INITIAL DECISION NO. 70

ADMINISTRATIVE PROCEEDING
FILE NO. 3-8304

UNITED STATES OF AMERICA
Before the
SECURITIES AND EXCHANGE COMMISSION

In the Matter of	)	
	)	
RICHARD H. MORROW	)	INITIAL DECISION
	)	JULY 25, 1995
	)	

APPEARANCES: Glenn A. Harris and Terence M. Tennant for the Division of Enforcement, Securities and Exchange Commission, Miami, Florida

Mitchell A. Margo, St. Louis, Missouri, for Respondent Richard H. Morrow

BEFORE: Burton S. Kolko, Administrative Law Judge

I. INTRODUCTION

This proceeding was instituted by order of the Commission on March 7, 1994, pursuant to Section 8A of the Securities Act of 1933, 15 U.S.C. § 77h-1, and Sections 15(b), 19(h) and 21C of the Securities Exchange Act of 1934, 15 U.S.C. §§ 78o(b), 78s(h), and 78u-3. In the order, the Division of Enforcement alleged that from the period in or about December 1989 through April 1990, Richard H. Morrow ("Morrow") violated Sections 10(b) and 15(c) of the Securities Exchange Act of 1934 ("Exchange Act"), 15 U.S.C. §§ 78j(b) and 78o(c), and Rules 10b-5, 10b-9, and 15c1-2, 17 C.F.R. §§ 240.10b-5, 240.10b-9, and 240.15c1-2, promulgated thereunder; and Sections 17(a)(1), (2) and (3) of the Securities Act of 1933 ("Securities Act") 15 U.S.C. §§ 77q(a)(1), (2), and (3), by selling units in a mini-max offering past the offering deadline and by failing to disclose his compensation.

A hearing was held on June 28 and 29, 1995 in New York City to determine whether the allegations with regard to Morrow were true and to afford him an opportunity to establish any defense.1/

II. FINDINGS OF FACT

BACKGROUND

Morrow is currently self-employed as an independent insurance agent, financial adviser and a registered representative associated with Sun America Securities. (Transcript pp. 74-75) (hereinafter "Tr."). Morrow's offices are located at 205 Route 46, Suite 16, Totowa, New Jersey. (Tr. 75). Morrow has been a registered representative since 1973 and currently holds a Series 7 license and a State of New Jersey insurance license. (Tr. 76).

During the period relevant to this proceeding, December 1989 through April 1990,

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1/ Robert Weston ("Weston"), the other respondent in this proceeding, submitted an offer of settlement which the Commission accepted on September 28, 1994. Weston was barred from association with any broker, dealer, investment adviser, investment company, or municipal securities dealer for a period of one year.

Morrow was associated as a registered representative with Anchor National Financial Services, Inc. (Tr. 81). Morrow used the means and instruments of transportation and communication in interstate commerce and the mails in connection with the offer and sale of units in Park Florida. (Plaintiff's Exhibits 10, 41, 49-60) (hereinafter "Px.").

Park Florida Associates, Ltd. ("Park Florida") was a Florida limited partnership that sponsored a private placement offering to raise capital for a real estate development project. The funds were to be used to purchase land, construct, and operate a strip mall shopping center near Tampa, Florida. Ultimately the partnership planned to sell the property for a profit that would be divided between the general and limited partners. (Px. 1).

Keystone Financial Holdings, Inc. ("Keystone") was the general partner of Park Florida. (Px. 1). John Michael Pratt ("Pratt") was the principal of Keystone and controlled the daily operations of Keystone and Park Florida. (Px. 1).

Morrow testified that he became aware of the Park Florida offering sometime during September or October 1989. (Tr. 80, 83). Morrow and Weston, Morrow's former financial adviser, flew to Florida to meet with Pratt about possible real estate development projects, including Park Florida. (Tr. 83-84). At the meeting, Morrow and Weston each agreed to raise half of the funds required for the Park Florida offering, or $400,000 each, by selling limited partnership units in the Park Florida. (Tr. 85, 103). Morrow further testified that he did not really become involved in the Park Florida offering until January 12, 1990 when he began soliciting investors. However, in November 1989, shortly after the meeting with Pratt and Weston in Florida, Morrow received copies of the Park Florida Private Placement Memoranda ("PPM") from Keystone for distribution to potential investors. (Tr. 93; Px. 10, 68).

SELLING DEADLINE

The Park Florida offering was structured as a "mini-max" offering and designed to raise a minimum of $600,000 and a maximum of $800,000 by January 31, 1990. The PPM included various representations to the effect that the investors' funds would be deposited into an escrow

account and would be returned if the minimum proceeds were not obtained by the offering's closing date. The January 31, 1990 closing date was critical to the offering and could only be extended by an agreement of the general partner and the investors. (Px. 1).

The minimum proceeds were not obtained by the January 31, 1990 closing date. In fact, as of the closing date the offering had only raised $187,000. (Px. 42; Tr. 111). Morrow nevertheless continued to offer and sell interest in Park Florida after the closing date. (Px. 41, 42; Tr. 95, 191).

Morrow testified that he knew there was a January 31, 1990 closing date but was told by Pratt and Weston that they were working on an extension and that the closing date was not effective anymore. (Tr. 107-108). Morrow also testified that he was confused about the difference between an "extension" and a "cut-off date or deadline." (Tr. 120). However, as of January 31, 1990, the cut-off date had not been properly extended by agreement of the general partner and the investors. (Tr. 122-227, 229-230).

Nevertheless, Morrow offered and sold limited partnership units in Park Florida to the following thirteen clients after the January 31, 1990 closing date, when in fact no valid extension to the offering had been approved. (Tr. 122-227, 229-230).

Investor	Amount	Date Sold
Delores Higgins	$75,000	2/1/90
Marie Partington	$25,000	2/1/90
Alfredo Pellegrini	$50,000	2/1/90
George Schumtzer	$25,000	2/5/90
Maria Simpson	$25,000	2/5/90
Rudolph Fantauzzi	$25,000	2/6/90
Saul Sender	$25,000	2/7/90
Russell Schwarz	$25,000	2/7/90
Morris Altman	$25,000	2/13/90
Jack Tuvel	$25,000	2/13/90
Nicholas Fedish	$25,000	2/16/90
Angelo Polidoro	$25,000	2/21/90
Marion Varricchio	$25,000	3/6/90

Morrow further testified that as of February 1, 1990 he had not seen a written extension to the offering, but merely relied on Weston's assurances that the offering deadline had been

extended. (Tr. 122-127). In most instances, Morrow never discussed the mini-max offering deadline with his clients when soliciting their investments. (Tr. 24, 44, 68).

On March 21, 1990, an addendum to the PPM was mailed to the investors for the purpose of providing additional disclosure. (Px. 17). The addendum purported to offer the investors an option to rescind their investments and receive a full refund. The addendum also purported to extend the offering deadline until April 15, 1990. (Tr. 203).

The designated escrow agent for the offering, Alan S. Gassman, an attorney, testified that the addendum could not extend the offering deadline because the offering itself ended as of February 1, 1990 when it failed to achieve the minimum subscription. (Tr. 229-30).

Unfortunately for the investors in Park Florida, the funds were improperly escrowed and misappropriated by Pratt. The Park Florida investors lost approximately $575,000 of their investments. (Px. 48,) (Tr. 213).

THE COMMISSIONS

The PPM stated in capitalized, bolded print that **"NO SELLING COMMISSIONS WILL BE PAID BY THE PARTNERSHIP IN CONNECTION WITH THE SALE OF UNITS."** However, Morrow was to be compensated for his services in connection with the Park Florida offering by receiving an eight (8) percent commission based on the total amount raised from his clients. (Tr. 112-113; Px. 37, 3, 4). Morrow was also to receive a five (5) percent equity interest in the Park Florida real estate development project. (Tr. 114). Although many of Morrow's clients presumed he was being compensated in some manner, most were not told about the details of Morrow's compensation arrangements. Two investors, Marion Manginello and Angelo Polidoro, testified that they never discussed commissions with Morrow and that Morrow never mentioned the subject. (Tr. 23, 44). Morrow testified that he understood that the commissions were to be paid by the general partner and not the partnership, and therefore did not consider his compensation to be inconsistent with the "no selling commissions" legend in the PPM. (Tr. 105, 112-13).

III. CONCLUSIONS OF LAW

A. Morrow's Violations of Section 10(b) of the Exchange Act and Rule 10b-9, thereunder

Rule 10b-9 provides that "It shall constitute a 'fraudulent, deceptive, or manipulative act or practice' as used in Section 10(b) of the Act" for any person in the offer or sale of any security to make any representation that:

> The security is part of an offering or distribution being made on the condition that all or a specified part of the consideration paid for such security will be promptly refunded unless (A) a specified number of units of the security are sold at a specified price within a specified time, and (B) the total amount due to the seller is received by him by a specified date.

The Commission adopted Rule 10b-9 in recognition of "the great potential for fraudulent conduct on the part of persons in connection with public offerings of securities on an 'all or nothing' basis." SEC v. Manor Nursing Centers, Inc., 458 F.2d 1082, 1095 (2d Cir. 1972). The Rule is designed to protect investors by ensuring that the "all-or-none" or "part-or-none" representation is neither misleading nor deceptive. Id.

"The 'all-or-none' and 'part-or-none' contingencies have been called a 'principal protection' of investors." In the Matter of Gallagher & Co., Securities Exchange Act Release No. 29244 (May 29, 1991), 48 SEC Doc. 1752, 1763, citing SEC v. Blinder, Robinson & Co., 542 F. Supp. 468, 476 (D. Colo. 1982). "They guarantee each investor that his money will be refunded unless other public investors share his view that the risk he is taking is worthwhile, and the price he is paying is fair." Gallagher & Co., 48 SEC Doc. at 1763-64 (emphasis in original, footnotes omitted). The underwriters' inability to sell the specified minimum number of shares may indicate, for example, that "the market judges the offering price to be too high." A.J. White & Co. v. SEC, 556 F.2d 619, 623 (1st Cir. 1977), cert. denied, 434 U.S. 969 (1977).

The Commission has stated that Rule 10b-9 "unlike Rule 10b-5 under the Securities Exchange Act, prohibits a specific type of misrepresentation. And we adopted it because we

considered the misrepresentation it bans always material." In re FAI Investment Analysts, Inc., 46 S.E.C. 1134, 1136, n.11 (Dec. 19, 1977).

In the present case, it is undisputed that all of Morrow's sales were made after the January 31, 1990 cut-off date. Morrow acted with the requisite scienter to establish violations of Rule 10b-9. Morrow testified at trial that he knew that the offering was a mini-max having a closing date of January 31, 1990, albeit he was told that the offering deadline was going to be extended. (Tr. 119). Nevertheless, Morrow was negligent in failing to ascertain whether the offering deadline had, in fact, been extended prior to selling interests in Park Florida during the months of February and March. See Svalberg v. SEC, 876 F.2d 181 (D.C. Cir. 1989); SEC v. Falstaff Brewing Corp., 629 F.2d 62, 77 (D.C. Cir.), cert. denied, 449 U.S. 1012, 101 S.Ct. 569, 66 L.Ed.2d 471 (1980).

In Manor Nursing Centers, Inc., 458 F.2d at 1095, the Second Circuit stated:

> [h]ere, it is clear that all appellants knew that the offering was presented on an "all or nothing" basis. Moreover, the evidence established that appellants knew, or should have known, that all of the shares had not been sold and that all of the proceeds had not been received by March 8, 1970. Under the circumstances, there can be no doubt that representing that the offering would be on an "all or nothing" basis violated Rule 10b-9.

Morrow violated Rule 10b-9 by offering and selling interests in Park Florida after the offering deadline. Morrow negligently relied on verbal assurances that the deadline was being extended. (Tr 124). Indeed, prior to offering interests in Park Florida, Morrow had a duty to investigate to determine whether in fact the offering deadline had been properly extended. See Hanly v. SEC, 415 F. 2d 592, 595-597 (2nd Cir. 1969). Instead, Morrow simply relied on Weston and Pratt and stated that he had no idea that Weston would let him do anything wrong. (Tr. 125). Had Morrow properly inquired as to the status of the extension prior to selling units on February 1, 1990, and refrained from selling, his clients would have avoided the loss of their investment funds.

The court observed Mr. Morrow throughout the entirety of this proceeding and twice on the witness stand, and finds that Morrow was testifying credibly to the best of his ability,

and that he, without concocting it for the purposes of aiding his situation, is genuinely remorseful. The court believes that Morrow was acting in good faith; however the legal standards require more that a good faith effort. See Hanly v. SEC, supra.

B. Morrow's Violations of Sections 17(a)(1), (2) and (3) of the Securities Act and Sections 10(b) and 15(c) of the Exchange Act and Rules 10b-5 and 15c1-2, Thereunder

Section 17(a) of the Securities Act, Section 10(b) of the Exchange Act and Rule 10b-5 thereunder, Section 15(c) of the Exchange Act and Rule 15c1-2 prohibit misrepresentations or omissions of material facts in connection with the offer, purchase, or sale of securities. Alstead, Dempsey & Company, Inc., 47 S.E.C. 1034, 1038-39 (1984). Morrow violated these Sections and Rules by failing to disclose properly to his clients that he was to receive an 8% selling commission based on the total amount he raised through his investors and a 5% equity kicker based on the eventual sale of the partnership property at some indefinite time in the future. Although Morrow never received any compensation for his efforts, he still had a duty to disclose his compensation arrangements to his clients when recommending that they invest in the Park Florida offering. Such disclosure is even more critical in light of the bold-faced representation on the first page of the PPM that **"NO SELLING COMMISSIONS WILL BE PAID BY THE PARTNERSHIP IN CONNECTION WITH THE SALE OF UNITS."** The fact that Morrow understood that he was to be compensated from the general partner's funds does not diminish Morrow's duty to disclose all material facts. Accordingly, Morrow's failure to disclose adequately his commissions violated Sections 17(a)(1), (2) and (3) of the Securities Act and Sections 10(b) and 15(c) of the Exchange Act and Rules 10b-5 and 15c1-2, thereunder.

It is well established that individuals recommending the purchase of a security must disclose whether they have a financial interest in the recommendation. In SEC v. Torr, 22 F. Supp. 602 (1938), in which the defendants recommended purchases of stock without disclosing that they were to receive commissions, the Court held as follows:

> [w]hen persons take the initiative in recommending a stock, as the free-lance brokers did in this case, they become what might be called volunteer fiduciaries;

> and if they do not tell the person to whom they make their recommendations that they are getting a commission therefor, they are guilty of a breach of duty to him because they omit to state a material fact necessary in order to make their recommendation not misleading in the light of the circumstances under which it is made.

Id. at 607; see also L. Loss, Fundamentals of Securities Regulation, 825-26 (2d ed. 1988).

Similarly, in Laird v. Integrated Resources, Inc., 897 F.2d 826 (5th Cir. 1990), the court concluded that a defendant who had not accurately disclosed his financial interest in investments he recommended to clients violated Rule 10b-5 of the Exchange Act, since [investors] must be "permitted to evaluate [the investment adviser's] overlapping motivations, through appropriate disclosure." Id. at 840. Thus, in applying the Court's reasoning in Laird and Torr, Morrow should have disclosed to prospective investors his "overlapping motivations," i.e., his 8% commission and his "back-end equity kicker."

The antifraud provisions of the federal securities laws prohibit not only outright misrepresentations, but also omissions to fully state all material facts. Investors are entitled to full and complete disclosure of all material facts. SEC v. Capital Gains Research Bureau, Inc., 375 U.S. 180, 189-90 (1963); SEC v. Texas Gulf Sulphur Corp., 401 F.2d 833, 860 (2d Cir. 1968), cert. denied, 394 U.S. 976 (1969); SEC v. General Refractories Co., 400 F. Supp. 1248, 1257 (D.D.C. 1975).

ORDER

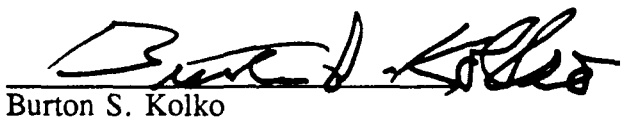
IT IS ORDERED that Respondent Richard H. Morrow cease and desist from committing any violation or causing any future violation of Section 17(a) of the Securities Act of 1933 and Sections 10(b) and 15(c) of the Securities Exchange Act of 1934 and Rules 10b-5, 10b-9 and 15c1-2 thereunder.

IT IS FURTHER ORDERED that Respondent Richard H. Morrow is suspended from association with any broker, dealer, municipal securities dealer, investment company, or investment adviser for a period of sixty (60) days.

This order shall become effective in accordance with and subject to the provisions of

Rule 17(f) of the Rules of Practice.

Pursuant to Rule 17(f) of the Rules of Practice, this decision shall become the final decision of the Commission as to each party who has not, within fifteen 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 the party timely files a petition for review, or the Commission takes action to review as a party, the initial decision shall not become final with respect to that party.



Burton S. Kolko
Administrative Law Judge

Washington, D.C.
July 25, 1995