable of producing sales. Ralston called Road-O-Scope a "gold brick scam from start to finish" that was "just as bad and maybe worse" than the Riccardi fraud on which he had worked the year before.¹⁵ But despite flagrant fraud, Ralston and Jacobson concluded that Arizona's securities laws were so weak that it was impossible to prosecute the promoters for more than a misdemeanor.

The Special Securities Committee

As a first step toward new laws, Jacobson, working with the Corporation Commission, invited business leaders to participate in a conference to study solutions. Invitations were sent to commercial bankers, securities brokers, the Arizona Chamber of Commerce and the Better Business Bureau.¹⁶ This led to the formation in January 1949 of a Special Securities Committee to draft new legislation for a Securities Division within the Corporation Commission.¹⁷ In addition to Jacobson and Phoenix attorney Joe Walton, the Committee included two securities professionals from leading Phoenix brokerage firms and five businessmen whose experience spanned the mining, oil, real estate and banking industries.

Lorna Lockwood assisted the Committee in drafting the Securities Division legislation.¹⁸ Like Jacobson and Ralston, Lockwood was a University of Arizona College of Law graduate, and she was the first woman appointed in Arizona as an assistant attorney general. In 1949, Lockwood, Jacobson and Ralston all were

working as assistant attorneys general. Lockwood left in 1951 to become a Superior Court judge and in 1961 was elected to the Arizona Supreme Court.

The 1949 legislation set statutory qualifications for an experienced securities director with supporting staff to enforce the state's securities laws. Before that, securities enforcement had been handled by an Investment and Securities Department whose only staff was a part-time stenographer.¹⁹



Expectations for the new Securities Division were high. As one newspaper put it, the Commission's Securities Division "would attempt to put the Iron Glove on such stock swindle schemes as the Riccardi

Affair."²⁰ To do the work, the legislation budgeted for a director and assistant director of securities as well as supporting staff.²¹

After the legislation passed in early 1949, the Commission appointed Earl Hastings, all of age 41, its first Director of Securities. Hastings, whom Jacobson supported for the position, had studied business and engineering in college. Afterward, he worked in managerial and consulting positions for a variety of companies, many in the mining industry, where he became certified as a mining and metallurgical engineer. His business background and familiarity with Arizona's mining industry, in which frauds like Riccardi's scheme were frequent, made him a sound choice.

Once appointed, Hastings, with Jacobson's assistance, quickly expanded the Securities Committee's work into preparing an entirely new securities act. Hastings wanted to start with a draft bill to show the Committee what he and Jacobson had in mind. His first step was to contact the SEC to get the federal agency's views on how best to draft a new act. He told the SEC that Arizona's existing laws "were inadequate in every way." What was needed, he said, was a "stiff law" to protect the public and help legitimate promoters.

Correspondence between the SEC and Hastings shows that the SEC had not developed a position on how state securities legislation should be written. But the SEC was willing to provide comments. By the end of 1949, a preliminary draft of the bill had been written and commented on by the SEC. After that, Hastings presented the bill for study and comment by the Securities Committee and other interested parties.

By soliciting differing views in this way, Hastings garnered wide support for the new act. In addition to the business and securities-industry representatives on the Securities Committee, the bill's supporters included the State Bar of Arizona, the Arizona Bankers Association, the Arizona Small Mine Operators Association, the state's new Legislative Committee on State Operations, and the national arm of the Investment Bankers Association (IBA).

The IBA's Influence

The preliminary draft that Hastings presented to the Securities Committee largely tracked model legislation prepared by the IBA the year before. The IBA, whose members in 1949 included most of the

country's principal underwriting firms, advocated simplified state securities laws written to deter fraud and streamline registration. It opposed Kansas-style registration laws like those in Arizona's 1912 Securities Act. It considered laws of that type poorly drafted and unworkable.²² As an alternative, the IBA drafted its own model securities laws.

These IBA-drafted laws were the only model securities legislation that existed when Hastings and Jacobson decided to prepare a new securities act. A uniform state act did not exist; the last uniform state securities law had been withdrawn in 1944 as obsolete,²³ and a replacement act was not finished until 1956.²⁴ In the interim, the IBA promoted its model legislation,²⁵ which Arizona and four other states used as templates for new securities acts.²⁶

But Hastings did not blindly accept the IBA's views. As he told the SEC, he wanted a "stiff law" that gave him discretion to regulate securities offerings. To that end, section 8 of the preliminary draft allowed the Corporation Commission to evaluate the merits of proposed offerings and deny registration if an offering was "unfair or inequitable." This type of merit review was opposed by the IBA, but it was retained in the Securities Committee's final draft and became a defining feature of the 1951 Act's regulatory provisions.²⁷

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ELIAS ROMLEY TO HEAD NEWLY ESTABLISHED ARIZONA BAR FOUNDATION

The new member board of directors of the Arizona Bar Foundation recently elected Elias M. Romley as the first President of the Foundation. Other officers and members of the Board include: Not pictured is Howard H. Korman.

Elias M. Romley
Jerry L. Angle-Treasurer
John P. Frank
Edward (Bud) Jacobson
Philip H. von Arnim-Vice-President
Aaron Kinsey
Joseph P. Buleton
Melvin Liba



Revisions to the Preliminary Draft

Many other departures from the IBA's model legislation were made during the study-and-comment process that Hastings used to produce a final bill.²⁸ Reports on the bill's drafting were sent to the Corporation Commission during what Hastings summarized as "days of discussion, unlimited contribution of time by the Special Securities Advisory Committee and legal counsel of firms and individuals interested in the effects of such legislation."²⁹ The resulting new ideas and improved drafting can be fully appreciated only by carefully comparing the preliminary draft with the final bill.³⁰ But the quality of the drafting is suggested by a comment from Harvard's Louis Loss, the draftsman of the 1956 Uniform Securities Act. Loss described the securities-registration provisions of the 1951 Arizona and 1953 Illinois acts as "perhaps the best drafted" of the pre-1956 securities acts.³¹

Federal-state coordination provisions in the 1951 Act illustrate Loss's comment. Under Hastings's direction, the Act included provisions that provided for cooperation with the SEC, allowed issuers to use SEC prospectus materials in parts of Arizona registrations, and created a registration exemption for securities listed on exchanges regulated by the SEC. In 1951, SEC-coordinated legislation like this was only beginning to appear in state securities laws.



Joseph P. Ralston.
Below: His UA Law graduating class.

Another noteworthy innovation for the time was prompted by the SEC's comments. The preliminary draft of Hastings's bill, like other state securities laws, provided civil remedies only for securities purchasers. The SEC recommended that the proposed act's civil-liability provisions protect both securities sellers and purchasers. In this way, the SEC noted, the civil-liability provisions would track the act's antifraud statute, which made it a crime to defraud either a seller or a purchaser. The drafters accepted these recommendations and revised the civil-remedies section to provide remedies for sellers and purchasers. As a result, Arizona became the first state to provide

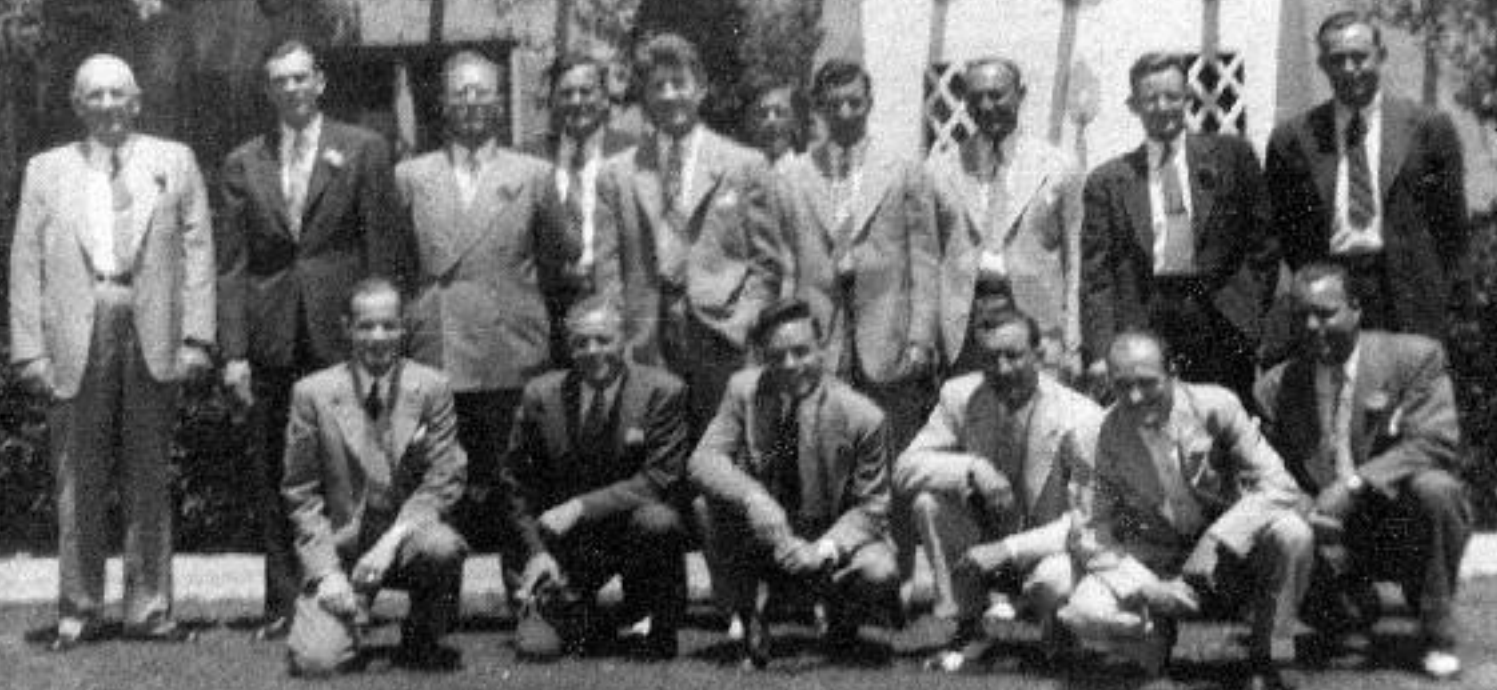
damage and rescission remedies for securities sellers³²—remedies that were omitted even from the 1956 Uniform Securities Act that Professor Loss drafted.

Passage of the Act

In a March 1950 letter, Hastings urged the governor to introduce the proposed legislation in a special session. He was unsuccessful that year but was able to introduce the bill in 1951. The bill passed with only one "No" vote and was approved by the governor on March 6, 1951.

Hastings summarized the Act's effect in reports filed after its passage. He described the Act as well received by business, securities dealers and public investors.³³ He reported that because of

GRADUATING CLASS OF 1947
Senior breakfast at Arizona Inn.
Back Row: 1. President Atkinson, 2. Shiak 3. Shortridge 4. [unclear] (7)
5. John Whitney 6. W.A. Seanland 7.
8. Robert Murrison 9. Jon B. Wilke
Front Row: 1. Samuel Guddard 2. Robert Fleming
3. Joe Ralston 4. Tom Schmae 5. Ken. Biattis
6. Joe Walton



Former Arizona Chief Justice
Lorna Lockwood.

Photo from the Herb and
Dorothy McLaughlin Collection,
Arizona State University Libraries.



improved registration laws, out-of-state securities offerings that were previously unavailable were rapidly becoming available to local investors.³⁴

Within a year, the dollar volume of newly registered securities nearly doubled³⁵—a trend that accelerated in later years.³⁶ By 1954, he reported that new issues by local companies that were funded by Arizona investors were becoming relatively common.³⁷ Simultaneously, trading in public securities increased at a greater rate than could be explained by population increases.³⁸

In short, with benefit of the continuing postwar economic boom, the 1951 Act opened Arizona's securities markets to increased capital formation and trading in securities.

The Act also expanded criminal and civil remedies. Felony prosecutions for securities violations that Jacobson and Ralston would have been unable to bring became possible under the Act's new criminal statutes.³⁹ The Securities Division used the Act's reg-

With benefit of the continuing postwar economic boom, the 1951 Act opened Arizona's securities markets to increased capital formation and trading in securities.

ulatory provisions to bring administrative actions in which the Corporation Commission's hearing officers interpreted the Act as remedial legislation that was broader than federal securities law.⁴⁰ In civil actions, the courts read the Act to relax common-law fraud rules⁴¹ and concluded, like the Commission, that the Act was more protective of investors than was federal law.⁴²

Today, 60 years later, the 1951 Act's provisions have been improved by many amendments.⁴³ But the original Act's core provisions continue to anchor it. Last year's decision in *Grand v. Nacchio*⁴⁴ is an example. *Grand* was the Arizona Supreme Court's first decision on civil liability in 30 years. In a testament to the 1951 Act's longevity, the Court began its statutory analysis by quoting the 1951 intent provision, which describes the Act as a "remedial measure" that is to be "liberally construed" for the "protection of the public."⁴⁵ These were Hastings and Jacobson's views when the Act was drafted, and they continue to inform the

Act's interpretation in modern securities litigation.

Epilogue

In 1956, after serving seven years as Director of the Securities Division, Hastings was appointed an SEC commissioner. He continued with the SEC until 1961, when he fell ill and suffered an early death at 53. Jacobson became a noted arts' patron and partner at Snell & Wilmer, where he practiced law



Joseph Ralston (bottom, second from left) with Phi Delta Phi fraternity, 1941-42.

endnotes

1. Securities Act of Arizona, ch. 18, 1951 Ariz. Sess. Laws 46.
2. The first of these laws was a 1909 territorial law that outlawed bucket shops in which people could bet on the rise and fall of stock and commodity prices. See *Bucket Shops in Arizona*, ARIZ. DEMOCRAT, Feb. 2, 1909, at 3.
3. Act of May 18, 1912, ch. 69, 1912 Ariz. Sess. Laws 338. The 1912 Act was supplemented by legislation in 1917 and 1921 that regulated securities brokers and dealers.
4. See Jonathan R. Macey & Geoffrey P. Miller, *Origin of the Blue Sky Laws*, 70 TEX. L. REV. 347, 361-62, 377 (1991) (describing the Kansas act and noting that Arizona's 1912 act was patterned on the Kansas model).
5. See 1 LOUIS LOSS, JOEL SELIGMAN & TROY PAREDES, SECURITIES REGULATION 54 (4th rev. ed. 2006) (describing the Kansas Act and other early securities statutes as "crude affairs").
6. See Richard A. Harvill, *The Economy of Arizona*, 6 ARIZ. BUS. & ECON. REV. 1, 2 (1957) (recapping the 10 years after World War II and noting that Arizona annually ranked first among the states in its rate of increase in total income, bank deposits, and the value of manufacturing, farm and mining output).
7. THOMAS C. SHERIDAN, ARIZONA: A HISTORY 272-73, 278-80 (1995).
8. *Id.* at 274-75.
9. See *State Bar v. Riccardi*, 294 P.2d 537 (Nev. 1931) (regarding Riccardi's disbarment); *Stock Promoter Wanted in East is 'Quite a Man'*, N.Y. TIMES, Mar. 19, 1947 (regarding Riccardi's criminal history).
10. See Herb Nelson, *Receivership Sought for Company*, PHOENIX GAZETTE, Sept. 16, 1948, at 1.
11. See *'Wealthy Rancher' Held in Mind Fraud*, N.Y. TIMES, Mar. 17, 1947.
12. See *Arizona to Inquire Into Mining Concern*, N.Y. TIMES, Jun. 13, 1948; *Princess Charges \$99,500 Swindle*, N.Y. TIMES, May 1, 1947.
13. *Convicted Lawyer Loses*, N.Y. TIMES, Apr. 30 1949, at 19.
14. Dan M. Madden, *Woman to Testify on Riccardi Deals*, PHOENIX GAZETTE, July 10, 1948; Herb Nelson, *Receivership Sought For Company*, PHOENIX GAZETTE, Sept. 16, 1948, at 1; *Board Finds Firm Funds Mishandled*, ARIZONA REPUBLIC, Sept. 17, 1948.
15. Claiborne Nuckolls, *Huge Stock Sale Probe Concluded*, ARIZONA REPUBLIC, Sept. 10, 1949, at 1; Herb Nelson, *Road-Scope Ordered Into Receivership*, PHOENIX GAZETTE, Sept. 13, 1949, at 1.
16. See *State Moves to Wipe Out Stock Frauds*, PHOENIX GAZETTE, Dec. 13, 1948, at 13.
17. See *Legislation for Securities Expert Drawn*, PHOENIX GAZETTE, Jan. 8, 1949, at 11.
18. *Id.*
19. *Id.*
20. *Statehouse Journal: Stock Sales*, MESSENGER, Jan. 22, 1949.
21. See Act of February 26, 1949, ch. 14, 1949 Ariz. Sess. Laws 15.
22. See Robert R. Reed, "Blue Sky" Law, 58 ANNALS AM. ACAD. POL. & SOC. SCI. 177, 179 (1920). Mr. Reed was the IBA's chief counsel for many years.
23. LOSS, SELIGMAN & PAREDES, SECURITIES REGULATION, *supra* note 5, at 62.
24. See *id.* at 63-67.
25. See Louis Loss & Edward M. Cowett, *An Interim Report on the Harvard Law School Study of State Securities Regulation*, 10 BUS. LAW. 15, 16-17 (1955).
26. The four other states were North Dakota (1951), Georgia (1953), Tennessee (1955) and New Mexico (1955).
27. See John M. Welch, *Arizona's 1989 Securities Legislation: A Step in the Right Direction*, ARIZ. ATT'Y, Nov. 1989, at 29 (discussing merit review).
28. The participate-or-induce standard for civil liability in A.R.S. § 44-2003(A) (2003) is an example of a unique provision in the 1951 Act that was not part of the IBA's model legislation.
29. 1949-50 ACC (38th) Annual Report, Securities Department's Report at 4-5.
30. Copies of the 1949 draft and the 1951 session laws are available through the author's webpage at www.tblaw.com.
31. LOUIS LOSS & EDWARD M. COWETT, BLUE SKY LAW 35 (1958).
32. See *id.* 135 (1958) (stating that Arizona "is unique in making certain purchases rescindable Elsewhere it is well recognized that the civil liability created by the blue sky laws is a one-way street running in favor of the buyer." (emphasis in original)).
33. 1951-52 ACC (40th) Annual Report, Securities Department's Report at 1.
34. *Id.*
35. *Id.* at 2.
36. 1953-54 ACC (42nd) Annual Report, Securities Department's Report at 1.
37. *Id.* at 3.
38. *Id.*
39. See, e.g., *State v. Goodman*, 110 Ariz. 524, 521 P.2d 611 (1974).
40. See, e.g., *In re Woodington Group, Inc.*, No. S-2798-I, 1992 WL 409822, at *5-*6 (Ariz. Corp. Comm'n Dec. 10, 1992).
41. See, e.g., *Trump v. Badet*, 327 P.2d 1001, 1005 (Ariz. 1958).
42. See, e.g., *Siporin v. Carrington*, 23 P.3d 92, 95, 99 ¶¶ 15, 35 (Ariz. Ct. App. 2001).
43. See, e.g., Richard M. Weinroth, Pamela H. Gulsvig & Michael L. Kaplan, *Reformation of the Arizona Securities Act: A Brief Summary*, ARIZ. ATT'Y, Aug.-Sept. 1996, at 25.
44. See *Grand v. Nacchio*, 236 P.3d 398 (Ariz. 2010).
45. *Id.* at 401 ¶ 16 (quoting section 20 of the 1951 Act).
46. *Riccardi Gets 10 Years*, N.Y. TIMES, June 22, 1948.