ADMINISTRATIVE PROCEEDING
FILE NO. 3-6700

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of

ARTHUR JAMES HUFF

INITIAL DECISION

December 15, 1987
Washington, D.C.

David J. Markun
Administrative Law Judge

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APPEARANCES: Charles C. Harper, Natalie Anne Aizpuru, and Susan B. Reinert, Esqs., Miami, Florida, for the Division of Enforcement.

Martin P. Unger, Christopher E. O'Brien, and Ann Parry, Esqs., of GASTON, SNOW BEEKMAN & BOGUE, New York, New York, for the Respondent.

BEFORE: David J. Markun, Administrative Law Judge.

I. THE PROCEEDING

This public administrative proceeding was instituted by an order of the Commission dated August 12, 1986 ("Order") pursuant to Sections 15(b) and 19(h) of the Securities Exchange Act of 1934 ("Exchange Act") (15 U.S.C. §§78o(b), 78s(h)), naming Philip Huber ("Huber"), Robert D. Punch ("Punch"), and Arthur James Huff ("Huff") as respondents.

The Order contained allegations of the Division of Enforcement ("Division") that Huber, Punch, and Huff failed reasonably to supervise Dennis E. Greenman ("Greenman"), a person alleged to be subject to their supervision, during the period July 1979 to May 1980 (the "relevant period"), within the meaning of Sections 15(b)(4)(E) and 15(b)(6) of the Exchange Act (15 U.S.C. §§78o(b)(4)(E), 78o(b)(6)), with a view to preventing Greenman's alleged violations of Section 17(a) of the Securities Act of 1933 ("Securities Act"), and of Section 10(b) of the Exchange Act and Rule 10b-5 thereunder.

The Order further alleged that Punch and Huff failed reasonably to supervise Huber, a person alleged to be subject to their supervision, within the meaning of Sections 15(b)(4)(E) and 15(b)(6) of the Exchange Act, in that Huber, as alleged, violated Section 15(b)(4)(E) of the Exchange Act by failing reasonably to supervise Greenman with a view to preventing Greenman's alleged violations.

The Order directed the holding of a hearing to determine whether the Division's allegations were true, to afford respondents the opportunity to establish any defenses, and to determine what, if any, remedial sanctions were appropriate in the public interest. Huber and Punch submitted offers of settlement that the Commission accepted simultaneously with the institution of proceedings,[1/] leaving Huff as the only remaining respondent.

A nine-day evidentiary hearing was held in February, 1987, in Miami, Florida and New York, New York. The parties have filed proposed findings of fact and conclusions of law and supporting briefs pursuant to the Commission's Rules of Practice.[2/] In addition, a statement of views has been received under the Commission's Rule 9(f)[3/] from the Compliance and Legal Division of the Securities Industry Association, together with the Division's response thereto.

1/ Pursuant to their Offers of Settlement, the Commission entered an Order Making Findings and Imposing Remedial Sanctions that barred Huber from association with any broker, dealer or municipal securities broker or dealer in a supervisory or managerial capacity; suspended Huber from association with any broker, dealer or municipal securities broker or dealer for 60 days, censured Punch; and suspended Punch from association with any broker, dealer, or municipal securities broker or dealer in a supervisory or managerial capacity, for 180 days.

2/ 17 CFR §201.16.

3/ 17 CFR §201.9(f).

The findings and conclusions herein are based upon the record and upon the demeanor of the various witnesses. The standard of proof applied is that requiring proof by a preponderance of the evidence. [4/]

II. FINDINGS OF FACT AND CONCLUSIONS OF LAW

A. The Respondent; the Relevant Period.

Respondent Huff has been employed by PaineWebber, Incorporated ("PaineWebber"), a broker-dealer registered with the Commission, in its New York headquarters office, since about mid July, 1979, as a vice president and as the Senior registered options principal ("SROP" or "Senior ROP") in PaineWebber's compliance department.

The "relevant period", i.e. the period during which Huff is charged with having failed reasonably to supervise Greenman and Huber, commences with mid July 1979, when Huff began his employment with PaineWebber, and runs to July 1980, when Greenman's employment with PaineWebber terminated.

B. Other PaineWebber Personnel Whose Conduct or Activities, Among Others, are Relevant to the Charges Against Huff.

Greenman was a registered representative in the Miami, Florida branch office of PaineWebber from September 1978 and throughout the relevant period to May 8, 1980.

4/ Steadman v. S.E.C., 450 U.S. 91, 101 S.Ct. 999 (1981).

Huber was the branch manager of PaineWebber's Miami, Florida branch office and a registered options principal ("ROP") from about September 1977 to December 1982. Huber was Greenman's immediate supervisor during the relevant period.

Punch was a regional manager of PaineWebber with supervisory responsibilities for various branch offices from about November 1977 to March 1982. Punch was Huber's immediate supervisor during the relevant period.

Ray Vass ("Vass") was a vice-president and the director of PaineWebber's compliance department from November 1977 to November 1981. Vass was Huff's immediate supervisor during the relevant period.

Vass reported to the General Counsel, Sam Scott Miller ("Miller"), who in turn reported directly to the chairman of the board. Miller headed up both the legal department and the compliance department of PaineWebber which, though separate departments, worked closely together on many issues. Among those in the legal department with whom Vass and others in the compliance department had occasion to work closely was Timothy E. Longworth ("Longworth"), who directed the portion of the legal department having to do with litigation, arbitration, and disputes between PaineWebber and its customers.

Vass's deputy director of compliance was Jane Larkin ("Larkin"). George Warner ("Warner"), Vass's assistant, and

William Dorman ("Dorman"), with specific responsibilities in compliance, also reported at various times directly to Vass.

Marvin Lippsett ("Lippsett") was employed as PaineWebber's "designated registered options principal" from November 1977 to March 1980, at which time, when Rule 9.8 of the CBOE was amended, his position designation was changed to "compliance registered options principal" ("CROP" or "Compliance ROP"). Respondent Huff was Lippsett's immediate supervisor during the relevant period.

Bruce Paine ("Paine") was Huff's predecessor as Senior ROP at PaineWebber.

C. Greenman's Fraudulent Violations.

The record establishes that Greenman, while employed as a registered representative at PaineWebber's branch office in Miami, Florida, from September 1978 to about May 8, 1980, conducted a massive securities fraud that violated Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and 18 U.S.C. §2314. 5/

When he commenced employment with PaineWebber, Greenman took with him only the 10 to 12 accounts that he had had with his prior employer, Merrill Lynch, that had been participating

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5/ Greenman commenced his fraudulent conduct while employed at Merrill Lynch just before joining PaineWebber and continued it after leaving PaineWebber for employment at Barclay Financial Corporation.

in Greenman's "special arbitrage program", which program continued to be called that for a time while Greenman was employed at PaineWebber and later came to be called a "short term trading program." Greenman described his arbitrage and short term trading programs as involving buying on one exchange and selling a like instrument on another exchange in order to take advantage of price disparities.

Greenman's trading in his customer accounts at Paine-Webber was in fact "discretionary" in that he, Greenman, not the customers, made the trading decisions, but Greenman never obtained written authority from his customers for discretionary trading. During the relevant period Greenman traded primarily in options in the accounts that were a part of his short term trading program; he did not obtain from his customers authorization for the trades made nor did he advise them of the actual trades made in their accounts.

Greenman's trading at PaineWebber during the relevant period was in the main and on balance unprofitable. In order to conceal losses from his customers and in furtherance of his overall fraud, Greenman intercepted his customers' real, or genuine, PaineWebber account statements and sent fictitious account statements to the customers.

The genuine account statments were sent to fictitious addresses, including post office boxes controlled by Greenman,

incorrect street addresses, and non-existent street adresses.

Greenman sent his customers two kinds of fictitious statements. Some customers received fictitious statements showing fictitious trades. Other customers received fictitious statements showing purported distributions resulting from Greenman's trading program under the heading "capital distribution reinvested" rather than showing the results of purported individual trades.

To aid him in carrying out his scheme, Greenman leased time on a computer away from PaineWebber, where he prepared the fictitious account statements on forms that were duplicates of authentic PaineWebber statements.

The fictitious statements generally showed purported monthly rates of return of 5 to 7 percent.

For some of his customers, Greenman chose never to open up accounts for them, depositing their invested funds instead into other customer accounts at PaineWebber that were participating in Greenman's purported short term trading program.

At the end of the relevant period, when Greenman left PaineWebber, he had some 200 to 250 customers in his short term trading program, and approximately 20 to 25 customer accounts on PaineWebber's books. Greenman's customers had from $10 to $15 million invested in the short term trading

program. During the relevant period, Greenman's customers sustained losses of over $7.6 million.

These losses stemming from Greenman's fraud during the relevant period were undisclosed and unknown to Greenman's customers during the relevant period, and the losses and the fraud did not become known to the customers until considerably later, after Greenman terminated his employment with PaineWebber and became employed by a different broker, taking the subject accounts and his ongoing fraud respecting them with him.[6/]

D. Huber's Failure Properly To Supervise Greenman.

The parties are in agreement that Huber, as branch manager of PaineWebber's Miami office, was Greenman's immediate supervisor and that, as such, Huber was obligated "reasonably to supervise" Greenman with a view to preventing violations by Greenman of various specified statutes and regulations,

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6/ On December 3, 1981, Greenman pled guilty in the United States District Court for the Middle District of Florida, Tampa Division, to a one count Information charging him with interstate transportation of property on or about August 4, 1980 in furtherance of a scheme to defraud in violation of Title 18 of the U.S. Code, Section 2314. The Information alleged that Greenman devised a scheme to defraud and, among other things: 1) created a "short term trading program" and represented to investors that the program would return large profits; 2) created bogus account statements reflecting large profits; and 3) intercepted genuine trading account statements before investors could see them. Greenman was sentenced to ten years in federal prison and fined $10,000.

within the meaning of Sections 15(b)(4)(E) and 15(b)(6) of the Exchange Act, during the relevant period. 7/

The parties are also in agreement on the point, which is amply supported by decisions of the Commission and of the Courts, that a branch manager is the first line of defense when it comes to supervision of registered representatives and endeavoring to assure their compliance with applicable laws and regulations.

Huber's supervisory duties included checking order tickets, commission runs, and customer statements, responding to written communications from clients, and approving new account forms.

Huber was a registered options principal ("ROP") during the time he was the branch manager of the Miami office. This was in conformity with PaineWebber's decision to have all of its branch managers specially qualified as ROPs, in recognition of the emphasis that the Commission and self-regulatory exchanges and other organizations involved with options trading

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7/ Although ultimately Huber's failure reasonably to supervise Greenman is relevant in the context of this proceeding only to the extent that it occurred within the previously defined "relevant period", i.e. while Greenman and Huff were both employed at PaineWebber, nevertheless what Huber learned about Greenman's options trading program prior to the relevant period has a bearing on the nature of the supervision of Greenman that might reasonably have been expected of Huber during the relevant period.

had placed upon the need for specially qualified personnel to supervise trading for public customers in the highly sensitive options product. As an ROP, Huber was responsible for supervising the registered representatives in his office who traded options with a view to assuring that they complied with the policies and procedures of the firm and of the various exchanges on which options were traded. Huber was also responsible for reviewing the objectives and suitability of clients who wanted to trade in options.

Huber understood that when he had compliance problems, he was free to contact the compliance or legal departments in New York directly, rather than his immediate line supervisor, Punch. Indeed, Huber testified that given the number of branches Punch supervised, it would have been impossible for him as a practical matter to entertain all of the day to day administrative and compliance problems that would arise in the various branches.

The record discloses a number of respects in which Huber failed reasonably to supervise Greenman in that he failed to follow various PaineWebber practices and procedures that were designed to increase the likelihood of uncovering fraud of the kind that Greenman perpetrated.

During the period Greenman was at PaineWebber, Paine-Webber's Standard Practices and Procedures Manual provided,

in part, with regard to addresses on customer accounts, that: "[w]herever possible, the permanent residence or business address must be used. A post office box number or hotel address is not acceptable unless it is the best address obtainable for the client." Huber was aware of this procedure.

Huber received in regular course a copy of a memorandum dated May 24, 1987, from "Legal/Compliance" to Punch listing various customer accounts for which Greenman was the registered representative with similar mailing addresses. The memorandum listed 36 of Greenman's accounts that had a mailing address identical or similar to that of another account. Of the accounts listed, 20 had post office box numbers as mailing addresses.

Huber obtained a handwritten explanation from Greenman for the similar mailing adresses of the various accounts listed in the memorandum from Legal/Compliance. However, Huber did not do anything to verify independently any of Greenman's explanations for the similar addresses on his customer accounts either then or later, when additional information raising questions about Greenman's options trading program came to Huber's attention.

Greenman's explanations for the similar mailing addresses were in fact essentially false. The post office box numbers listed as mailing addresses for 20 of Greenman's

customer accounts were post office boxes controlled by Greenman. One of the street addresses for 8 of Greenman's customer accounts was the location of a retail store owned by one of Greenman's friends.

Greenman's written explanation for the similar mailing addresses on his customer accounts was forwarded to the compliance department in New York.

On May 24, 1979, Huber sent a wire to Vass and Punch which stated:

> Re Dennis Greenman
> Similarity of accounts that will jump out at me don't waste your time sending list I reviewed statements with Dennis. Acct [sic] same PO Box numbers are Accts [sic] that either work for the same firm or are indemnified by Demery.

Huber's responses were based entirely on Greenman's explanation, with no effort on Huber's part at independent verification.

During the period Greenman was at PaineWebber, PaineWebber's Branch Office Manager's Manual provided, in part, with regard to deliveries of checks drawn on customer accounts, that:

> Deliveries of checks to clients by stockbrokers should be permitted only under extraordinary circumstances. Deliveries by stockbrokers require prior approval of the branch office manager who must confirm the deliveries in writing to the client on the day delivery is made.

In violation of that provision, Huber permitted Greenman to hand-deliver customer checks on a regular basis. No other registered representative in the Miami office hand-delivered customer checks on a regular basis.

Moreover, Huber did not confirm with Greenman's clients the hand-delivery of customer checks by Greenman, as the PaineWebber Manual required.

Further, during the same period, Huber did not follow the recommendation of PaineWebber's internal auditor that there be maintained a log book in the Miami office recording the hand-delivery of checks by stockbrokers.

During the period Greenman was at PaineWebber, PaineWebber's procedures required branch managers to initial big option orders before they were entered by the broker. Orders of 50 or more options were considered big option orders.

Greenman routinely entered big option orders at PaineWebber under Huber's "blanket authority," and Huber did not initial each option order before it was entered by Greenman, all in contravention of PaineWebber's procedures.

During the period Greenman was at PaineWebber, PaineWebber's Branch Office Manager's Manual provided, in part, with regard to incoming mail, that:

> All incoming mail must be opened, time stamped and screened in the operations department by a member of the management staff before it is

> distributed in the office. The review of incoming mail cannot be assigned to any member of the staff other than a manager or assistant manager. It is a serious violation of New York Stock Exchange Rules and firm policy to assign this function to a member of the secretarial or clerical staff. . . All checks and securities received should be routed directly to the cashier.

In contravention of this established requirement, Huber allowed Greenman to open his own mail during the period mentioned.

During the period Greenman was at PaineWebber, PaineWebber's Branch Office Manager's Manual provided, in part, regarding active accounts, that:

> Active accounts should be subject to a special review which would include a conversation with the client, discussing with him the frequency of trades and establishing that the account is being operated by him in this manner on his own initiative and in accordance with his instructions. This discussion should also establish that he is aware of the substantial commissions derived by us as a result of his trading. A letter from the client confirming this should also be obtained...

Huber considered Greenman's customer accounts to be active accounts, and the record confirms this belief.

PaineWebber had a form letter which was to be used as a guideline when drafting activity letters for options accounts. The form letter suggests that it should be signed by the branch manager.

Activity letters were mailed to Greenman's customers on only two occasions during the mentioned period. In both instances Huber allowed Greenman to sign the activity letters mailed to Greenman's customers.

Greenman mailed the first set of activity letters to his customers in February 1979. When the letters were returned by the customers, Greenman destroyed them, prepared a new set on which he entered fabricated figures for the principal amounts invested and the profits for 1978, forged his customers' signatures on those letters, gave the forged letters to Huber, who thereafter forwarded the activity letters that were purportedly filled in by Greenman's customers to Vass in New York.

Huber received only 9 out of the 12 activity letters that were purportedly sent to Greenman's customers. Huber did not contact the customers who apparently failed to respond. Such contacts by Huber were particularly called for here since Huber had allowed Greenman to send out the letters himself rather than following the suggested practice of having the branch manager send them out.

In December 1979, Greenman prepared another set of activity letters on which he again forged his customers' signatures.

The December (form) activity letters requested the

customer to fill in the approximate principal invested in 1979 and the approximate profit or loss for 1979. Greenman filled in fictitious amounts, sometimes showing trading profits when the customers' accounts had in fact lost money.

Greenman gave the fictitious December activity letters to Huber, who made no effort at comparison with the customers' actual account results or at other means of independent verification, even though several months earlier Huber had been made aware that some of Greenman's customers had experienced large trading losses.

The record also discloses a number of documents generated by PaineWebber's compliance department and its internal audit staff that came to Huber's attention and that should have alerted Huber to the need for taking a closer, deeper, and more thorough look at Greenman's short term options trading program and for taking steps to obtain independent verification of what Greenman was telling him rather than relying solely upon Greenman's statements, as well as for exercising closer supervision over Greenman generally and making a more penetrating inquiry into the problems. Regrettably, these red flags did not have the effects on Huber they should have had.

Thus, Huber in April 1979 received a copy of a memorandum dated April 23, 1979 from Vass to Punch concerning Greenman, including a double-spaced, four page attachment thereto.

Vass stated in the memo in part that:

> (W)e have a number of concerns about Dennis Greenman's options trading system, the fact that a number of his clients have sustained very substantial losses over the past several months, and some disturbing indications which we continue to get from various sources as to the manner of his solicitation of new customer accounts. [Ex. 32, p. 1] 8/

According to Huber, the disturbing indications were that a couple of people reported that significant returns were being generated from Greenman's trading program, including one report that the customer was getting or knew of people who got a seventy percent return.

The memorandum described various contacts PaineWebber had received from outside persons who had spoken with Greenman or someone who claimed to be working with Greenman.

The persons who contacted PaineWebber reported that Greenman or someone who claimed to be working with Greenman made representations that:

- Greenman had a special options arbitrage program that was sponsored by PaineWebber;
- Greenman was the only one in the State of

8/ Because the memorandum with its attachment, constituting Exhibit 32 in this proceeding, is relevant not only to the point immediately under discussion but to other portions of this decision as well, the entire text of Exhibit 32 is attached hereto as "Attachment A."

Florida who was authorized to provide a program of this kind;

- An investor could not possibly lose money if he invested in this type of program; and
- The minimum investment would be $10,000 and one could earn 75 percent of his money in a short period of time.

The attachment to the memorandum recommended that ". . . Greenman's activities be very closely supervised by the branch manager and that periodic contact be made with the clients concerning their accounts."

Huber did not contact any of Greenman's clients as a result of receiving Vass's memorandum, nor did the sorry level of Huber's supervisory vigilance improve.

In late June 1979 the Miami branch office was examined by a PaineWebber internal auditor, and Huber received a copy of the Audit Report dated August 24, 1979.

The report indicated that the auditor reviewed the new account documentation for Greenman's active options accounts.

The report noted that the new account documentation for Greenman's customer accounts disclosed an unusual number of accounts with H. Preston Demery as a partner.

The auditor recommended in the report that:

> . . . new account information with regard to all related H. Preston Demery accounts should

> be verified with respect to name, addresses (note all addresses are P.O. box numbers) and references. Personal contact with each general partner (other than H.P. Demery) would provide additional evidence of meeting the requirements of N.Y.S.E. Rule 405 'know your customer'.

Huber understood that the recommendation regarding making personal contact with each general partner applied to him, but he failed to follow this recommendation.

The auditor recommended in the report that "[n]ew accounts information should be verified to ensure full compliance with N.Y.S.E. Rule 405."

Huber understood that Rule 405 is the "Know Your Customer" rule and involves a question of whether the investments are suitable for the customer.

Following the auditor's recommendation, Huber received partnership agreements from the limited partnerships; however, Huber did not ascertain who the limited partners were in the various limited partnerships.

In June 1979, Greenman and Huber went to New York to meet with personnel from PaineWebber's compliance department.

The purpose of the June 1979 meeting was to try to resolve a number of concerns the compliance department had with Greenman's trading activities.

Huber testified he believed that all issues with respect to Greenman had been resolved at the June 1979 meeting, but

given Huber's knowledge of his faulty supervision of Greenman, his awareness of facts that called for a searching inquiry, and his knowledge that no one at PaineWebber had conducted such an inquiry, he had no reasonable basis for believing the "problems" with Greenman's options trading program had been "resolved".

The record discloses that Huber had incidental contacts with a few of Greenman's customers, but that he failed to take advantage of those contacts to make the kind of inquiry into Greenman's options trading program that the situation called for.

Thus, after Huber had been contacted by W.W. Gay ("Gay"), a customer of Greenman's in the short term options program, Huber told Greenman that the customer was complaining that he was making too much money in his account with Greenman. Greenman indicated to Huber that there was nothing he could do about that, after which Huber told Gay that everthing was okay.

Another of Greenman's customers who contacted Huber with questions about his account was Downing Nightingale ("Nightingale"), a Jackson, Florida, resident who invested in Greenman's short term trading program through a limited partnership.

Nightingale had obtained a copy of the fictitious account statement prepared by Greenman for his limited partnership.

Nightingale telephoned Huber and told him he had a copy of the account statement for his limited partnership for the previous month, and asked Huber to explain the line item on the statement: "Capital Distribution Reinvested."

While Nightingale was on the phone, Huber reviewed PaineWebber's copy of the genuine account statement for the limited partnership. Huber asked Nightingale to read the account statement for the limited partnership to him. Huber thus learned that his copy of the account statement for the limited partnership was different from Nightingale's copy in that Nightingale's statement had a line item entitled "Capital Distribution Reinvested" whereas Huber's (genuine) statement did not show that line item.

Huber asked Nightingale to send a copy of his account statement to PaineWebber's Miami office.

Huber related his conversation with Nightingale to Greenman, who told Huber that the partnership must have superimposed its distribution statement to the limited partners on the PaineWebber statement.

The record shows that Greenman thereafter called the general partner in Nightingale's limited partnership and persuaded him to convince Nightingale not to send his account statement to PaineWebber, with the result that Nightingale never did send a copy of the account statement for his limited partnership to PaineWebber.

Huber did not inquire further of Greenman or Nightingale about the discrepancy in the two account statements.

A third customer in Greenman's short term trading program with whom Huber had contact was H.P. Demery ("Demery"), of Jacksonville, Florida. Demery was a particularly significant investor in that he "guaranteed" various other investors in the program who participated in the limited partnerships against loss of their investments in return for a share of the profits realized.

After Greenman arranged for Huber to meet Demery, Greenman and Huber went to Jacksonville where they visited with Demery for four or five hours. During that period Huber failed to discuss with Demery the customer's account at PaineWebber. Nor does the record show that Huber ever thereafter discussed with Demery his participation in Greenman's short term options trading program even though Huber had abundant indications that Demery was a key investor in the program.

One period during which Huber failed completely to exercise reasonable supervision over Greenman occurred in the summer of 1979.

Greenman spent approximately eight weeks during that summer at a cottage in Monroe, New York. Greenman continued trading in his normal manner while in Monroe, New York. He

had a WATS line set up so that his customers in Florida could call him there. He had another line set up to contact PaineWebber's trading department in New York.

Huber did not supervise Greenman during the two months Greenman was in Monroe, New York. Greenman only spoke with Huber once or twice during the entire summer and those conversations took place while Greenman was in Miami.

A final, and very serious, failure in Huber's pattern of failing reasonably to supervise Greenman during the relevant period occurred in May 1980, when Greenman left PaineWebber and went to work for Barclay Financial Corp. ("Barclay")[9/], another broker-dealer. Before leaving PaineWebber, Greenman liquidated all open positions in his customers' accounts and PaineWebber issued checks payable to his customers.

Huber gave Greenman permission to hand-deliver the checks to his customers in contravention of PaineWebber procedures. This enabled Greenman to carry over his fraudulent program to his new employment. Instead of delivering the checks, Greenman forged his customers' endorsements and deposited most of the checks into an account he opened at Royal Trust Bank in the name of A.G. Becker, Inc. ("A.G. Becker").[10/] The other

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9/ Barclay's name was later changed to Capital Brokerage Services, Inc.

10/ A.G. Becker was the clearing broker for Barclay.

checks were deposited into Greenman's personal account at Royal Trust Bank.

The checks deposited into the A.G. Becker account at Royal Trust Bank totalled approximately $3.4 million. The checks deposited into Greenman's personal account at Royal Trust Bank totalled approximately $75,900. As already noted, Greenman continued to operate his fraudulent purported "short term trading program" at Barclay.

Huber's compensation was based upon the profits from his branch office. The volume of commissions generated by the brokers in his office was one of the factors that determined the profitability of his office.

Greenman was the biggest "producer" in the Miami branch. In 1979 Greenman produced over $612,000 in commissions and was ranked nationally by PaineWebber as its fifth largest producer of commissions. The record strongly suggests that these were significant factors accounting for Huber's failure reasonably to supervise Greenman during the relevant period. But whatever the reason, the record establishes clearly that there was such a failure.

E. Huff's Failure Properly to Supervise Huber and Greenman.

Huff had worked in the options area of the securities brokerage business for some ten years before joining

PaineWebber. That prior employment included employment by various broker-dealers in the options areas (1970-1974), and positions with the Chicago Board Options Exchange, Inc. ("CBOE") as a compliance examiner, and, later, director of the CBOE's New York office (1974 - July 1979).

When Huff left the CBOE in about mid July, 1979, he joined PaineWebber in its headquarters office in New York, N.Y., as a vice president in its compliance department and as Senior ROP.

PaineWebber did not have a written position description setting forth Huff's responsibilities as SROP. His duties were defined and governed, subject to elaboration by his superiors, by the rules of the self-regulatory organizations ("SRO"s) that have adopted rules governing their members' conduct with respect to public (non-member) customer transactions in options. The rules of the various SRO's as pertinent here are not materially different from those of the CBOE.

The pertinent CBOE rule in effect when Huff began his employment at PaineWebber was Rule 9.8 as amended January 26, 1977, which provided:

> "Every member firm shall provide for the supervision by a Senior Registered Options Principal who is specifically identified to the Exchange, and who is an executive officer or general partner of the member organization, of all of its non-member customer accounts

> and all orders in such accounts, insofar as such accounts and orders relate to options contracts."

Interpretation and Policy .01 under Rule 9.8 provided as follows:

> "The Senior Registered Options Principal, in meeting his responsibility for supervision of non-member customers' accounts and orders, may delegate to qualified employees responsibility and authority for supervision and control of each branch office handling options transactions, provided that the Senior Registered Options Principal shall have overall authority and responsibility for establishing appropriate procedures of supervision and control over such employee."

This version of Rule 9.8 remained in effect until April 25, 1980, shortly before Greenman left PaineWebber. Effective April 25, 1980, the Rule was amended as a result of the Special Options Study to provide, in a new Rule 9.8(a):

> "Duty to Supervise; Senior Registered Options Principal. Every member organization shall develop and implement a written program for the review of the organization's non-member customer accounts and all orders in such accounts, insofar as such accounts and orders relate to option contracts. This program shall be under the supervision of a designated Senior Registered Options Principal who is specifically identified to the Exchange and who is an officer (in the case of a corporation) or general partner (in the case of a partnership) of the member organization."

Interpretation and Policy .01 was not changed.

In March 1980 an educational handbook entitled "Handling Options Transactions for Public Customers" ("the handbook")

was jointly prepared by seven SROs that have adopted rules governing their members' conduct with respect to public options trading.

The material contained in the handbook does not constitute the official rules of any SRO but was written as a jointly-formulated guide for member firms to assist them in complying with applicable rules with respect to their public customers' options business.

The handbook states in part that "[t]he SROP has overall authority and responsibility for supervision of all non-member customer option accounts and related options transactions."

The handbook cites examples of particular matters that are the direct responsibility of the SROP, including, among others, that he:

a) supervise all options transactions of customers;

b) administer program for supervisory review of selected options accounts; and

c) assist branch office managers in supervising customer options activities.

The handbook further states:

> [i]n meeting his supervisory responsibilities, the SROP may delegate the duty to review the options activities of branch offices within the firm to employees (generally ROP-qualified) under his direct control. Such delegation does not relieve the SROP of his responsibility for overall supervision and control over the firm's options activities.

Following the above section is a direct reference to CBOE Rule 9.8(a).

Huff received a copy of a November 9, 1979 memorandum from Vass that had direct bearing on industry construction of Rule 9.8/9.8(a). The memorandum reported that Vass had attended a meeting of the self-regulatory organizations on November 7, 1979, at which representatives of the SROs had discussed the language contained in an October 1, 1979 draft of the handbook. In his memorandum, Vass reported upon some of the discussion at the meeting, and quoted several passages from the draft handbook. Vass's memorandum stated in part:

> In Chapter I, item C of the handbook the SROP is described as being "responsible for overall supervision of all his firm's options activity on behalf of customers..."
>
> In Chapter I, item B the handbook states 'in meeting his supervisory responsibilities, the Senior ROP may delegate the duty to employees (generally ROP qualified) under his direct control.' The handbook then goes on to state 'such delegation does not relieve the Senior ROP of his responsibility for overall supervision and control over the firm's options activities.'

Vass expected the SROP to guide the activities of the compliance department which related to the options business; Vass considered Huff more expert in the options area than he (Vass) was.

Huff understood that he had, among others, the following duties and responsibilities as SROP during the relevant period:

- to develop and implement policies regarding options activity within PaineWebber.
- to follow through on options situations where there were appearances of a concern or problem.
- to set up compliance guidelines.
- to review the activity in options accounts on a selected basis.
- to investigate any options-related problems or complaints that were brought to his attention.
- to have in place supervisory procedures for the review of large and active options accounts.
- to assist branch managers in supervising customers' options activities where certain situations were brought to his attention by branch managers or otherwise came to his attention.

Within the relevant period Huff became aware of numerous, various, and significant "red flags" that should have alerted him to the need for further, and more diligent and searching inquiry into the circumstances surrounding operation of Greenman's options trading program.

Firstly, shortly after Huff came aboard at PaineWebber, Vass, Huff's immediate supervisor and the director of the compliance department, handed Huff a one-to-two inch thick file that had been developed with respect to Greenman and his

options trading program. The file contained memos, documents, etc., including handwritten notes by PaineWebber compliance and other personnel. Vass instructed Huff to keep on top of Greenman's activities and to follow through if a question arose concerning Greenman. Huff familiarized himself with the Greenman "compliance" file, which was added to from time to time and remained accessible to Huff throughout the relevant period.

One of the items Huff reviewed and had available to him concerning Greenman was a memorandum dated March 13, 1979, directed to Vass and Dalton, that had been prepared by Bruce Paine, Huff's predecessor as SROP, on the subject "Dennis Greenman's Trading Program - Options" ("the Paine Memorandum"). Paine's description of Greenman's short term options trading program was based entirely upon Greenman's statements to him. The record indicates that in reality Greenman did not trade options for his customers in accordance with the methods and limitations (e.g. placing all but 15-20% of a customer's hypothetical $100,000 deposit in money market funds) described in the Paine Memorandum. The record further establishes that at no time during the relevant period did Huff attempt to obtain independent verification of the information in the Paine Memorandum even after various red flags had come to Huff's

notice and attention that should have alerted him to the need for a deeper, more searching inquiry.

At about the time Huff joined PaineWebber, he received a copy of a memorandum dated July 12, 1979, from Vass to Punch concerning Greenman. 11/ The memorandum reported that a former CBOE chairman, Leo Pomerance, had advised that "people were going around talking about 70 percent returns and an option arbitrage program." Vass's memorandum continued, "[t]his is clearly our man Greenman or possibly some of his clients who have themselves been promoting his abilities as an options expert." In the memorandum, Vass reported that he had urged both Huber and Greenman to be diligent in order to be able to demonstrate proper business practices, documentation and supervision. Vass related that he was convinced that Greenman and Huber should be prepared for close regulatory scrutiny. Vass concluded his memorandum with the following blunt admonition:

> I am reaching the end of my patience with receiving reports of the nature of that from Pomerance. I do not know if these quoted percentage returns and the use of the word 'arbitrage' is originating with Greenman or his clients .... In any event, Greenman (and his clients) must either be controlled or Greenman must be terminated.

11/ Because the memorandum, Exh. 14 in this proceeding, is relevant to a number of points discussed herein, it is attached hereto as "Attachment B".

Although Vass's memorandum concerned Greenman's options activities, Huff never spoke to Huber, Punch or even Greenman, about the reported representations of 70 percent returns on Greenman's trading program, either then or at any subsequent time during the relevant period after Huff had become aware of further "red flags" calling for searching inquiry.

And, of course, this memorandum gave Huff notice very early during the relevant period that Greenman's options trading program was one that was creating special problems that had already taxed the patience of the director of compliance and that called for close supervision and surveillance by all concerned.

Given all the memoranda in the Greenman compliance file and the amount of activity in Greenman's customer accounts, Huff considered it appropriate to review Greenman's customer accounts more frequently than other brokers' customer accounts. By mid September 1979, Huff had become quite familiar with Greenman's accounts and the activity therein. Vass had, as already noted, instructed Huff to keep on top of Greenman's activities, and to follow through if a question arose concerning Greenman's accounts. Huff had reviewed the Greenman file and other correspondence relating to Greenman that had come to his attention. In addition, Huff was reviewing, on a random basis, monthly account statements for

Greenman's customers and computer printouts showing the activity in Greenman's customer accounts. Huff was also reviewing PaineWebber's "top forty" listings.

Huff received a copy of a memorandum from Vass to A.L. Meentemeier, director of Internal Audit at PaineWebber, dated September 11, 1979, concerning Greenman.[12/] The memo was in response to an inquiry from internal audit regarding Greenman's option accounts. Vass noted in his memorandum that "[t]he Compliance Department has been very much involved for an extended period of time with Mr. Greenman and his option accounts" and "Mr. Greenman tends to have large accounts which trade actively in the options market." Vass stated in part in his memorandum:

> Our Senior ROP Jim Huff and our Compliance ROP Marvin Lippsett are both quite familiar with Greenman's accounts and his activity. They observe daily listings of large positions and frequently observe Greenman's accounts in this regard. In addition, they are reviewing the monthly statements for Greenman's accounts.

Vass's memo to Meentemeier served as further notice to Huff that Greenman's options trading program required special attention, inquiry and surveillance.

On or about October 8, 1979, Dorman, Vass's assistant,

12/ Because the memorandum, Exh. 18 in this proceeding, is relevant to a number of points treated herein, it is attached hereto as "Attachment C".

sent Huff a copy of portions of a PaineWebber internal audit report of the Miami office, which related to Greenman's options trading program. The audit report was dated August 24, 1979, and had been conducted in late June. (See pp. 19-20 above). In the portions of the report furnished to Huff, the auditor recommended that all new account information for the H.P. Demery accounts serviced by Greenman should be verified with respect to names, addresses, and references. The auditor included a list of the names and addresses of the limited partnership accounts involving Demery. Each of those accounts had a post office box designation as the address.

Huff did not attempt to verify the account information for the Demery accounts, nor did he request Huber, or anyone else, to do so. Although PaineWebber's internal procedures required use of a permanent residence or business address whenever possible, as already noted, Huff did not attempt to obtain the home or business address for any of the Demery accounts, nor did he request Huber, or anyone else, to do so. Further, Huff did not contact any of Greenman's customers in order to verify that the account addresses were correct nor did he request Huber or anyone else to do so.

The internal auditor had suggested that personal contact be made with each general partner (other than H.P. Demery), in order to provide further evidence of meeting the requirements

of N.Y.S.E. Rule 405 ("Know Your Customer"). Huff himself did not contact the general partners; nor did he ask Huber, or attempt otherwise to verify, whether the general partners had been contacted.

In November 1979, Dorman, Vass's assistant, received a letter from an investigator in the Office of the Comptroller of the State of Florida, inquiring about the "short-term trading program." Huff read the letter and recognized Greenman's program from the description. Huff learned from the investigator's letter that Huber had responded to an earlier inquiry by the Comptroller's Office and had requested that direct "confrontation" with PaineWebber's clients be avoided. Huff testified he was not concerned that Huber had requested direct "confrontation" with PaineWebber's clients be avoided. Huff met with Dorman, Lippsett, and Greenman concerning preparation of a response to the inquiry. Huff reviewed Dorman's response before it was sent out. Dorman's letter to the Comptroller stated in part that "Huber's March 22, 1979 letter should never have been sent and that its wording has created unnecessary work for you." Huff testified he presumed that Dorman thought there were some "inaccurate" statements in Huber's earlier letter to the Comptroller.

Knowing what Huff then knew about the entire circumstances, Huber's request that Greenman's customers not be

contacted should have constituted a red flag to him, and Huff should not have allowed the response to the Florida Comptroller's inquiry to be based upon unverified representations made by Greenman. Moreover, the inquiry from the Florida Comptroller's office should have prompted Huff to initiate the kind of searching inquiry into Greenman's program that the overall circumstances by then known to Huff called for.

In late 1979 and early 1980 Huff began conducting informal profit and loss computations on Greenman's customer accounts. Huff discovered that some of Greenman's customers were losing money. He did not discuss the losses with anyone.

Shortly after joining PaineWebber, Huff saw activity letters that had purportedly been sent to Greenman's customers in early 1979. These were sent out over Greenman's signature rather than the branch manager's. 13/ Huff did not check to see whether any additional activity letters were sent to Greenman's customers. As SROP, Huff occasionally requested branch managers to obtain letters of activity for active option accounts. Yet he never asked Huber to obtain activity letters from Greenman's customers even though he was on clear

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13/ In fact, the early 1979 activity letters Greenman gave to Huber, which were forwarded to PaineWebber's Compliance Department in New York, contained false information and forged customers' acknowledgments, as earlier noted herein.

notice that Greenman's program required active surveillance.

Another cautionary signal arose when Huff received a letter dated March 28, 1980, from an investigator at the Midwest Stock Exchange ("M.S.E."), requesting detailed information relating to certain option orders executed for one customer account number.

The M.S.E. investigator requested, among other things, the following:

- names, addresses, places of employment and individual account numbers of the persons whose orders were assigned to that account number;
- name of the registered representative who entered orders for that account; and
- whether the orders were solicited by the registered representative.

These orders in question had been executed by Greenman. Huff responded in writing to the M.S.E. investigator's inquiry on April 11, 1980. Huff's response listed five different customer accounts, serviced by Greenman, that were assigned a single order number for trades in Freeport Minerals options. Each of the five customer accounts had a post office box address, and three of the five accounts shared the same post office box.

Huff understood that the use of post office boxes as customer addresses was a "red flag" indicating further inquiry was indicated. Nevertheless, he did not attempt to obtain a home or business address for any of those customer accounts.

Huff's response to the M.S.E. investigator further advised that Greenman had entered the orders in question and that the orders were unsolicited. Huff did not make any effort, other than talking to Greenman, to ascertain whether the orders were, in fact, unsolicited. Nor did Huff attempt to determine whether those customer accounts were otherwise "acting in concert" for position-limit purposes. Although Greenman told Huff the orders were unsolicited, they were in fact "discretionary" orders although, as previously noted herein, proper authorization for discretionary trading had not been obtained. Huff should have known or strongly suspected this since the nature of Greenman's program, as Huff understood it from the Paine Memorandum and otherwise, was such that Greenman suggested trades to customers. Huff should have used this occasion to get to the bottom of things regarding Greenman's options trading program. Instead, Huff acted as if he were reluctant to turn over a stone of suspicion for fear of what might turn up underneath.

Later, Huff received another letter from the M.S.E. investigator, requesting additional information concerning

the Freeport Minerals options orders. The M.S.E. investigator requested the names, addresses, and places of employment for all persons with authority to enter orders for the customer accounts Huff had listed in his previous response. On or about May 8, 1980, Huff responded by letter to the M.S.E.'s follow-up letter. He listed five individuals and provided their addresses. Three of the five persons shared the same street address in Jacksonville, Florida. Huff did nothing to verify the shared addresses, nor did he request Huber, or anyone else, to do so.

Another clear occasion for getting to the bottom of things with respect to Greenman's options trading program presented itself to Huff in April, 1980, when Vass asked him to look into the case of the customer who reported he had a profitable account with Greenman but for whom Huff could find no account at PaineWebber. Unfortunately, Huff again muffed the opportunity.

Arthur May ("May") was an investor in Greenman's "short term trading program" who received fictitious account statements from Greenman showing profits of 5 to 7 percent per month. About April 10, 1980, Huff and Vass had one of several conversations concerning May. Vass told Huff that May was one of Greenman's clients, and that Bill Cavell ("Cavell"), an attorney employed by PaineWebber, had spoken with May at a

social function. May had reportedly related to Cavell that he had a profitable account at PaineWebber. Vass asked Huff to contact May. Before contacting May, Huff attempted to obtain May's account number from PaineWebber's records but was unable to locate an account for May.

Huff telephoned May and asked him whether he had an account with Greenman. May replied that he did. Huff told May that PaineWebber made it a practice to contact clients occasionally to ascertain whether they were satisfied with the handling of their account, whether there was any information they would like about additional services, and whether they had any problems with their account. Huff asked May whether he was satisfied with his account at PaineWebber and the service he had been receiving from Greenman. May responded in the affirmative. The entire conversation lasted only a couple of minutes.

Huff did not ask May for his account number or for the name of his account, although Huff had been unable to locate May's account. Huff did not ask May if he was a limited partner in a limited partnership account, although he knew that a number of Greenman's customers were limited partners. Huff did not ask May if he had lost money in his account, nor did he ask him anything about the earnings in his account.

Huff reported back to Vass that there was nothing he could find out from May and that May had no complaints.

Huff made no further efforts to locate May's account. Except for May, Huff did not contact any of Greenman's customers.

While it is understandable that a compliance officer in contacting a customer concerning a potential compliance problem would want to do so in a manner that would not scare the customer away or cause him/her unneeded concern, in this case, given what Huff knew about Greenman's options trading program and the questions it had engendered, there was no reason for Huff to be quite as circumspect or pusillanimous as he was in his contact with May. Moreover, there was no excuse for not following up through the other avenues available to Huff to conduct or cause to be conducted the searching inquiry that the situation called for.

In April 1980, Huff prepared a formal profit and loss analysis of 25 of Greenman's customer accounts, covering the period from the time each account was opened at PaineWebber until March 28, 1980. Huff's profit and loss analysis showed that, of the 25 accounts analyzed, 24 had total realized and unrealized losses of over $7.6 million and only one account had a profit, of approximately $3,200. Even after this, Huff did not contact any of Greenman's customers, nor did he contact Huber, concerning the losses.

Huff's findings of huge losses were particularly significant in light of the recurring reports that some customers had been talking about huge <u>profits.</u> Additionally, the findings of huge losses were also highly significant in view of the fact that no complaints from any of Greenman's customers came to Huff's attention during the relevant period. Huff testified that "customers are notorious for complaining when they're losing money." According to expert testimony at the hearing, if a client is losing money [in significant amounts], he usually closes his account or complains to the branch manager or the compliance department.

In early May 1980, Huff and Vass after consulting together sent Lippsett, PaineWebber's CROP, to PaineWebber's Miami office to interview Greenman, due to a significant level of concern about Greenman's options trading program in PaineWebber's compliance department. 14/

As already noted, Huff had discovered losses of over $7.6 million in 24 out of 25 of Greenman's customer accounts, and yet there were no complaints from Greenman's customers. Prior to Lippsett's visit to Miami, Huff suggested that consideration be given to terminating Greenman on the basis of the

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14/ Lippsett testified he has made only approximately six such trips to branch offices in the nineteen years he has been with PaineWebber.

losses alone, but Vass demurred on the basis that before that step could be taken additional information to support it would be required.

Prior to Lippsett's visit, Huff and Vass discussed with Lippsett what questions he should ask Huber and Greenman. Among the concerns Huff and Vass had was the fact that in a number of the Greenman customer accounts money appeared to be going in and coming out of the accounts for no apparent reason, i.e. the transfers of funds seemed unrelated to any securities transactions.

Huff and Vass gave Lippsett a number of questions to ask Greenman and Huber. In addition, Lippsett prepared some of his own questions.

While in Miami, Lippsett directed only one question to Huber. All other questions were posed to Greenman. Lippsett made notes of the responses given by Greenman.

Lippsett asked Greenman why investors were still referring to his program as an "arbitrage" program. This question was posed because May had used the word "arbitrage" in a conversation with Cavell when describing his account with Greenman. Greenman's response, as summarized by Lippsett in his notes, was as follows:

> Arbitrage - Exposure into other areas - long term loans in U.S. from Europe and Saudi Arabia, 12 trusts of a billion or more, permits attorneys to practice in

> front of them to set up deals, etc. Provisions bank or a country guaranteeing loan (rates are currently 8 1/4% swiss francs). Placed 2 billion in loans in with La. Oil Co. backed by Turkish Government (750 million); 250 million to develop truck stops for black truck ownership, gtd. by Dept. of Agri., 10% by bank in California, 15 year loans averaging 1 1/8 pt. spread . . . about 22 million a year, $87,000 per day.

Lippsett asked Greenman why people were quoting "7% a month" returns on his options trading program. Lippsett's notes of Greenman's answer state "7% return - uses trading program to invest and expand their people in the program. Losses . . . being used to offset capital gains. Searching . . . foreign money to set up offshore corporation."

Lippsett asked Greenman "Are clients aware they lost money?" Greenman's answer, according to Lippsett's notes, was that "limited partners are advised of net asset value of partnership, sent a statement monthly, no break down." Lippsett understood from Greenman's response that the limited partners were advised by the general partners only of the net asset value of the partnerships.

Lippsett asked Greenman, "Can we get an updated listing of all partners in the corporation and their occupations?" Greenman's response, as summarized by Lippsett, was "will try to get a listing of limited partners . . . clients are super-sensitive to security."

Lippsett's notes stated "If I find May's account, why is he advised he's making money." Lippsett did not find out why May thought he was making money because Lippsett could not locate May's account in the New York office. Lippsett did not attempt to locate an account for May in the Miami office, nor did he ask Greenman anything about May.

When Lippsett returned to New York, Vass and Huff met with him and discussed his findings. Lippsett reported at the meeting, among others things, that:

- the monies invested at PaineWebber were just a small portion of the total worth of the parnerships; and
- the partnerships were involved in loaning money to foreign countries.

Lippsett expressed to Huff and Vass his continuing concern that there were large losses in Greenman's customer accounts, and still there were no complaints from Greenman's customers. Lippsett's concern about losses in Greenman's customer accounts and the absence of any complaints from Greenman's customers was alleviated, he testified, at least in part, by Greenman's "explanation" that the partnerships while losing substantial sums in trading options, were, as partnerships, doing well. But given the paucity of reliable data Lippsett had obtained about the numerous concerns about

Greenman's options trading program, and the fact that the compliance department still had only Greenman's word about things, there was no basis for being sanguine, either on the part of Lippsett or Huff. Moreover, it was clear from the responses Lippsett elicited from Greenman that limited partners were very probably unaware of the losses being incurred as a result of Greenman's options trading program. This situation clearly called for a searching inquiry that Huff failed to insist upon.

Huff testified he was "satisfied" with the responses obtained by Lippsett in Miami. He never asked Huber or Greenman to supply him with financial statements for the limited partnerships. Huff did not do anything further to check on any of the questions about Greenman's accounts.

Before Lippsett met with Greenman in Miami, Huff, Vass and Lippsett learned that Greenman was going to resign. Huff, Vass and Lippsett had a discussion as to whether Lippsett should continue with his trip. Huff and Vass decided that he should.

If Greenman had not resigned, Huff testified, he might have followed through on several matters, including obtaining the identify of limited partners and locating May's account.

I conclude that Greenman was allowed to resign from PaineWebber not because Lippsett's visit to Miami had produced

or was believed by Huff or others in the compliance department to have produced any satisfactory or credible answers to the significant concerns that Huff and others in the compliance department had about Greenman's options trading program, but because resignation was viewed as a convenient way of getting rid of an employee whose continued employment presented substantial risk of harm to the firm. Huff's failure to take the proper, indicated course by undertaking, initiating or insisting upon the searching inquiry called for, and recommending Greenman's discharge if the fraud were uncovered by such search, made it possible for Greenman to continue his fraud when he shifted to his new employer.[15/]

Moreover, Huff did nothing to ensure that when Greenman was allowed to "resign" from PaineWebber and move on to his new employer established PaineWebber procedures respecting the transfer of accounts in the Miami Branch office would be followed. Huff did not contact Huber to remind him of his obligations in this respect (which step was clearly indicated under all the circumstances), with results that were disastrous, as already noted herein (See p. 24-25 above).

15/ Huff made a point of warning a friend at Greenman's new firm (see footnotes 5, 9 and 10 above) that Greenman's customer accounts showed substantial losses, but did not tell him of the full range of concerns he and others in compliance had about Greenman's options trading program.

A final element in Huff's failure reasonably to supervise Greenman and Huber derives from the striking fact that during the whole of the relevant period, Huff never discussed the subject of Greenman's program with Huber or Punch. The record indicates that Huff's predecessor as SROP spoke to Huber at least twice concerning Greenman's short term trading program. For Huff not to have maintained contact with and guided Huber in his supervisory responsibilities over Greenman under the circumstances that Huff became aware of at various times during the relevant period is incomprehensible and inexcusable.

F. Respondent's Contentions.

Sections 15(b)(6) and 15(b)(4)(E) of the Exchange Act provide, in relevant part, that the Commission, if it finds that doing so is in the public interest, shall censure or place limitations on the activities of any person associated with a broker or dealer, or suspend for a period not exceeding twelve months or bar any such person from being associated with a broker or dealer, if the Commission finds that such person ". . . has failed reasonably to supervise, with a view to preventing violations of [specified securities laws, rules, or regulations], another person who commits such a violation, if such other person is subject to his supervision."

There is no requirement in the relevant statutes that the failure to supervise be shown to have been wilful.

Respondent Huff argues that neither Greenman nor Huber was a person "subject to his supervision" within the meaning of the relevant statutes discussed above and that Huff therefore had no supervisory responsibilities with respect to them.[16/] Huff makes two separate, and, as will be seen, contradictory, arguments in support of this asserted defense.

Firstly, Huff argues that under PaineWebber's organizational structure, as set forth in Respondent's Exhibit CM, only "line" officers within the sales organization branch system chain of command such as the branch office managers (e.g. Huber), the regional or division manager (e.g. Punch), the head of the Division of Branch Office system (Schmidt), and, ultimately, the PaineWebber president (Curley) had supervisory responsibility over Greenman (or Huber), since only they had "line" supervision and only they had the power to discharge or take disciplinary action against such an

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16/ Since Respondent Huff's arguments on this point are in substance the same as or similar to those expressed in the statement of views of the Compliance and Legal Division of the Securities Industry Association (see footnote 3 above and related text) it is unnecessary to treat separately herein the statement of views.

employee. People in the compliance department,[17/] on the other side of the chart, such as Huff, the argument continues, had purely an "advisory" role, within which they were limited to advice and suggestions, and therefore had no obligation to supervise Greenman or Huber.

Secondly, Huff argues, when confronted with the language of CBOE Rule 9.8/9.8(a) (see pp. 26-27 above), which he concedes "seemingly placed full responsibility for supervision of all non-member customer accounts and all orders in such accounts insofar as the accounts and orders relate to options contracts on the SROP," that under Interpretation .01 of the Rule all of the SROP's (Huff's) supervisory responsibility had been delegated to the branch managers (here, Huber), leaving Huff with no supervisory responsibility over Huber or Greenman.

Respondent's arguments lack merit for a number of reasons.

First of all, the compliance department, as its very name suggests, is an integral part of the supervisory process, particularly in a large, geographically dispersed brokerage house such as PaineWebber. Thus, the Commission has said, in Prudential-Bache Securities, Inc. [1985-86 Transfer Binder] Fed. Sec. L. Rep. (CCH ¶83,948, at p. 87,946):

17/ As earlier noted, the Compliance and Legal Departments reported to the General Counsel, who in turn reported to the Chairman of the Board, to whom Exhibit CM also shows the President (Curley) as reporting.

The Commission has long recognized that it is not sufficient for a broker-dealer to establish a system of supervisory procedures which rely solely on supervision by branch managers. See Shearson, Hamill & Co., 42 S.E.C. 811 (1965). In Shearson, Hamill, the Commission found that the firm abdicated its responsibility of supervision over its organization by excessive reliance on branch managers, and noted that a firm cannot dissipate its managerial responsibilities by geographic fragmentation, stating:

> The need for central control increases, not decreases, as branch offices become more numerous, dispersed and distant . . . It is essential . . . not only that a system of controls adequate to meet the problems inherent in a large and scattered organization be established but also that such controls be effectively enforced by those in authority.

Id. at 843. In the present matters, the fact that branch managers were remiss in their supervision, therefore, does not insulate Prudential-Bache from liability.

The Commission has also stated that "[t]here must be adequate follow-up and review when a firm's own procedures detect irregularities or unusual trading activity in a branch office . . . " [footnote omitted] A firm must have adequate procedures to assure that trading restrictions issued by its Compliance Department are not ignored by the branch managers or other personnel. A firm's Compliance Department is an important means for assuring adherence by its employees to the federal securities laws. A broker-dealer is not meeting its supervisory obligations under the federal securities laws if its Compliance Department can be disregarded or otherwise rendered ineffective by a branch manager. Similarly, a firm should seek to foster an attitude among its staff of cooperation with and acceptance of actions by the Compliance Department that will on occasion necessarily interfere with retail sales activity. Under no circumstances should a firm continue to tolerate a supervisor who persistently ignores legitimate Compliance Department recommendations or directives.

Although Prudential Bache involved the issue of the failure of the firm to supervise, rather than that of an individual within the compliance department, it is nevertheless evident that the Commission there rejected, at least implicitly, Huff's concept that officers in the compliance department serve merely an advisory role and are insulated from supervisory responsibility.

More specifically, the Commission found a failure reasonably to supervise on the part of a compliance officer in Alfred Bryant Tallman, Jr. et al., 44 S.E.C. 230 (1970). Even more specifically, the Commission found a failure reasonably to supervise on the part of a SROP in Michael E. Tennebaum, Exchange Act Release No. 18429 (January 19, 1982) [1981-82 Transfer Binder] Fed. Sec. L. Rep. (CCH) ¶83,092, at p. 84,811. Although Tennenbaum is indeed distinguishable in certain respects on its facts from the instant case, as Respondent Huff argues, the differences do not affect the basic holding that a SROP may be sanctioned for a failure reasonably to supervise.

The record herein establishes that PaineWebber made a conscious choice, as do most brokerage firms of that size and geographical scope, to place its SROP in the compliance department rather than in a "line" position because they considered he would by such placement be more effective in performing his

compliance and supervisory functions. Acceptance of Huff's argument would result in gross irony since it would render largely meaningless and ineffective one of the SROP's major functions.

Perhaps the most significant and conclusive refutation of Huff's arguments on the point under discussion is that the findings herein and the record as a whole show in great detail that the actual practice of PaineWebber during the relevant period, and, indeed, during all the time Greenman was employed at PaineWebber, was to have the compliance department, including Vass, the SROP (Paine, and later Huff), Lippsett (the CROP), and others, actively engaged in endeavoring to supervise and to ensure compliance by, Greenman and Huber.[18/] That the compliance department did not accomplish what it should have under the circumstances does not undermine the point that PaineWebber in fact considered the compliance department, including most significantly its SROP, an integral part, along with Punch, of the "team" that shared responsibility for ensuring compliance by and supervision over both Greenman and Huber.

18/ See especially Exhibits 32, 14, and 18 attached hereto as Attachments A through C, and Exhibits 16, 20, and 21, among others.

Moreover, it is significant that PaineWebber's compliance department (unlike that discussed by the Commission in _Prudential-Bache_, above), did not lack "clout". As found herein, Vass did not hesitate to write (and presumably to speak) forcefully and bluntly to Punch. If push came to shove, e.g. if the issue came to involve a proposal to fire Greenman over the objection of "line" managers, Vass without doubt would have been able through his superior, the general counsel, to get his view to the chairman of the board and/or the president of PaineWebber.

In addition, the record shows clearly that Huff and the compliance department had ready access to information and assistance from any relevant source within PaineWebber, e.g. the audit division, the legal department, and new accounts unit.[19/]

19/ Were the conditions described in this and in the immediately preceeding paragraph not so, it is doubtful that PaineWebber would be deemed to have had in place, as respects supervision of options trading, ". . . established procedures, and a system for applying such procedures, which would reasonably be expected to prevent and detect . . . [securities and other violations by employees]" within the meaning of Section 15(b)(4)(E)(i) of the Exchange Act. As already noted, the record herein establishes that PaineWebber's "line" supervision was ineffective without the shared supervisory assistance of Huff and the compliance department. The Order in this proceeding does not allege a failure on PaineWebber's part to have such procedures and system, but only a failure of Huff (and other personnel) to discharge their obligations thereunder.

In short, it is clear that PaineWebber's actual practice and system of procedures during the relevant period constituted a supervisory system under which supervision over Greenman and Huber was shared by "line" officers with Huff and other compliance department personnel. Moreover, from the record as a whole, it is evident that this is the general industry practice among firms of PaineWebber's size and geographical scope.

Turning next to Huff's "delegation" argument, i.e., that under Interpretation .01 to CBOE Rule 9.8/9.8(a) Huff's authority and responsibility as SROP had been delegated to Huber, the branch manager, the first question that comes to mind is how Huff could delegate supervisory authority and responsibility he claims he never had to the branch manager(s). A second question, for which Huff has no satisfactory answer either, is how the responsibility for supervising Huber in the performance of Huber's supervisory functions can be delegated to Huber. Is Huber to supervise himself in his supervision of Greenman and others in the Miami branch?

The simple fact is that Interpretation .01 to CBOE Rule 9.8/9.8(a), while authorizing the SROP to delegate " . . . to qualified employees responsibility and authority for supervision and control of each branch office handling options transactions . . .", expressly makes such delegation subject

to the proviso that the Senior ROP ". . . shall [continue to] have overall authority and responsibility for establishing appropriate procedures of supervision and control over such employee [the delegate, e.g., Huber]."

Whatever else the residual, non-delegable duties of the SROP must be deemed to include, they certainly must be held to include the obligation to conduct or to cause to be conducted and overseen, the type of searching inquiry that was here called for in light of the numerous, repeated, and significant red flags that came to Huff's attention. In addition, the residual obligations of the SROP must certainly be held to include an obligation to maintain contact with and a measure of supervision over the delegate (Huber) in the face of such red flags. As found herein, Huff failed to carry out these irreducibly minimal obligations.

Let it be clear that I am not holding Huff responsible simply because he was the Senior ROP, on something akin to a _respondeat superior_ concept. Nor am I holding that he could not delegate to a branch manager, subject to the restrictions on delegation discussed above. Also, I do not hold the nature of the supervision required of, or the manner of its exercise, will be the same when the SROP is (as here) assigned to the compliance department as it would have been if he had been placed in a "line" position. Further, I do not hold that

Huff was bound to uncover Greenman's fraud -- if he had taken the reasonable steps required of him under the circumstances, as already noted, and still failed to uncover the fraud, he would not have failed "reasonably to supervise". Regrettably, he did not take those steps. Lastly, I make no ruling respecting compliance personnel in general respecting their supervisory obligations, since the issue presented here is limited to the obligations of a Senior ROP.

Another argument made by Respondent Huff is his contention that Section 15(b)(4)(E) as it would be applied to him is unconstitutionally vague because the terms "reasonably to supervise" and "person . . . subject to his supervision" are not defined in the statute or in regulations thereunder.

At the outset, it must be noted that the Commission takes the position that it lacks power to declare unconstitutional the statues it has been directed to enforce.[20/] Aside from that, the terms in question have been applied both by the Commission and by the Courts in many cases without successful challenge to their constitutionality. And the terms are certainly no more imprecise than many other terms in the securities laws that have been upheld by the Courts.

20/ Todd v. S.E.C., 137 F.2d 475, 478 (C.A. 6, 1943); Milton J. Wallace and Joshua L. Becker, 45 S.E.C. 694, 697 (1975).

A further argument advanced by Respondent Huff is that deposition testimony given by Huff, Greenman, Huber and Vass in connection with prior Greenman-related litigation should not have been received in this proceeding or, at any rate, should be accorded little if any weight.

The Division correctly responds that if the Federal Rules of Evidence were applicable Huff's depositions would be receivable as admissions of a party opponent, and that, since all of the four individuals whose prior testimony is involved testified and were available for cross examination during the hearings herein, the prior testimony of the three other than Huff was admissible either because it was non-hearsay, if the prior statements were inconsistent with testimony given at the hearing, or as exceptions to the hearsay rule since they were statements against interest.

The parties recognize, at least implicitly, that hearsay evidence is receivable in Commission administrative proceedings subject to certain limitations. Here, I had the opportunity to observe and evaluate the credibility of all four of the witnesses in question, and the parties had opportunity to cross examine. I conclude that there was no prejudice to Respondent in receiving in evidence the prior testimony of the four individuals nor in my relying upon it to the extent the findings made herein indicate such reliance.

Lastly, Respondent argues that Exhibit 8, an educational handbook prepared by the CBOE and six other SROs entitled "Handling Options Transactions for Public Customers" was improperly received in evidence and should, if received, be accorded little if any weight.

The Division correctly points out in rebuttal that the handbook was properly authenticated by Vass, that the cover of the handbook indicates its "1st Printing" as March, 1980, and that the actual date of the book's dissemination is not significant since Huff was aware by early November 1979 of the SRO views set forth in the handbook.

It is anomalous for Respondent to argue that CBOE Rule 9.8/9.8(a) should be construed in the light of "custom and practice in the brokerage industry" and then turn about and seek to have rejected the industry views formally and specifically adopted by the industry to guide securities firms in the handling of options transactions for public customers. Respondent's objections to Exhibit 8 are not accepted. To the extent that expert witnesses dispute the relevant guidelines of Exhibit 8 they are not credited. Significantly, Respondents experts did not generally address the question of a SROP's obligation to act when red flags come to his attention, and at least one of them indicated that in such a situation the SROP would be obliged to make or cause to be

made the necessary inquiry. In any event, given the specific findings that form the bases for my conclusions herein, my decision would be no different if Exhibit 8 were not part of the record.

G. Conclusions of Law.

In general summary of the foregoing conclusions of law, it is concluded that during the relevant period from about mid July 1979 through about May 1980, Huff failed reasonably to supervise Huber, a person subject to his supervision, within the meaning of Sections 15(b)(6) and 15(b)(4)(E) of the Exchange Act, with a view to preventing Huber's violation in that Huber failed reasonably to supervise Greenman with a view to preventing Greenman's violations, as found herein, of Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, and Huff failed reasonably to supervise Greenman, a person subject to his supervision, within the meaning of Sections 15(b)(6) and 15(b)(4)(E) of the Exchange Act, with a view to preventing Greenman's violations, as found herein, of Section 17(a) of the Securities Act, Section 10(b) fo the Exchange Act and Rule 10b-5 thereunder.

III. THE PUBLIC INTEREST

In determining what sanctions, if any, it is appropriate to apply in the public interest, it is necessary for the

Commission, among other factors, to ". . . weigh the effect of . . . action or inaction on the welfare of investors as a class and on standards of conduct in the securities business generally." 21/

Effective supervision has long been recognized both by the Commission and by Self Regulatory Organizations as an essential ingredient in the maintenance of public trust and confidence in the integrity of the securities markets and industry.

The special importance of proper supervision was recognized in particular with reference to the options product, which affords special opportunities for abuse in its trading in public customer accounts, following the report of the Special Study of the Options Markets to the Commission in December 1978. CBOE Rule 9.8/9.8(a) (and its counterparts in other SROs) constituted clear recognition of the importance of effective supervision in the sale of the options product in the accounts of public customers by requiring each firm dealing in options to establish and specifically identify to

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21/ Arthur Lipper Corporation, Securities Exchange Act Release No. 11773 (October 24, 1975) 8 SEC DOCKET 273, 281. Although the reviewing court In Arthur Lipper Corp. v. S.E.C., 547 F.2d 171, 184-5 (2nd Cir. 1976) reduced the Commission's sanctions on its view of the facts, it recognized that deterrence of others from violations is a legitimate purpose in the imposition of sanctions.

the SRO a Senior ROP and by defining his duties and responsibilities. It would be a travesty of the self-regulatory process if this rule were construed or applied in a manner that would negate, attenuate, or in any manner serve to defeat the obvious purposes in establishing the positions of Senior ROP and ROPs.

The Division recommends a suspension of Respondent Huff for sixty (60) days. Respondent insists no sanction is indicated, for reasons discussed herein.

I conclude that the recommended 60-day suspension is fully warranted, both to deter similar failures in the future by Respondent Huff and to serve as a deterrent to failures by others reasonably to supervise.

IV. ORDER

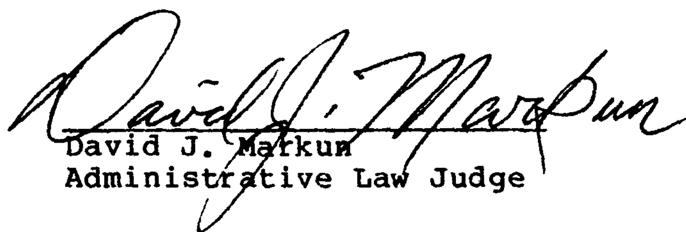
Accordingly, IT IS ORDERED as follows:

Respondent Arthur James Huff is hereby supsended from association with any broker or dealer for a period of sixty (60) days.

This order shall become effective in accordance with and subject to Rule 17(f) of the Commission's Rules of Practice, 17 CFR §201.17(f).

Pursuant to Rule 17(f), this initial decision shall become the final decision of the Commission as to each party

who had not, within fifteen (15) days after service of this initial decision upon him, filed a petition for review of this initial decision pursuant to Rule 17(b), unless the Commission pursuant to Rule 17(c) determines on its own initiative to review this initial decision as to him. If a party timely files a petition for review, or the Commission takes action to review as to a party, the initial decision shall not become final with respect to that party. 22/



David J. Markun
Administrative Law Judge

December 15, 1987
Washington, D.C.

22/ All proposed findings, conclusions, and supporting arguments of the parties have been considered. To the extent that the proposed findings and conclusions submitted by the parties, and the arguments made by them, are in accordance with the findings, conclusions and views stated herein they have been accepted, and to the extent they are inconsistent therewith they have been rejected. Certain proposed findings and conclusions have been omitted as not relevant or as not necessary to a proper determination of the material issues presented. To the extent that the testimony of various witnesses is not in accord with the findings herein it is not credited.

ATTACHMENT "A"

Greenman personal file

PAINE WEBBER JACKSON & CURTIS
INCORPORATED

NEW YORK OFFICE

April 23, 1979

TO: Robert D. Punch

FROM: O. Ray Vass

SUBJECT: Dennis Greenman - Miami Office Broker

Please excuse the rough draft form of the attached material. I will be away from the office almost all of next week and I think we should have some discussions relating to the attached material soon after my return (I'll call you).

George Warner and Marvin Lippsett put together the drafted material dated April 19, 1978. We have a number of concerns about Dennis Greenman's option trading system, the fact that a number of his clients have sustained very substantial losses over the past several months, and some disturbing indications which we continue to get from various sources as to the manner of his solicitation of new customer accounts. We are also very confused and concerned about the part Mr. Demery plays; supposedly being an extremely wealthy customer and acquaintance of Greenman who is so enamored of Greenman's system as to be willing to back seemingly unlimited numbers of other clients with some arrangement to guarantee them against loss.

I'll be in touch when I am back in the office.

ORV

Copy to Phil

call me - this is very dangerous

ORV:GK
Attach.

PW 287

Div Exh 32
2/4/87 3-6700
KA rec'd KA

April 19, 1979

On or about January 19, 1979, Mr. John Sykes of our Arbitrage Department contacted Sam Miller concerning a call that he had received from a friend of a friend, a man by the name of John Sefton, an attorney in Jacksonville, Florida. John Sykes told Sam Miller that Mr. Sefton had informed him that a client of his received a telephone call from Mr. Dennis Greenman of our Miami office. Mr. Gree: told Mr. Sefton's client that he had a special options arbitrage program that was sponsored by Paine Webber. Sam Miller requested that someone from the Complianc: Department investigate the nature of the program that Dennis Greenman was selling.

On the same day, George Warner of the Compliance Department contacted Mr. Sefton. Mr. Sefton related that his client had been informed by Mr. Greenman that he was authorized by Paine Webber to offer a special options arbitrage program which he had used very successfully at Merrill Lynch and now that he was a broker at Paine Webber was continuing to implement this particular program. According to Mr. Sefton, Mr. Greenman told his client that he was the only one in the State of Florida authorized to provide a program of this kind and that he could not possibly lose money if he invested in this type of program. Mr. Sefton stated that not only was his client interested in this type of option trading but that he himself would be interested in signing up for such a program if he could be assured that this was Paine Webber sponsored. At this point in time Mr. Sefton was thanked for this information and was told that this matter would be investigated and that he would be contacted shortly.

After the telephone conversation with Mr. Sefton, all of this information was related to Ray Vass. It was decided at this point in time to contact Phil Huber, Manager of our Miami office, where this broker works, in order to determine what type of program the broker was using with regard to options. During our conversation

with Phil Huber, he assured us that the broker had a good option program to provide to clients and that this program was tried and tested when Mr. Greenman was a broker at Merrill Lynch. Phil Huber also told us that he believed that Mr. Sefton and his client misunderstood Mr. Greenman with regard to the terminology "arbitrage". At this point in time we asked Phil Huber to give us the names and numbers of some of the accounts that were already participating in this program. Upon receipt of these account numbers, Marvin Lippsett did a P & L on about ten accounts for a period of approximately five months. The P & L findings for the accounts in question showed losses in practically every account. In one particular account, there were losses in every transaction. After this information was related to Ray Vass, a meeting was held with Bruce Paine, Marvin Lippsett and Ray Vass in which the matter of Mr. Greenman's trading procedures was discussed. It was then decided to contact Mr. Huber again and discuss the situation with him. In discussions with Phil Huber, it was brought out that Mr. Greenman had sent letters to his clients giving a breakdown as to their profit and losses for the year. This letter, in essence, asked the clients if they were satisfied with the trading in their accounts. Mr. Huber had informed us that he had received returns from 9 of the 12 customers that had been sent the letters and they were all on a positive note. Bruce Paine at that time asked Phil Huber to send copies of these letters to New York.

On or about March 26, Bruce Paine called Dennis Greenman and discussed the program that he was using. He was advised by Mr. Greenman that a particular client, a Mr. Demery was so pleased with the results of the program that he was willing to guarantee new clients' accounts that he introduced to Mr. Greenman. Bruce told Denni that this was not satisfactory but that we would allow Mr. Demery to have joint accoun with these people and Greenman agreed that he would open the accounts in this fashion

The first qualification forms were processed through our New Accounts Department; however, it was noted that on ~~all of the forms;~~ those set-up as joint accounts, only ~~provided~~ financial information concerning Mr. Demery and no particular information concerning the other party involved. Bruce Paine again spoke to Greenman and advised him that this was not satisfactory, that we would need information on each individual concerning the account, and that prior to the accounts being opened, Greenman would have to get specific approval from Bruce Paine and/or Marvin Lippsett.

Subsequent to the above, George Warner spoke to Mr. Sefton again, informing him that this was not a Paine Webber sponsored program and that there was no way that Mr. Greenman nor anyone at Paine Webber could promise him in any way that he would make money or that his money would be guaranteed in this or any type of investment program.

Tom Manchester, Manager of the Tulsa office, called on April 5th, to advise us of a conversation he had with a Bob Hughes who is associated with the Chamber of Commerce in Tulsa. Hughes stated that he was approached by a Glenn Copland who represented himself as being associated with Protex Bookkeeping Services. Mr. Copland stated that he was working with a Paine Webber broker in Miami and that he was interested in being introduced to people to describe a marketing strategy involving short term trading and arbitrage. Reference was made by Mr. Copland to a wealthy real estate investor in Jacksonville, Florida who would be willing to guarantee against loss those individuals who availed themselves of the trading program. The minimum investment would be $10,000 and an indication was given that one could earn 75 percent of their money in a short period of time. We noted that Glenn Copland carries an account with our Miami office.

Attached is a memo from Bruce Paine, dated March 13, 1979, which outlines in essence the program that Dennis Greenman is using. After reviewing this program and the procedures being used by Mr. Greenman in selling this program, it is our recommendation that Mr. Greenman's activities be very closely supervised by the branch manager and that periodic contact be made with the clients concerning their accounts.

ATTACHMENT "B"

PAINE
WEBBER
JACKSON
& CURTIS
INCORPORATED

NEW YORK OFFICE

July 12, 1979

TO: Robert D. Punch

FROM: O. Ray Vass

SUBJECT: Dennis Greenman

On Monday, June 25th, we met with Phil Huber and Dennis Greenman as requested and discussed at length Greenman's options business. Notwithstanding the professed urgency of that meeting, Tim Longworth has yet to receive additional material from the Miami office in the form of certain correspondence on the part of an attorney working with a partnership proposal to be used with certain of Greenman's customers. Some of the proposed arrangements raise very important questions as do a number of aspects of Mr. Greenman's activities; yet, almost three weeks after that meeting we have received absolutely none of the information requested.

To turn to a matter of even more urgency, I have this morning learned from Jim Dalton that Jim was contacted by telephone by Leo Pomerance who is now associated as a consultant with Drexel Burnham. Pomerance works through Drexel's Miami office. I am sure you are aware that he is an ex-chairman of the board and a founder of the CBOE.

Pomerance's message to Dalton was to the effect that people are going around talking about 70 percent returns and an option arbitrage program. Contacts are being made with Drexel Burnham customers and those customers are asking Drexel Burnham about the program. This is clearly our man Greenman or possibly some of his clients who have themselves been promoting his abilities as an options expert.

In the course of the discussion with Huber and Greenman in New York, I cautioned them that with the amount of publicity which constantly surrounds Greenman, either of his own generation or by his customers', a detailed regulatory inquiry into Mr. Greenman's activities and methods is almost certain to arise at some point in the near future. I urged Huber and Greenman to be particularly diligent so as to be able to show good evidence of proper business practices, documentation, and supervision. With contacts of the nature of that made by Pomerance (and in view of Pomerance's closeness to the industry), I am even more convinced that Greenman and Huber should be prepared for a close regulatory scrutiny.

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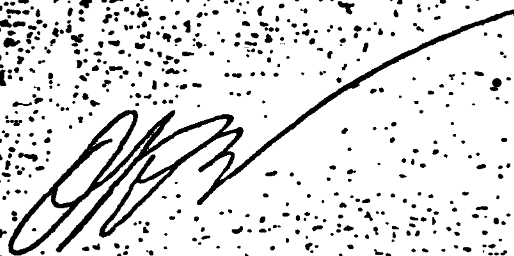
I am reaching the end of my patience with receiving reports of the nature of that from Pomerance. I do not know if these quoted percentage returns and use of the word "arbitrage" is originating with Greenman or his clients (whom he has assured us he has cautioned along these lines). In any event, Greenman (and his clients) must either be controlled or Greenman must be terminated.



ORV/mm

cc J. Dalton
P. Huber
J. Huff

ATTACHMENT "C"

PAINE
WEBBER
JACKSON
& CURTIS
INCORPORATED

NEW YORK OFFICE

copy

CONFIDENTIAL TREATMENT REQUESTED
BY PAINE, WEBBER, JACKSON & CURTIS, INC.

September 11, 1979

TO: A.L. Meentemeier

FROM: O. Ray Vass

SUBJECT: MIAMI - NEW YORK COMPLIANCE REPORT

Thank you for your memo of August 24, 1979 relating to the option accounts handled in our Miami office by investment broker Dennis Greenman.

The Compliance Department has been very much involved for an extended period of time with Mr. Greenman and his option accounts; particularly those accounts financially backed by H. Preston Demery or in which Mr. Demery is a participant. This has included a review of the documentation of the partnership accounts in which Demery is a partner by Tim Longworth of our Legal Department.

Mr. Greenman tends to have large accounts which trade actively in the options markets. This was the case at Mr. Greenman's previous employer firm where he dealt with a large number of the accounts which now do business with him here. Among other things, we have reviewed "activity" letters sent by Mr. Greenman to a number of his accounts which point out quite clearly the risks involved in options trading and the fact that previous results may not be indictive of those in the future.

We have met with Mr. Greenman and branch manager Phil Huber here in New York for a extensive discussion of Greenman's activities. Greenman and Huber have been cautioned in detail that they must maintain very good records and be especially cognizant of compliance with all applicable rules and regulations in anticipation of an external regulatory review of Greenman's options activity at some point in time. Though we have received no customer complaints of any kind relating to Greenman, there have been instances of our competitors becoming upset when their clients have been approached by customers of

Div Exh 18 2/5/87 3-6700 KA

GS [illegible]

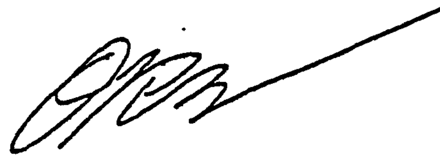
Dennis Greenman who have been extremely complimentary of Greenman's abilities and results and strong in their recommendations of him as a broker. Greenman himself has advised his own clients to be conservative in their comments on him and not to use the term "arbitrage" which was used at an earlier time in describing Greenman's options trading systems.

Detailed discussions have been held with branch manager Phil Huber and with division manager Bob Punch as to the need for careful and diligent supervision over Greenman's activities; not because of any developed problems but simply because of the size and nature of his business and because of the displeasure on the part of other firms as a result of their customers being contacted by Greenman's customers, as mentioned earlier.

Our Senior ROP Jim Huff and our Compliance ROP Marvin Lippsett are both quite familiar with Greenman's accounts and his activity. They observe daily listings of large positions and frequently observe Greenman's accounts in this regard. In addition, they are reviewing the monthly statements for Greenman's accounts.

Jim Dalton and various individuals in our Options Department and on the Options Trading Desk are also familiar with Greenman's business and accounts and have on a number of occasions in the past been in direct contact with us when transactions were observed and gave rise to concern. I anticipate this will continue to be the case.

In short, I believe appropriate steps have been and will continue to be taken in terms of monitoring the activity in Greenman's accounts. If any problem should arise, I believe we will be able to demonstrate having done our due diligence.



CONFIDENTIAL TREATMENT REQUESTED
BY PAINE, WEBBER, JACKSON & CURTIS, INC.

cc: J. Huff
M. Lippsett
T. Longworth
L. Leon
E. Niemiec
J. Larkin