

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of :
PHILIP S. BUDIN & CO., INC. :
PHILIP S. BUDIN :
File No. 8-13488 :

INITIAL DECISION
(Private Proceedings)

February 22, 1974
Washington, D.C.

Sidney L. Feiler
Administrative Law Judge

I. THE PROCEEDINGS

These private proceedings were instituted by order of the Commission pursuant to Sections 15(b) and 15A of the Securities Exchange Act of 1934, as amended, ("Exchange Act") to determine whether certain allegations set forth in the order are true and, if so, what, if any, remedial action is appropriate in the public interest.

The order for the proceedings, as amended, sets forth allegations by the Division of Enforcement (formerly known as the Division of Trading and Markets) that during the period from approximately October 1, 1968 through approximately December 20, 1968 Philip S. Budin & Co., Inc. ("Registrant") and Philip S. Budin, at all times here relevant President of the Registrant, a director, and owner of more than 10% of its shares, willfully violated and willfully aided and abetted violations of Sections 5(a) and (c) of the Securities Act of 1933, as amended, ("Securities Act") in connection with the offer and sale of shares of the common stock of Memory Magnetics, International ("MMI") (at all relevant times known as Comstock-Keystone Mining, Co., "C-K"). It is also alleged that these Respondents during the aforementioned period willfully violated and willfully aided and abetted violations of the anti-fraud provisions of the Securities Acts (Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder) in connection with the offer and sale of the aforementioned securities during the period stated above. It is further alleged that during the relevant period these Respondents willfully violated and willfully aided and abetted violations of Section 10(b) of the Exchange Act and Rule 10b-6 thereunder in connection with the distribution of Comstock-Keystone shares. Additional allegations in the order are that during the relevant period Registrant

violated Section 5(a) and (c) of the Securities Act in connection with the offer and sale of shares of the common stock of XI Production, Inc. and that the Registrant and Budin failed reasonably to supervise persons under their supervision with a view to preventing violations of the Securities Acts and Rules and Regulations thereunder, such persons 1 / having committed violations of said provisions as alleged in the order. The Respondents filed answers in which the material allegations of the order were denied. 2 /

Pursuant to notice a hearing was held in Los Angeles, California, New York, New York, and Miami, Florida. The parties were represented by counsel and full opportunity was afforded them to present evidence and to examine and cross-examine witnesses. Proposed Findings of Fact, Conclusions of Law, and Supporting Briefs were filed on behalf of the parties.

On the basis of the entire record, including his evaluation of the testimony of the witnesses, the undersigned makes the following:

II. FINDINGS OF FACT AND LAW

A. The Respondents

The Registrant has been registered with the Commission as a broker-dealer pursuant to Section 15(b) of the Exchange Act, since October 6, 1967. During the relevant period the firm was engaged in the trading of over-the-counter securities. During the last half of 1968

1 / The order also included allegations against Louis Freshman, who was a trader for the Registrant during the relevant period. The Commission, pursuant to an offer of settlement, has issued its Findings and Order imposing remedial sanctions upon Freshman (Sec. Exch. Act Rel. No. 9542, March 27, 1972). Because of the nature of the charges and the alleged activities of the Respondents and their association with Freshman, this initial decision will necessarily include discussion of the activities of Freshman but solely for the purpose of resolving the issues remaining in this proceeding.

2 / The Respondents stipulated that they made use of the facilities of interstate commerce and of the mails in connection with the transactions set forth in the order.

the firm had 30 to 40 employees with 6 to 8 traders. It made a market in approximately 500 stocks for which it inserted quotations in sheets published by the National Daily Quotation Service, Inc. The retail operations of the firm comprised less than 1% of its total business. It was a member of the National Association of Securities Dealers, Inc., a national securities association registered pursuant to Section 15A of the Exchange Act.

Philip S. Budin, during the relevant period, was the President, a director, and the owner of at least 50% of the stock of the Registrant. In addition to his other duties Budin also acted as a trader and in late 1968 he was placing quotations in the quotation sheets for between 125 and 150 issues a day. Budin had overall supervisory responsibility for the firm, including direct supervisory responsibility for the trading and sales activities of the Registrant.

Louis Freshman, during the relevant period, was a trader for the Registrant having started work there in March 1968. He traded between 75 and 90 different stocks.

B. Activities of the Respondents with Respect to the Stock of Comstock-Keystone

1. History of C-K until June 1968.

C-K, incorporated in 1933, had been a shell corporation with no assets, employees or business operations for at least 20 years prior to 1968. Since 1948 it had been under the control of a Paul Schwarz who kept it alive in the hope that it might be of interest to others for takeover. In the Spring of 1968 Schwarz owned and controlled at least 177,250 shares of the approximately 1,137,000 shares outstanding. He

and his family had options to purchase 350,000 additional¹ shares. Schwarz also was a creditor of C-K to the extent of \$16,000 to \$18,000.

Around April 1968 Angie Anapol and Ben Evans approached Schwarz concerning a possible takeover of C-K and Smuggler Mining Company, another company controlled by Schwarz and his family. Eventually an arrangement was made for the takeover of both C-K and Smuggler by Anapol and his associates, as reflected in the C-K minutes of April 3, 1968 and in the Smuggler minutes of May 20, 1968. Anapol and his associates were elected chief officers of C-K.

In addition to the transactions reflected in the minutes, Anapol and his associate, Evans, asked for some tradeable stock of C-K. Schwarz sold them 100,000 of purportedly free trading shares. Evans at that time made a list showing share amounts and certificate numbers and gave a copy to Schwarz. Schwarz sold an additional 52,000 shares to Anapol when the latter said he needed more stock for persons he was dealing with to take over C-K.^{3/}

2. Acquisition of Control of Comstock-Keystone by Wesley Powers.

Anthony Doria was a long-time acquaintance of Anapol. Through Anapol, Doria acquired approximately 104,000 shares of C-K for approximately 12¢ per share during the months of April and May 1968.

Doria also knew Wesley Powers who owned a California company, Economy Plating Company, and other companies. In a discussion between Powers and Doria, Powers told Doria that he had developed a new computer disc pack and was ready to market it. Doria suggested to Powers that

^{3/} Schwarz testified that due to a mistake on his part he actually delivered certificates for 68,000 to Anapol instead of 52,000 shares which were the subject of the transaction.

that he "go public", but Powers told Doria that this would take a lot of time and would not be of immediate financial help to him. Doria then suggested C-K and Smuggler as vehicles to accomplish Power's plan, and put him in touch with Anapol. Powers met with Anapol in May 1968, and on June 7, 1968, at a meeting in Reno, Nevada, an agreement was reached whereby Powers took over control of C-K and Smuggler.

Under the terms of the agreement, on June 7, 1968, C-K issued 3,515,000 shares of its authorized but unissued shares of stock to Powers, who in return transferred to C-K 1,975 shares of Economy Plating, representing an 80% interest in Economy Plating. Powers thereby acquired approximately a 70% interest in the then outstanding 5,000,000 shares of C-K. At the June 7 meeting, Anapol and his associates resigned as officers and directors, Powers was elected president, and he and his associates became directors and filled the remaining officer positions. After Powers took over control, C-K undertook to engage in the manufacture of computer peripheral equipment and plating. Powers, at all times thereafter, was the dominant factor in the affairs of C-K, made all important decisions, and controlled the activities of C-K.

3. Powers' Participation in the Sale of C-K shares.

No registration statement has ever been filed with the Commission for C-K or Memory Magnetics shares. On June 7, 1968 when Powers took control of C-K, its shares were being traded on the over-the-counter at 15¢ per share. By July 15, 1968 the price had risen to \$8 per share. On July 22, 1968 the Commission issued an order suspending over-the-counter trading in C-K shares stating that its action was based upon the need for information concerning the financial condition and the

activities of C-K (Div. Ex. 8(a)). It noted that shares of C-K had been issued in exchange for shares of Economy Plating and stated that no certified financial data was available concerning Economy and that the last annual report filed by C-K showed that its liabilities exceeded its assets.

In the last week of July 1968, Thomas Matthews, an old friend of Powers discussed with Powers the latter's financial problems and on July 31, 1968 Matthews made an unsecured loan to Powers of \$100,000. At that time, Powers voluntarily gave Matthews a certificate for 5,000 shares of C-K. This certificate was one of the certificates that Schwarz had turned over to the Anapol group.

Matthews testified that a few days prior to August 20, 1968, Powers told Matthews that C-K needed money very badly, that it could collapse and that he (Powers) had formulated a plan whereby more money could be obtained. The essence of the plan was that Matthews would go with Powers to the Torrance Airport. There he would go to a person whom Powers would point out, receive a sealed envelope containing stock certificates, fly with Powers to Las Vegas and then turn the envelope over to a person at the Las Vegas Airport whom Powers would identify.

According to Matthews, this plan was carried out. Powers took Matthews to the Torrance Airport and pointed out a man from whom Matthews obtained a sealed envelope. The man was Anthony Doria, the person who had introduced Powers to Anapol. Doria gave Matthews a sealed envelope and then Matthews and Powers flew in a private airplane

to Las Vegas. ^{4 /} The shares handed Matthews were shares Doria received from Anapol and, of these, at least 50,000 had been obtained by Anapol from Schwarz.

At the Las Vegas Airport, Powers pointed out or introduced Matthews to another man to whom Matthews gave the envelope he had received from Doria. The man was Edward J. Kiefaber, a partner in Universal Securities, a broker-dealer firm.

A few days later Matthews received two documents. One, on Universal stationery, signed by Kiefaber, and dated August 20, 1968 was a receipt for 65,000 C-K shares stated to be deposited for safe-keeping. The other was an option agreement, dated August 20, 1968 purporting to be between Matthews and Kiefaber giving the latter a one-year option to purchase the 65,000 shares at \$5 a share for 32,500 and the balance "at 25% below the going market price at the time of execution." Matthews testified he turned these documents over to Powers.

Thereafter, beginning in October and continuing through December 1968, Matthews received four checks from Kiefaber totalling \$179,000 reflecting proceeds from the exercise of the option. Matthews testified that he turned these checks over to Powers and received notes from him for the amounts, although he did not ask for the notes. Shares from the block Matthews turned over to Kiefaber ultimately went from the latter to the Registrant.

^{4 /} Doria corroborated Matthews' version and testified that at Powers' request he agreed to turn over 75,000 shares of C-K to Matthews and that he placed them in a brown envelope and handed them to Matthews at the Torrance Airport.

Counsel for the Respondents contends that in testimony Matthews gave in the course of an investigation more than two years prior to his testimony in this proceeding his version of what took place was diametrically opposed to his later testimony.^{5/}

In the earlier version, Matthews testified that he had told Powers that he wanted to buy all the C-K shares he could, they discussed a price of 10¢ a share, Matthews got stock from Doria, and flew to Las Vegas with Powers where they met Kiefaber. Matthews agreed to turn over the shares to Kiefaber and left it to the latter to figure out what the shares were worth. Thereafter, according to Matthews in his earlier version, he deposited checks he received from Kiefaber into his own bank account and loaned these sums to Powers or his corporations and endorsed checks over directly. He received notes for the loans and intended to collect on them.

Counsel for the Respondents contends that the investigative testimony given by Matthews is diametrically opposed to that which he gave at the hearing and his testimony at the hearing should be disregarded in its entirety and not be used to make adverse findings against the Respondents.

Matthews testified that prior to his appearance at the investigation Powers told him to say that the funds he received from Kiefaber and turned over to Powers were loans, that the stock he received from Doria was his and that he sold it through Kiefaber (Tr. 526, 528-530). The undersigned agrees with the contention made as to Matthews' testimony.

^{5/} Resps. Ex. 6. Certain portions of this transcript were offered on behalf of the Respondents during cross-examination of Matthews and received for the limited purpose of testing his credibility. The Division offered additional pages from that transcript, pp. 93-110, as amplifying or explaining prior answers. Decision was reserved on this offer. They are received in evidence for the limited purpose stated in the record.

The two versions given by Matthews are completely at variance. The undersigned has decided to accept only that portion of Matthews' testimony which finds corroboration in other independent testimony or from other portions of the record.

Doria's testimony and both versions of Matthews' testimony are in agreement that Doria had no negotiations with Matthews concerning the sale of his stock, nor did he receive any sums from Matthews. Rather, Doria was very definite that he agreed with Powers to turn over his stock to the latter and looked to him for eventual compensation for those shares. The arrangement to turn the envelope containing the shares to Matthews at the Torrance Airport was part of the scheme concocted by Powers.

Matthews did not know Kiefaber until Powers arranged their meeting at the Las Vegas Airport. Of the two versions which Matthews gave as to what transpired there: (1) that he merely handed a sealed envelope to Kiefaber or (2) that he gave the envelope to Kiefaber and also told him that he owned the stock and Kiefaber should give him whatever he could get for it, the former version is the more logical and conforms to the fact that the stock purchase agreement which Kiefaber sent Matthews had a definite purchase price formula and ultimately Kiefaber remitted \$179,000, a not insignificant sum, one which he undoubtedly would not have sent if the price had been left to his discretion.

The undersigned, therefore, concludes that, to the extent indicated, the testimony of Matthews at the hearing finds support in other evidence and is accepted as to the parts played by Powers,

Matthews and Kiefaber in the transfer of 65,000 shares of C-K from Doria (who had obtained them from a person then in control of C-K) to Kiefaber. Budin & Co. ultimately obtained a substantial portion of these shares from Kiefaber. Doria, at Powers request, placed his shares under the control of Powers. Powers made the arrangements with Kiefaber, both as to the delivery and price of the shares. Matthews followed Powers' instructions in the transfer plan and did not share in the proceeds.^{6/}

4. Disposition of C-K Shares by Kiefaber

a. Promotional Activities by Powers and Kiefaber

On September 30, 1968, the Commission issued a release announcing the termination of the C-K trading suspension as of October 7, 1968. It pointed out that until recently C-K had been a dormant "shell" corporation, the company had filed unaudited, incomplete financial data, that an audit then in progress would quite likely show that the company was insolvent. Broker-dealers were cautioned that before effecting transactions in C-K for their customers, they should make the information contained in the release known to their customers and

6/ The one factor that does not fit into this view of the evidence is that Matthews received notes, not requested he claimed, for the money turned over to Powers. Matthews never received any payment on these notes and there is no evidence he pressed for payment.

The evidence demonstrates that Powers was a devotee of devious schemes and devices, including masterminding the transfer of sealed envelopes between strangers and surreptitious meetings at airports. (He used the sealed envelope device in transferring 15,000 C-K shares he obtained from Kiefaber to an investor. These were part of the shares Matthews had turned over to Kiefaber. Powers received the \$15,000 obtained for these shares). Probably the best of his schemes is his disappearance and unavailability for testimony at the hearing. What his motivation was in giving the notes is not clear, but the evidence establishes that there was no loan transaction in Matthews' transfer of the Kiefaber checks to Powers.

avoid violations of the anti-fraud provisions of the Federal Securities Laws (Div. Ex.(8b)).

There is evidence that Powers and Kiefaber took action designed to blunt the impact of the Commission's cautionary admonition to brokers and investors and to organize an effective stock-selling scheme.

Emmett Paddon, a Detroit resident, had been a friend of Powers for a number of years and had had some business dealings with him. In the early part of 1968 Powers met with Paddon at the Detroit Airport and sought to have him make a personal investment in C-K or to raise a substantial investment fund with others. Nothing came of this meeting, according to Paddon, although Powers continued to call him from time to time with optimistic reports on the C-K stock.

Later in the year, in November, when Paddon said he was interested in the stock and wanted to know what Powers had in mind, the latter said he would "turn [him] over to Ed Kiefaber" (Tr. 692). Powers gave Paddon contradictory answers as to Kiefaber's association with him, but did assure Paddon that, "Kiefaber knows everything I do. Whatever Kiefaber tells you is the same as my telling you." (Tr. 693)

Shortly afterwards, Paddon started receiving calls from Kiefaber. Kiefaber told him that he had made arrangements with stock brokers whereby a position would be taken in a stock and the price would be moved up by pre-arrangement. He suggested that Paddon buy C-K stock and, according to Paddon, told him to do business with Philip Budin of New York (Tr. 697, 717-718).

Paddon bought no C-K stock at that time, but at the end of November, 1968 or the beginning of December, when he picked up Kiefaber

at the Detroit Airport, he placed an order for some of the stock at the latter's urging. Kiefaber had come to Detroit to meet brokers and to talk to them about C-K.^{7/} During the course of Kiefaber's 3-day visit, Paddon introduced him to 3 brokers whom he knew personally and accompanied him on visits Kiefaber made to approximately 9 other brokerage offices.

Paddon testified that Kiefaber made a uniform presentation to brokers stating that he had a network of brokers, who would work with him to increase the price of a stock he was interested in, offered brokers options in C-K stock and spoke of increases in price and earnings it would attain.

Kiefaber also suggested to Paddon that he carry on after him and make similar presentations to other brokers. At Paddon's suggestion, he made a tape of a model presentation and left it with Paddon (Div. Ex. 43). The tape which was transcribed into the record herein (pp. 723-731) started as a presentation of the merits of C-K, mentioned a recent contract for \$20,000,000, other contracts, and estimated gross sales of \$50 to 60,000,000, with earning of \$2 to \$3 per share. The statement was made that "we are conservatively looking at a \$70, \$80 stock at the end of '69" (Tr. 726, the stock was then selling at about \$21). Mention also was made of a network that would act in concert and move the stock to any level it wanted. Paddon testified that he heard Kiefaber use a presentation to brokers in his presence similar to that on the tape and adding the inducement of stock options.

^{7/} Powers, according to Paddon, knew that Kiefaber was coming to Detroit and had told Paddon that he would take care of any expenses incidental to showing him around (Tr. 700).

According to Paddon, Kiefaber made numerous telephone calls to brokers and several of these were to Philip Budin. He did not recall the content of these conversations (Tr. 780-781).

Paddon's testimony was corroborated by that of John T. DeHayes, a broker to whom Kiefaber made a sales presentation on C-K after being introduced by Paddon. DeHayes stated that Kiefaber offered him a stock option for 300 shares at several points below the market, told him that the stock should sell at about \$70 in a year, that he was going to make calls on a number of brokerage houses, after which the stock would rise. DeHayes also identified a pamphlet which Kiefaber showed him -- an Economic Report to C-K by a purported "Financial Relations and Underwriting" firm forecasting sales of \$30 million in 1969 and \$59 million in 1970 and net income of \$4 million in 1969 and \$10 million in 1970 (Div. Ex. 31).

The undersigned credits Paddon's testimony and concludes that the evidence establishes that Powers and Kiefaber were engaged in an extensive effort to interest brokers in different cities to join in a group effort to manipulate the price of C-K stock and push the price up to the mutual benefit of all participants in the scheme.^{8 /}

8 / Objection was made to this evidence on hearsay and relevancy grounds. The Commission has stated, in Alessandrini & Co., Inc., Sec. Ex. Act Rel. No. 10466 p. 9, (Oct. 31, 1973) "It is well established that the technical hearsay rules are not applicable to administrative proceedings which favor liberality in the admission of evidence, and that all evidence which 'can conceivably throw any light upon the controversy' should normally be admitted in such proceedings," citing Samuel H. Moss, Inc. v. F.T.C. 148 F. 2d 378, 380 (C.A. 2, 1945), Cert. den 326 U.S. 734, (1945).

The evidence also is relevant on the question of the connection between Powers and Kiefaber and the part they played in the distribution of stock that ultimately wound up at Budin and Co. When there is participation in a distribution of unregistered stock, those who play some part do not necessarily know everyone who plays some part and evidence of the entire course of events is necessary to understand exactly what took place (see S.E.C. v. North American Research and Development Corp., 424 F. 2d 63, 1970).

That Powers and Kiefaber were successful in their scheme is demonstrated by the fact that on October 7, 1968, when the Commission permitted over-the-counter trading in C-K to resume, it opened at about \$10 a share. It rose steadily thereafter until it traded at approximately \$20 by December 17, 1968. On that date the Commission again suspended trading in C-K, stating that the suspension was ordered "by reason of the dissemination by the company of financial and other information about the company, its operations, financial condition and future prospects which appears to be false and misleading." Also an audit report had not been filed, as expected (Div. Ex. 8 (c)).

b. Participation of Respondents in the Purchase and Sale of C-K Shares.

At all times here relevant Louis Freshman was a trader employed by the Registrant. His wife owned a 50 percent interest in the firm.^{9 /} Freshman initiated trading in C-K by the Registrant

According to Freshman, he first heard of C-K when, on a Western trip, he stopped off in Las Vegas and noticed the offices of Universal Securities. He had done some business with this firm and went in for a visit. While waiting to see Kiefaber, who was associated with Universal, he heard persons asking for quotations on C-K. Freshman then asked Kiefaber about the stock. The latter told him it was a stock he had an interest in and that he himself had bought an "awful lot of the stock on the market." (Tr. 910). Additional information that he obtained from Kiefaber at that time, Freshman testified, was that a Budin correspondent was handling the stock, that the company made peripheral drives, was producing material cheaper than any competitor, and had been suspended

9 / It has been previously noted that Freshman, while named in the order for these proceedings, is no longer a party (see fn. 1).

by the Commission, but was "reinstated," and that he, had bought "quite a bit of the stock" for himself. While Freshman had no present recollection of it, he did testify in the course of an investigation conducted while he was still employed by the Registrant, that Kiefaber suggested that C-K would be a good trading number for him "to go into the sheets with." (Div. Ex. 47(a), p. 21).^{10/} Freshman did not receive any further information about C-K from Kiefaber or any details on the suspension. He recalled that Kiefaber had mentioned acquiring about 25 or 30,000 shares, on the open market, but made no effort later to check on the sources from which he had acquired the stock.

Continuing his testimony, Freshman stated that about a week later, after talking to a trader employed by the Budin California correspondent who assured him it was "a good trading number," he decided to trade C-K. He telephoned an assistant and told him to enter quotations in the pink sheets. He made no effort to learn anything further about the issue.

Shortly thereafter, Freshman received an inquiry from the correspondent, P.N. McIntyre, asking whether he had stock available -- 3,000 shares was the amount sought. Freshman attempted to reach Kiefaber, at Universal Securities, but was told that he was no longer associated with that firm. He did reach Kiefaber and did purchase 3,000 C-K shares from him.

^{10/} Respondents have objected to the use of any portions of Freshman's investigative transcript as against them. Freshman's testimony was given while he was in the employ of the Registrant and dealt with matters within the scope of his employment and peculiarly within his knowledge. The objections are not valid (McCormick, "Evidence", p. 518).

Records in evidence show that the initial appearance of the Registrant in the pink sheets was on October 22, 1968 (Div. Ex. 33). The transaction with Kiefaber took place on the preceding day, October 21 (Div. Ex. 35). Thereafter Budin & Co. continued to quote C-K in the pink sheets through December 17, 1968 with most of the quotations inserted by Freshman. Freshman also effected the firm transactions in the stock. He had no discussions about the merits of C-K either when he purchased or sold the stock at retail or in dealings with other brokers (Tr. 939-940). He stated that he had no discussion about the stock with Budin and since the firm was trading about 500 stocks a day, C-K did not loom large in the firm's affairs. Budin would receive a printout showing each trader's position at the end of the prior day and whether he had made or lost money (Tr. 943). Freshman also stated he unilaterally determined to quote C-K and that Budin who was with him during part of the aforementioned western trip knew of his decision (Tr. 958).

Freshman conceded that Kiefaber told him initially that he had 25 or 30,000 shares of C-K. He denied that he made any agreement to sell them or that Kiefaber said he wanted to sell them.^{11/} He maintained that each transaction he had with Kiefaber was an individual transaction as a result of hard bargaining. Kiefaber would call several times a day for quotations, he stated, but came to the office once or twice. Freshman stated that Kiefaber originally had told him he had bought his shares on the open market and that checking was done with the transfer agent on shares purchased from Kiefaber. He denied that he received any money or other inducements to make a market in C-K.

11/ In his investigative testimony he testified that Kiefaber had said he wanted to sell his shares (Tr. 968-970).

Registrant's principal transactions in C-K commenced on October 21, 1968 and ended on December 17, 1968, the date of the second suspension of trading (Div. Ex. 35). It purchased 35,625 shares at a cost of \$506,762.50 and sold 35,705 shares at total price of \$524,923.75. (Div. Ex. 35). There was only one agency transaction of 4,000 shares at a price of \$30,000 (Div. Ex. 36).

Transactions with Kiefaber by the Registrant in C-K stock began on October 21, 1968 and ended on December 10, 1968. All transactions were purchases by Registrant from Kiefaber. Registrant purchased 23,800 shares from Kiefaber and also purchased for retail customers 4,000 shares from him upon an agency basis. These shares were all subsequently sold by or through Registrant to other broker-dealers.

Kiefaber severed his connection with Universal Securities prior to his first C-K transaction with the Registrant, and Freshman, who negotiated the trade, knew this. Kiefaber's new account card at Registrant, dated October 23, 1968, lists his occupation as "insurance agent". All certificates he tendered Registrant with the exception of those for 300 shares were in the name of Unico and were shares which Kiefaber had received from Matthews. Almost all C-K shares delivered by Kiefaber were in street name.

Registrant's practice on receipt of stock from Kiefaber was to telephone the C-K transfer agent to find out if the certificates were "free and clear" or had any restrictions against them (Tr. 809). Four such calls were made and payment then made to Kiefaber. Registrant remitted \$311,700 to Kiefaber. At least \$179,000 was sent by Kiefaber to Matthews, who turned this money over to Powers (Tr. 205 - 210).

Contentions of the parties; Conclusions

The Division contends that the Respondents willfully violated the registration provisions of the Securities Act in the offer and sale of C-K stock.^{12/} It is conceded that no registration statement was ever filed with respect to any C-K shares and that the Registrant used the facilities of interstate commerce and of the mails in effecting transactions in C-K.

The Division contends that there was a violation of Section 5 by the Respondents, that the burden of proving an exemption from Section 5 is on the Respondents, and that no exemption was established. It is also urged that no adequate inquiry was made to determine whether Registrant was participating in a distribution of C-K, as defined in the Securities Act.

The Respondents contend that Registrant's transactions in C-K were exempt transactions and that after trading resumed in C-K on October 7, 1968 after the suspension by the Commission other broker-dealers both in the East and the West quoted C-K, although the extent of their transactions in it is not available. It also contends that Matthews' testimony, which has been dealt with in some detail, should be disregarded and that Registrant should be held to have engaged in exempt dealer transactions as defined in Section 4(3) of the Securities Act.

^{12/} Section 5 of the Securities Act provides, in pertinent part, that it shall be unlawful to make use of the instruments of transportation or communication in interstate commerce or of the mails to offer to sell or to sell a security unless a registration statement is in effect as to it.

In any event, it is asserted, any violation of Section 5 was not willful, the Respondents did not know that any C-K shares Registrant sold were part of a distribution, there were no circumstances surrounding the transactions between Registrant and Kiefaber which should have alerted them to make any inquiry, and that any searching inquiry, even if undertaken, would have unearthed nothing.

It is undisputed that Registrant offered to sell, sold, and delivered C-K stock when no registration statement was in effect as to those securities. Therefore, Registrant's sales activity was violative of Section 5 of the Securities Act unless some exemption from the registration provisions can be established. The burden of proof is ^{13/} on the party seeking to establish the availability of an exemption.

The exemption relied on must be strictly construed against the person ^{14/} claiming its benefit, as public policy strongly supports registration. ^{15/}

Certain transactions are exempt from the provisions of Section 5 of the Securities Act pursuant to the provisions of Section 4 of that Act. However, no exemption is available under this section to an issuer or underwriter (Sec. 4(1)). The term "underwriter" is defined in Section 2(11) of the Securities Act as:

" . . . any person who has purchased from an issuer with a view to, or offers or sells for an issuer in connection with, the distribution of any security, or participates or has a direct or indirect participation in any such undertaking, or participates or has a participation in the direct or indirect underwriting of any such undertaking; . . ."

^{13/} SEC v. Ralston Purina Co., 346 U.S. 119, 126 (1953); Pennaluna & Co., Inc. v. SEC, 410 F. 2d 861 (C.A. 9, 1969), cert. den. 396 U.S. 1007 (1970); SEC v. Culpepper, 270 F. 2d 241, 246 (C.A. 2, 1959).

^{14/} U.S. v. Custer Channel Wing Corp., 376 F. 2d 675, 678, cert. den. 389 U.S. 850 (1967); SEC v. Sunbeam Mines, 93 F. 2d 699 (C.A. 9, 1938).

^{15/} Garfield v. Strain, 320 F. 2d 116, 119 (C.A. 10, 1963).

With respect to an "issuer", the section states:

". . . As used in this paragraph the term "issuer" shall include, in addition to an issuer, any person directly or indirectly controlling or controlled by the issuer, or any person under direct or indirect common control with the issuer. . . ."

"Distribution" has been held to comprise "the entire process by which in the course of a public offering the block of securities is dispersed and ultimately comes to rest in the hands of the investing public."^{16/}

Applying these principles to the facts of the instant case, it is evident that, at all times here relevant, Powers was an "issuer" within the meaning of the Securities Act as a person in control of C-K both by reason of his position as operating head of C-K and his stock ownership.

The evidence further establishes that Doria, who had obtained his shares through a person then in control of C-K, placed those shares at the disposition of Powers. It makes no difference on this point, that the shares were actually handed by Doria to a nominee of Powers (Matthews) rather than to Powers, himself. At that point the shares were under the control of Powers, an issuer.

Kiefaber had a close relationship with Powers.^{17/} The plan to move the Doria shares to Kiefaber was devised by Powers with the connivance of Kiefaber. At that point, Kiefaber fell within the definition of

^{16/} Oklahoma - Texas Trust, 2 S.E.C. 764,769 (1932), aff'd 100 F. 2d 888 (C.A. 10, 1939); Ira Haupt & Company, 23 S.E.C. 589,596-599, (1946); Lewisohn Copper Corp.; 38 S.E.C. 226, 234-235 (1958).

^{17/} In addition to evidence previously detailed, there is evidence that Kiefaber had free use of the C-K office in Las Vegas (Tr. 274-279).

issuer since he was working with Powers in a joint scheme for the disposition of C-K shares and the manipulation of the market. He also was an "underwriter" as that term is defined in the Securities Act since he was playing a vital part in the distribution of the Doria shares, among others, to the public. Most of the shares Kiefaber turned over to Registrant were part of the Doria block and went from the Registrant into the general stream of distribution to the investing public. Thus Registrant played a key role in the distribution process as defined in Section 2(11) of the Securities Act.

Of the 35,625 C-K shares purchased by Registrant as principal, 30,500 (86%) came directly or indirectly from Kiefaber ^{18/} (Div. Ex. 35). The remainder of 5,125 shares came from other brokers. The record of the purchases from Kiefaber is as follows. ^{19/}

<u>Trade date</u> <u>1968</u>	<u>Number Shares</u> <u>Purchased</u>	<u>Cost or Price</u> <u>Per Share</u>	<u>Total</u> <u>Cost</u>	<u>Firm</u> <u>Position</u>	<u>Budin Cost</u> <u>Per Share</u>	<u>Budin Pink</u> <u>Sheet Bid</u>
Oct. 21	3,000	\$ 8	\$24,000	3000L		
Nov. 7	2,000	6½	13,000	1900L	6½	6
" 14	1,000	7½	7,500	1000L	7½	6
" 18	2,300	10½	23,575	1555S	10½	7½
" 18	4,000	12½	50,000	2945L	12½	9½
" 26	1,000	13 3/4	13,750	3270S	13 3/4	13½
" 27	4,000	14 3/4	59,000	3545S	14 3/4	13½
" 29	1,000	19	19,000	2745S	19	16
" 29	2,000	17	34,000	745S	17	16
Dec. 6	2,000	14 3/4	29,500	5105L	14 3/4	16
" 10	1,500	14 3/4	22,125	1405L	14 3/4	

^{18/} 6,700 shares which came from Kiefaber were sold to retail customers who then resold the shares to Registrant (Div. Ex. 41).

^{19/} This table does not include an additional transaction of 4,000 shares bought on November 29, but cancelled as of December 6.

There was in addition a single agency transaction on November 14 when Registrant purchased 4,000 shares at \$7½ per share and divided them among 3 accounts, a Budin profit-sharing account, David Budin, Budin's brother, and Phyllis Freshman (Freshman's wife)(Div. Ex. 36).

The Commission has summarized applicable principles and key decisions in a release published in 1962.^{20/} In it, it cautioned broker-dealers of steps they must take to avoid participation in an illegal stock distribution. In particular, it stated:

". . . a dealer who offers to sell, or is asked to sell a substantial amount of securities must take whatever steps are necessary to be sure that this is a transaction not involving an issuer, person in a control relationship with an issuer or an underwriter. For this purpose, it is not sufficient for him merely to accept 'self-serving statements of his sellers and their counsel without reasonably exploring the possibility of contrary facts'.

The amount of inquiry called for necessarily varies with the circumstances of particular cases. A dealer who is offered a modest amount of a widely traded security by a responsible customer, whose lack of relationship to the issuer is well known to him, may ordinarily proceed with considerable confidence. On the other hand, when a dealer is offered a substantial block of a little-known security, either by persons who appear reluctant to disclose exactly where the securities came from, or where the surrounding circumstances raise a question as to whether or not the ostensible sellers may be merely intermediaries for controlling persons or statutory underwriters, then searching inquiry is called for.

The problem becomes particularly acute where substantial amounts of a previously little known security appear in the trading markets within a fairly short period of time and without the benefit of registration under the Securities Act of 1933. In such situations, it must be assumed that these securities emanate from the issuer or from persons controlling the issuer, unless some other source is known and the fact that the certificates may be registered in the names of various individuals could merely indicate that those responsible for the distribution are attempting to cover their tracks." (footnote omitted)

^{20/} Sec. Act Rel. No. 4445 (Feb. 2, 1962).

Freshman denied that he ever received all the Kiefaber shares purchased in one lot from the latter or had any agreement to market those shares. The record of the various purchase transactions would seem to bear him out. Respondents argue, in effect, that Registrant was never offered a large block of C-K stock by Kiefaber, but only made purchases from him in separate, individual trades, each of which was not large.

However, these trades cannot be evaluated in isolation. It is evident that Kiefaber was by far the key supplier of C-K to the Registrant. Kiefaber had the status of a retail customer, having severed his connection with Universal Securities shortly after Freshman met him, but he was no ordinary retail customer, and Freshman did not treat him as such. Freshman knew of Kiefaber's experience as a professional trader. He had learned from Kiefaber that he had bought 25 to 30,000 shares. While he denied in his testimony at the hearing that Kiefaber told him he wanted to dispose of all those shares, he did state that Kiefaber would call him 2 or 3 times a day to find out Freshman's quotations on C-K and offer to sell him some shares. (Div. Ex. 47(a) p. 43-44). The purchases Freshman made from Kiefaber enabled the former to maintain a market in C-K and to complete his other transactions in that stock. The transactions with Kiefaber occurred so frequently and in so short a period that they can only be viewed in their totality and not in isolation. As such, they were the prime source of supply of C-K shares for Registrant and totalled a substantial amount.^{21/} The undersigned concludes that Registrant violated

21/ The Commission has held that when shares emanate from an issuer, the fact that a relatively small amount of shares are involved does not make the sales any the less a public distribution requiring registration under the Securities Act and sales by a person who obtained his shares from the issuer cannot be likened to ordinary trading activity (Merrill Lynch, Pierce, Fenner & Smith, Inc., Sec. Exch. Act Rel. No. 9959, (Jan. 24, 1973)).

the registration provisions of the Securities Act in the offer and sale of C-K stock, by acting as underwriter for C-K stock.

Budin had knowledge of the Registrant's participation in C-K from the beginning. He was with Freshman during part of the latter's western trip when Freshman first met Kiefaber. Freshman told Budin there that he intended to trade C-K. Budin bought 2,000 shares of C-K for his wife's account at the Registrant. Others who would have undoubtedly looked to him for guidance also bought C-K. His brother, David, bought 3,000 shares in two transactions (Tr. 944). A close friend, Melvin Haber, bought 1,000 shares in two transactions. A Budin Profit Sharing Plan, in which Budin would have had a voice, bought 1,000 shares. All these purchases were liquidated within a 3-week period at substantial profits (Div. Ex. 37).

Budin occasionally took telephone calls from Kiefaber when the latter wanted quotations on C-K and would give him that information (Tr. 1118-1119). He knew of the course of the trading by Freshman in C-K and participated in it. Under these circumstances, it is concluded that he aided and abetted the violations by the Registrant of Section 5 of the Securities Act.^{22/}

^{22/} Respondents are responsible for the violations committed by their staff under the doctrine of respondeat superior (Armstrong, Jones & Co., Sec. Exch. Act Rel. No. 8420 (Oct. 3, 1968)), aff'd 421 F. 2d 359, 362 (C.A. 6, 1970), cert den. 398 U.S. 958 (1970).

Respondents contend that any violations of Section 5 of the Securities Act, even if committed by them, were not willful. It is well established that a finding of willfulness under the Exchange Act does not require an intent to violate, but merely an intent to do the act which constitutes a violation.^{23/} The Commission has held that brokers have a responsibility to be aware of the requirements necessary to establish an exemption from the registration requirements of the Securities Act and be reasonably certain that such an exemption is available before engaging in transactions which raise a question of compliance with those requirements.^{24/}

There was ample evidence to alert the Respondents to the need for further investigation before continuing their trading with Kiefaber. Kiefaber initially suggested that Freshman trade C-K. Kiefaber was in touch with Freshman several times a day checking Registrant's C-K quotations and negotiating trades. All his transactions were sales -- it was evident he was unloading a block of stock. Freshman's trades with Kiefaber, beginning in November 1968, were frequent and substantial (see table p. 21). Freshman was using Kiefaber as his major source of supply of C-K stock.

^{23/} Tager v. SEC, 344 F. 2d 5, 8 (2nd Cir. 1965), affirming, Sidney Tager, Sec. Exch. Act Rel. No. 7368 (July 14, 1964); Accord, Harry Marks, 25 S.E.C. 208, 220 (1947); George W. Chilian, 37 S.E.C. 384 (1956); E.W. Hughes & Company, 27 S.E.C. 629 (1948); Hughes v. SEC, 174 F. 2d 969 (C.A.D.C. 1949); Shuck & Co., 38 S.E.C. 69 (1957); Carl M. Loeb, Rhoades & Co., 38 S.E.C. 843 (1959); Ira Haupt & Company, 23 S.E.C. 589, 606 (1946).

^{24/} See, e.g., Strathmore Securities, Inc., Securities Exchange Act Release No. 8207, p. 8 (December 13, 1967); Mark E. O'Leary, Securities Exchange Act Release No. 8361, p. 7, n. 13 (July 25, 1968). As two Courts have stated, "Brokers and salesmen are under a duty to investigate and their violation of that duty brings them within the term willful." Hanly v. S.E.C., 415 F. 2d 589, 595-6 (C.A. 2, 1969); Quinn and Company, Inc. v. S.E.C., 452 F. 2d 943, 947, (C.A. 10, 1971), cert den., 406 U.S. 957 (May 30, 1972).

Yet beyond checking the certificates received from Kiefaber with the C-K transfer agent, Respondents did nothing. This was insufficient under the circumstances.^{25/}

Respondents assert that any investigation by them would not have revealed anything.^{26/} Actually, if Respondents had reviewed the Commission's suspension order, they would have noted that C-K was a newly reactivated shell and it was probably insolvent.^{27/} The precipitous price rise of its stock thereafter should have given Respondents reason for further checking on Kiefaber and his sustained interest in the stock. The fact that other brokers were quoting the stock does not excuse Respondents' failure here because the actual trading by those brokers has not been established nor the extent of their knowledge of C-K, Kiefaber and Powers. Another item that should have given Respondents some pause was that Kiefaber came to them to trade while the center of C-K trading activity, according to Freshman, was on the West Coast.

Freshman made it abundantly clear in his testimony that he was only interested in what the telephone told him, as he put it. The evidence establishes that this approach was adopted and acquiesced in by the Respondents. The undersigned concludes that their violations were willful.

^{25/} Inquiry from the transfer agent was insufficient. Although the transfer agent could furnish information on the state of the transfer records he was not an arbiter of the validity of transactions (Stead v. S.E.C., 444 F. 2d 713, 716 (C.A. 10, 1971)).

^{26/} The Commission has held that it need not speculate what reasonable inquiry would have disclosed where no such inquiry has been made. Herbert L. Wittow, Sec. Ex. Act Rel. 9303 p. 7, n. 20 (1971); Strathmore Securities Inc., 43 S.E.C. 575, 584 (1967) aff'd 407 F. 2d 722 (C.A.D.C. 1969); L.A. Frances Ltd., Sec. Ex. Act Rel. 9220 p. 5 (1971).

^{27/} "Where the sale of securities of a shell corporation is involved, it is incumbent on a broker-dealer to exercise special care so as to be reasonably assured that no violation of the securities laws is involved" (Bohn-Williams Securities Corp., Sec. Exch. Act Rel. No. 9327, p. 4, 1971).

5. Violations of the Anti-Fraud Provisions of the Securities Acts

It is alleged in the order for these proceedings that the Respondents, singly and in concert, willfully violated the anti-fraud provisions of the Securities Acts in a number of respects.^{28/}

a. Arrangements with Kiefaber

It is alleged in the order for these proceedings that the Respondents entered into an agreement under which they agreed to and did purchase unregistered securities of C-K for Registrant's account and for the accounts of Budin, Freshman and members of their families. It is evident that Kiefaber and Freshman did find it mutually advantageous to deal with one another on a regular basis. Freshman decided to trade C-K at Kiefaber's suggestion and after some discussion with a trader from Registrant's California correspondent Freshman almost immediately completed a 3,000 share C-K trade with Kiefaber. The record of Kiefaber's transactions with the Registrant has been previously set forth (supra, p.21). It shows very clearly that Freshman used Kiefaber as his principal source of supply of C-K stock and Kiefaber used Registrant as a principal outlet for his C-K shares. There are other indications that the relationship between Freshman and Kiefaber was not a casual one. At one point, Kiefaber told Paddon to deal with Budin & Co. While Kiefaber had the status of a retail customer, Freshman dealt with him substantially as a

^{28/} Section 17(a) of the Securities Act and Section 10(b) of the Exchange Act and Rule 10b-5 thereunder. The composite effect of these provisions, as applicable here, is to make unlawful the use of the mails or interstate facilities in connection with the offer or sale of any security by means of a device or scheme to defraud or untrue or misleading statements of a material fact, or any act, practice, or course of conduct which operates or would operate as a fraud or deceit upon a customer or by means of any other manipulative or fraudulent device.

trader. Kiefaber was in daily communication with Freshman seeking C-K quotations and negotiating C-K sales. He was not charged any commission on an agency sale. Budin & Co. was on the East Coast whereas according to the evidence presented the center of interest in C-K was on the West Coast and it appeared strange for Kiefaber to deal with a broker 3000 miles away from the center of interest.

All the above items are indicia of more than a routine trading relationship between Registrant and Kiefaber. However they fall short of establishing a definite agreement between those parties for the purchase of unregistered C-K shares by Registrant from Kiefaber. Budin & Co. made its first C-K trade with Kiefaber on October 21. Its next transaction with him was on November 7, two weeks later. This is hardly indicative of a firm agreement between Budin & Co. and Kiefaber. The ten transactions between them were negotiated over a two-month period at different prices. The evidence does not establish anything more concrete than that Registrant and Kiefaber developed a close relationship whereby Kiefaber became the major supplier of C-K stock to Registrant and Kiefaber, thereby, was able to dispose of a substantial amount of unregistered C-K stock. These shares went into Registrant's account as principal, primarily, and Budin, Freshman and members of their families acquired shares directly or indirectly which they sold at substantial profits within a few weeks of their purchases.

b. Quotation Activity

It is alleged that quotations for C-K by Registrant were entered in the National Daily Quotation Service (Eastern Edition, commonly referred to as the "pink sheets") and thereby giving the appearance of making a bona-fide two-sided market when, in fact, a bona-fide two-sided market was not being made in that said quotations were being made below the prevailing prices at which said securities were being quoted; said activities being carried out in order to facilitate a distribution of said shares and for the purpose of attracting buying interest and of discouraging other selling interest in C-K.

The Division contends that Budin & Co. had an agreement with Kiefaber to sell his stock; to effectuate this agreement, Budin & Co. inserted unrealistically low quotes in the sheets seeking only to attract buying interest in order to distribute Kiefaber's stock and to deter other selling interest. Ultimately, Registrant acquired 86% of its total C-K shares from Kiefaber. It is argued that Registrant consistently traded at prices much different from its quotations over a two month period.

The trading ban on C-K was lifted on October 7, 1968 and trading in C-K commenced immediately and continued until December 17, 1968 when a trading suspension was again reimposed. During this period 14 broker-dealers appeared in the pink sheets, some more frequently than others. Budin & Co. first appeared in the pink sheets on October 22, and was listed a total of 30 times until December 13, including dates when its name appeared with no quotations (Div. Ex. 33). During the same period, 9 broker-dealers appeared in the Western Edition of the National Daily Quotation Service ("White Sheets"), 3 of whom also appeared in the

pink sheets (Div. Ex. 34). Budin & Co. did not appear in the white sheets. As previously noted, the greatest trading interest was on the West Coast.

The issue raised here is really a two-part issue, although there is an inter-connection. The first part relates to the quotations inserted by the Registrant in the pink sheets. The Division contends these were unrealistically low, inserted to deter selling interest and to attract buying interest for the purpose of facilitating the distribution of Kiefaber's stock. Respondents argue that this contention has not been established, pointing out that of the 25 quotations inserted by Budin & Co. for C-K stock it had the lowest bid of all broker-dealers on 11 days, but only on 3 of these days was it the lowest of all broker-dealers (Div. Ex. 33). On two of the days Registrant's bid was lowest by a point and on the other day it was lowest by $\frac{1}{2}$ a point. The rest of the days there were a substantial number of brokers who submitted the same or lower bids.

On the ask side, other brokers had lower bids than Registrant on 17 of the 24 days Registrant inserted bids in the pink sheets. On 3 of the remaining 7 days, other brokers had the same ask price.

A large number of brokers placed quotations in the sheets for C-K in the October--December 1968 period. Under ordinary conditions it would have been impossible for Budin & Co. or any other broker to have been able to exercise control in the market unless he was the leader of a conspiracy, joined in by most of the other brokers, or if he controlled

the supply of the stock. No evidence has been presented as to the existence of any conspiracy nor is there any proof as to the actual activity of other brokers in C-K. While Budin & Co. had quotations on the low side on a number of days, it cannot be said that the record establishes that it had unrealistically low quotations during the 29/ period.

The other part of the issue raised is the relationship between the quotations Registrant was inserting in the pink sheets and the prices at which it was concluding contemporaneous trades.

The Division points out that on 8 or the 25 dates that Budin & Co. placed quotes in the pink sheets, the firm executed no trades at their quoted prices, rather all their trades were above the quotations, including trades with Kiefaber (Div. Ex. 35).

Of Budin & Co.'s 39 buy transactions, 27 (69%) were over its bid price, 3 (8%) were below it, two (5%) were at the bid price and for 7 (18%) there were no comparison bid prices. Of the 27 that were above the bid price, 12 (44%) were 2 points or more over it and 21 (78%) were a point or more over it.

On the sell side, of the 71 transactions involved, 34 (48%) were above the asked price, 16 (22%) were below it, 9 (13%) were at it, and for 12 (17%) there was no comparison asked price. Of the 34 trades above the asked price, 11 (32%) were 2 or more points over it, and 22 (65%) were a point or more over the asked price. The Respondents contend that the

29/ It is deemed unnecessary to review the white sheet quotations on this question (Div. Ex. 34).

Budin & Co. quotations in the pink sheets merely showed its range of prices and that it was not bound to stay within those limits.

It has been pointed out in the Special Study of the Securities Markets that, "the 'sheets' published by the National Quotation Bureau, Inc. . . . are the primary medium for the dissemination of wholesale or 'inside' quotations among professionals. They are of crucial importance to the over-the-counter markets. . . . Professionals use the sheets to find and communicate buying and selling interests in securities and to judge activity."^{30/} These quotations are affected with a public interest (Exchange Act, Sec. 2) and have been held to constitute proof of prevailing market prices.^{31/}

A comparison of Registrant's actual trades, especially its purchases, demonstrates that the prices paid were consistently over its contemporaneous bid price in the pink sheets. The differences in many instances were substantial. Several trades with Kiefaber had a spread of 3 points (see table p. 21). There were a few 4 points gaps. (Div. Ex. 35). There was a fairly consistent pattern of these substantial spreads from mid-November 1968 until the end of Registrant's trading in C-K stock.

The result of these practices was that the pink sheet quotations of Budin & Co. did not reflect the actual market it was making in C-K stock. The divergencies were not fractional, but substantial. They continued over a long period and while quotations were changed the practice of inserting lower than actual market quotes continued. These quotations could not then be regarded as indicative of Registrant's current market in C-K stock. To that extent they were a misrepresentation

^{30/} Report of Special Study of Securities Market, Part 2, p. 585.

^{31/} Merritt, Vickers Inc. v. SEC 353 F. 2d 293, 296 (C.A. 2, 1965).

of Registrant's position, were a misuse of the quotation system, and by these acts, the Respondents willfully violated the anti-fraud provisions of the Securities Acts.

c. Activities while effecting a distribution of C-K shares.

It is also alleged that the Respondents effected a distribution of C-K shares, and in connection therewith failed to make any disclosure of the source of said stock, the interests of Registrant, Budin, Freshman and members of their families therein, the nature of the market being made by Registrant, and the facts and circumstances under which said securities had been acquired.

It is also alleged that while engaged in the aforesaid distribution, Respondents bid for and purchased C-K securities for accounts in which they had a beneficial interest and induced and attempted to induce other persons to purchase said securities. This conduct is alleged to be violative of the anti-fraud provisions of the Securities Acts and of Section ^{32/} 10(b) of the Exchange Act and Rule 10b-6 thereunder.

It has been found that the Respondents participated in a distribution of shares purchased from Kiefaber, the latter having acquired the shares and acted for an issuer. It is undenied that while transactions with Kiefaber were taking place, the Registrant was bidding for and purchasing C-K stock for its account and that the facilities of interstate commerce were being used in the process.

^{32/} Regulation 10b-6, promulgated pursuant to Section 10(b) of the Exchange Act provides, in pertinent part, "It shall constitute a 'manipulative or deceptive device or contrivance' as used in Section 10(b) of the Act for any person, . . . (3) who is a broker, dealer, or other person who has agreed to participate or is participating in such a distribution, directly or indirectly, by the use of any means or instrumentality of interstate commerce, or of the mails to bid for or purchase for any account in which he has a beneficial interest, any security which is the subject of such distribution . . . or to attempt to induce any person to purchase such security . . . until after he has completed his participation in such distribution."

Respondents contend that they were not engaged in a distribution, an issue which the undersigned has considered in connection with the Section 5 violation. It is further urged that cases relied on by the Division are inapposite to the evidence adduced in the instant case, maintaining that those cases are factually distinguishable from the instant case, especially on the extent of Budin & Co.'s knowledge with respect to C-K shares as compared to that found in the cited cases. It is also asserted that the number of Kiefaber's C-K shares traded by Budin & Co. was relatively small (27,800) in proportion to the total number of shares outstanding (5,000,000); no special commission was paid to Budin & Co. on its sales of Comstock shares; there is no evidence that Budin & Co. unduly concentrated pushing C-K shares over any other security, and there was no agreement between Budin & Co. and any alleged selling group.

The factors urged by the Respondents are not determinative of the issue here. There is no requirement that a respondent trade a specific number or percentage of shares in order to become subject to the provisions of Section 10(b) and Rule 10b-6.^{33/} If a respondent participates in a distribution, he cannot bid for or purchase such securities until he has completed his participation in the distribution. This mixed activity did occur here. The undersigned therefore concludes that the Respondents violated and aided and abetted violations of Section 10(b) of the Exchange Act and Rule 10b-6 thereunder, and that these violations were willful.

It is undisputed that in the course of the trading by Registrant in C-K stock no disclosure was made of the source from which a substantial majority of Registrant's C-K stock was obtained, the facts and circumstances

^{33/} See, Kennedy, Cabot & Co., Inc., Sec. Exch. Act Rel.No. 8817, p. 3 (1970).

under which those shares had been acquired, and the nature of the market being made by Registrant. This information was of vital importance to those with whom Budin & Co. was dealing and the failure to furnish it was violative of the anti-fraud provisions of the Securities Acts, chargeable to the Respondents as willful violations.

6. Failure of Supervision

It is alleged in the order for these proceedings that during the relevant period Registrant and Budin failed reasonably to supervise persons under their supervision with a view to preventing violations of the Securities Acts and rules and regulations thereunder, such persons having committed violations of said provisions as alleged in the order.

Budin, as chief officer of the Registrant, was in charge of all operations of the Registrant, including trading activity. He also was taking a full-time part in Registrant's trading activities. During the relevant period the firm was making a market in approximately 500 stocks and employing 6 to 8 traders. Budin, himself, handled 125 to 150 issues.

A broker-dealer has a general obligation to properly supervise employees to avoid violations of the Securities Acts.^{34/} This obligation also is imposed on supervisory personnel within the area of their supervision. Supervisors must be alert to avoid violations of the registration provisions of the Securities Act and the anti-fraud provisions of the Securities Acts.^{35/}

^{34/} L.A. Frances, Sec. Exch. Act Rel No. 9220, p. 5-6 (1971); Security Planners Associates, Sec. Exch. Act Rel. No. 9421, p.5 (1971).

^{35/} L.A. Frances, supra; D.H. Blair & Co., Sec. Exch. Act Rel. No. 8888, p. 7-8, 10 (1970); Dunhill Securities Corp., Sec. Exch. Act Rel. No. 9066, p. 4 (1971); Stone Summers & Company, Sec. Exch. Act Rel. No. 9839, p. 6 (1972).

Budin was the sole supervisory officer of the Registrant. Admittedly he had no time during regular trading hours to perform any supervisory duties. Budin testified that he commenced work two hours before the market opened and would continue working late into the evening and would review operations during that time and check transaction sheets. He further testified that before a stock could be traded he had to give his permission and the trader involved would have to advise Budin why he wanted to trade the stock, its price spread, the number of shares outstanding and whether other dealers were making a market in the stock. Budin further stated that he obtained this information on C-K directly from Freshman or a trader for P.N. McIntyre. He also knew Kiefaber and his connection with another brokerage firm with whom Budin & Co. had traded. All certificates turned in by Kiefaber were checked with the transfer agent, Budin pointed out.

Budin's testimony is at variance with that of Freshman as to general supervisory procedures. According to Freshman, he made his own decision on whether to trade a stock and would only refrain from doing so if another trader were already trading the stock. (Freshman was trading 75 to 80 stocks at the time). His only obligation, Freshman stated, was to stay within the funds allotted him for trading purposes.

The undersigned credits Freshman's testimony. In any event, even under the standards Budin set forth, it is clear that he was interested in trading information on a company and not the underlying information which would assist him in evaluating whether any Securities Acts violations would be involved in dealing with certain customers.

There is no evidence that Freshman had other than a free hand in dealing in C-K. At no time did Budin review his trades with him or question why a majority of the purchases of C-K were made with Kiefaber. None of the past history of C-K was reviewed. Under all the circumstances, the undersigned concludes that Budin failed reasonably to supervise as alleged in the order. Registrant is also responsible for this violation.

C. Activities of the Respondents with Respect to the Stock of XI Productions, Inc.

It is alleged in the order that the Registrant violated Section 5 of the Securities Act in the offer and sale of approximately 20,000 unregistered shares of XI Productions, Inc. The failure to supervise allegation in the order also applies to the sales activities in this stock by Registrant and its employees.

Approximately in March 1968 Mickey Rooney conceived the idea of forming a new corporation for the purpose of obtaining public financing for his ideas concerning stage, screen and television productions. Through a Robert Bryson, contact was made with Kachina Uranium Corp. On July 11, 1968, after negotiations had taken place, a final agreement was signed merging Barbroo Enterprises (which held Rooney's contract) with Kachina. By the terms of the merger agreement, Kachina, which at that time had approximately 1,000,000 shares outstanding, issued 4,600,000 shares of investment stock to Barbroo for the assets of Barbroo which included Rooney's service contract, various interests in residuals, Rooney's television shows and other literary properties.

Of the 4,600,000 shares issued by Kachina to Barbroo, 1,000,000 shares were transferred to a group including Robert Bryson for their efforts in locating and negotiating for Kachina. These included two certificates, issued on July 12, 1968, for 210,000 shares each and bore restrictive legends. On August 12, 1968, at a meeting of stockholders, the name of Kachina was changed to XI Productions, Inc. The two certificates, previously mentioned, were reissued as XI Productions certificates in Bryson's name on August 27, 1968. These certificates were reissued as one certificate in the name of Unico on September 16, 1968. Ultimately, on November 29, 1968, this certificate,

broken down into smaller denominations still in Unico's name, were transferred into certificates in the name of Edward Kiefaber.

The records of Budin & Co. show that on December 6, 1968, Budin & Co. purchased 20,000 shares of XI Productions from Kiefaber for \$20,000. These shares which originated from shares issued by XI Productions to Bryson were resold to others. No registration statement was filed with the Commission or was in effect with respect to these shares of XI Productions and the mails were used in connection with the above transactions.

Budin & Co. had been trading the stock of XI Productions since November 15, 1968 and continued to do so until May 1969. Trading was in substantial amounts, but no individual transaction approached 20,000 shares; the highest buy transaction being 5,000 shares and the highest sell transaction being 8,000 shares.

Bryson was part of the control group that took over control of Kochina. The subsequent changes in stock certificates issued to it, both in name and in denominations, all of which took place in a short time, were obviously steps taken to facilitate a distribution in violation of Section 5 of the Securities Act. Here, as in the case of C-K stock, Kiefaber cooperated with persons in the control group in helping to dispose of unregistered stock.

The Registrant, outside of a routine call to the transfer agent, made no searching inquiry into the circumstances under which Kiefaber obtained possession of the block of XI Productions stock. The prime interest of the Budin trader in this stock was to see whether he could dispose of the stock on the market. This was done even before the transaction with Kiefaber was technically completed. The XI Productions transaction came at the end

of the series of transactions Registrant had with Kiefaber in C-K stock. This was an additional basis for the exercise of caution in dealing with Kiefaber, but it did not have that effect. It is concluded that no basis for exemption for the offer and sale of this unregistered stock has been established and it is further found that Registrant willfully violated Section 5 of the Securities Act in the offer and sale of XI Productions, Inc. stock obtained from Kiefaber.

Budin knew of the negotiations between his trader and Kiefaber and had knowledge of the plan of this trader to sell Kiefaber's shares into the market before the actual purchase was made. He made no effort to intervene or insist that some further inquiries be made, other than a call to the transfer agent, before the transaction was closed. It is concluded that Budin failed reasonably to supervise to prevent this violation. Registrant was also responsible for this violation.

III. CONCLUDING FINDINGS, PUBLIC INTEREST

The Commission, pursuant to the provisions of Section 15(b)(5) of the Exchange Act, so far as it is material herein, is required to censure, suspend for a period not exceeding twelve months or to revoke the registration of any broker or dealer if it finds that such action is in the public interest and that such broker or dealer, subsequent to becoming such, has willfully violated any provision of the Exchange Act, the Securities Act, or any rule or regulation thereunder, or has failed reasonably to supervise, with a view to preventing violations of such statutes, rules, and regulations, another person who commits such a violation, if such other person is subject to his supervision. It also may, pursuant to the provisions of Section 15(b)(7) of the Exchange Act,

censure, bar, or suspend for a period not exceeding twelve months any person from being associated with a broker or dealer if it finds that such sanction is in the public interest and that such person has willfully violated any provisions of the Exchange Act, the Securities Act, or any rule or regulation thereunder. Furthermore, pursuant to Section 15A of the Exchange Act it may expel or suspend a member of a registered securities association who has violated any provision of the Securities Acts or rules and regulations thereunder.

It has been found that Philip S. Budin & Co., Inc., the Registrant, and Philip S. Budin, its president and the person in charge of its operations, willfully violated the registration provisions of the Securities Act, the anti-fraud provisions of the Securities Acts, and failed reasonably to supervise persons subject to their supervision with a view to preventing their participation in the violations found. These provisions are key provisions of the Securities Acts designed to protect investors and the public interest in the integrity of the securities markets. The Division urges that severe sanctions should be imposed on the Respondents.

The Respondents have been involved in prior administrative and Court proceedings. The Commission, on October 31, 1973, revoked the registration of the Registrant and barred Budin from association with any broker-dealer with the provision that after four months he could apply to the Commission for permission to become so associated in a non-supervisory capacity, subject to adequate supervision.^{36/} The decision was based on findings that during the period December 1967 to June 1968, the Respondents here violated the anti-fraud provisions of the Securities Acts by participating in or aiding and abetting in the execution of a scheme to manipulate

^{36/} Alessandrini & Co., Inc., et al., Sec. Exch. Act Rel. No. 10466. This decision is now on appeal.

the market in and establish an artificial market price for a stock so that it could be pledged as security for bank loans.

On July 13, 1973, the NASD, in a proceeding involving these Respondents, issued its Decision and Order of Acceptance of Offer of Settlement. The basis for the complaint against the Respondents was violation of net capital rules in 1969, 1970, and 1971 plus the filing with the Commission on or about March 20, 1971 of a computation of net capital and aggregate indebtedness which was inaccurate and misleading. The Registrant was expelled from membership in the NASD. Budin was suspended from association with any member in the capacity of a registered representative for six months (until 2/26/74), suspended as a principal from association with any member in a supervisory or managerial capacity for one year (until 8/27/74), and was suspended from association with any member in the capacity of a financial principal for five years (until 8/27/78).

On June 7, 1971, a receiver was appointed for Budin & Co. (see Litigation Rel. No. 5041 (June 11, 1971)). A preliminary injunction had previously been issued against the Respondents here for violation of the net capital rule.

Since the registration of the Registrant as a broker-dealer has been revoked and it has been barred from membership in the NASD no order from the undersigned with respect to Philip S. Budin & Co., Inc. by the undersigned is necessary. However, the findings of its further violations are noted for the record should there be an effort to have it return to the securities business.^{37/}

^{37/} Benjamin Werner, Sec. Exch. Act Rel. No. 9579 (April 24, 1972).

Budin's violations were serious. Prior violations by him buttress the conclusion that substantial sanctions are warranted. He has demonstrated an inability to properly exercise supervisory authority and it will be ordered that he be barred from acting in such a capacity. However, while there may be some doubt as to permitting him to continue in the securities business in any capacity, the undersigned has concluded that his violations are attributable primarily to his failure to exercise proper managerial and supervisory control of his brokerage business and that after a period of time he should be permitted to apply to the Commission for permission to be associated with a broker-dealer in a non-supervisory capacity. Accordingly,

IT IS ORDERED that Philip S. Budin is barred from association with any broker-dealer, provided that after six months he may apply to the Commission for permission to become so associated in a non-supervisory capacity, subject to adequate supervision.^{38/}

Pursuant to Rule 17(b) of the Commission's Rules of Practice a party may file a petition for Commission review of this initial decision within fifteen days after service thereof on him. This initial decision pursuant to Rule 17(f) shall become the final decision of the Commission as to each party unless he files a petition for review pursuant to Rule 17(b) or the Commission, pursuant to Rule 17(c), determines on its on its own initiative to review this initial decision as to

^{38/} This four months period shall be in addition to the period specified in the prior order of the Commission (Sec. Exch. Act Rel. No. 10466, October 31, 1973).

him. If a party timely files a petition to review or the Commission takes action to review as to a party, this initial decision shall not become final as to that party.^{39/}

Sidney L. Feiler

Sidney L. Feiler
Administrative Law Judge

Washington, D.C.
February 22, 1974

^{39/} All contentions and proposed findings and conclusions have been carefully considered. This initial decision incorporates those which have been accepted and found necessary for incorporation therein.